

BULLETIN NUMBER: **INS-06-010**

TITLE: **PLACEMENT OF RISKS WITH UNAUTHORIZED INSURERS**

LEGISLATION: **SECTION 76 OF THE *FINANCIAL INSTITUTIONS ACT***

DATE: **OCTOBER 2006**

PURPOSE

The purpose of this bulletin is to clarify the position of the Superintendent of Financial Institutions ("Superintendent") with respect to the placement of risks with unauthorized insurance companies.

BACKGROUND

Periodically, it comes to the attention of the Superintendent that agent licensees are placing business with insurers not authorized to do business in this province.

The purpose of this bulletin is to remind agent licensees that unauthorized insurers are prohibited from conducting insurance business in the province and that agent licensees are not permitted to place risks with unauthorized insurers except as permitted under section 76 of the *Financial Institutions Act* ("FIA").

The remainder of this bulletin sets out the circumstances under which the legislation permits an agent licensee to place a risk with an unauthorized insurer and expectations for compliance with those requirements.

DISCUSSION

Under section 76, agent licensees may place a risk with an unauthorized insurer if:

- (i) The agent has not directly or indirectly solicited the client for the placement of the risk; and
- (ii) The agent has been authorized by the client to place the insurance with an unauthorized insurer.

The Superintendent believes that this section is not meant to be used by agents or insurers to circumvent the licensing requirements and consumer protections built into the legislation. Agent licensees have both a legislative responsibility and a duty of care to their clients to only use appropriately authorized insurers to insure risks in this province. (For a list of authorized insurers visit our website at <http://www.fic.gov.bc.ca/>).

Section 76 is only intended to cover situations where:

- A client has on their own pre-selected an unauthorized insurer and subsequently approaches an agent licensee and specifically requests assistance in placing the risk with that insurer; or
- The client of their own accord and initiative and without having been solicited by the agent specifically directs a licensee to seek placement of the clients risk with an unauthorized insurer.

When an agent licensee finds that they have been directed by a client to seek placement of a risk with an unauthorized insurer, the agent still has a duty of care to the client to use due diligence in selecting an insurer that can reasonably be expected not to place the client unduly at risk. Further, the agent licensee is expected to provide disclosure to the client about the risks of using an unauthorized insurer.

As guidance to a licensee in conducting due diligence on whether to place business with a particular unauthorized insurer, the agent may wish to consider the principal factors that this office looks at in assessing whether it will take regulatory action with respect to the placement of a risk with an unauthorized insurer.

Where the coverage is mandatory, (i.e., for licensing or some other requirement), and the only form acceptable would be coverage provided by an authorized insurer, staff of the Financial Institutions Commission ("FICOM") believe the agent licensee should refrain from placing coverage with an unauthorized insurer even if instructed to do so by the client.

FACTORS

1. Why wasn't the risk placed with an insurer authorized in the province?

In investigating the use of an unauthorized insurer, agent licensees can expect to be asked to demonstrate that they could not locate an authorized market willing to quote on the risk or to demonstrate that there was a compelling coverage reason why a quote from an authorized insurer was not accepted before they turned to the unauthorized market. Where an agent licensee finds their markets are not willing to quote on a risk then the Superintendent expects the licensee to seek the assistance of the industry trade organizations and other agent licensees to help place the risk with an authorized insurer.

2. Was the client solicited to be placed with an unauthorized insurer?

Agent licensees are prohibited by section 76 of the FIA from soliciting the placement of risks with unauthorized insurers. Accordingly, where an agent licensee finds they are unable to place a risk with an authorized insurer they must refrain from soliciting the client for permission to seek to place the risk with an unauthorized insurer. Soliciting includes promoting, inferring or otherwise suggesting or holding out to the client that the risk might be insured by an unauthorized insurer.

3. Did the client authorize the agent licensee to use an unauthorized insurer?

The client must, of their own accord, initiate the authority given to procure the coverage without being solicited or encouraged to provide such consent.

FICOM staff do not believe that general instruction is sufficient. Examples of general instruction are: "Can you find coverage elsewhere?" "Do you know of someone else that might insure me?" Such instructions can infer that the client still expects the coverage to be provided by an authorized insurer. The instructions must be specific enough that there can be no ambiguity that the client intends that the agent licensee seek placement of the coverage with an unauthorized insurer.

4. Did the agent licensee provide adequate disclosure of the risks involved in taking out coverage with an unauthorized insurer?

FICOM staff expect that clients will be provided with adequate disclosure so they can appreciate the risks of having the coverage provided by an unauthorized insurer.

5. Is there an ongoing business relationship between the agent licensee and the unauthorized insurer?

Agent licensees are not permitted to establish an ongoing business relationship with an unauthorized insurer, either directly, or through other agents to place risks with the insurer on an ongoing basis, including entering into any formal or tacit agreement for the placement of risks.

Placement of risk under section 76 is expected to be on a "one-off" basis. Agent licensees are expected to do due diligence on the unauthorized insurer at the time of placement of the risk before approaching that insurer to determine if the insurer would be willing to accept the risk. As well, the agent licensee has a duty to advise the client as to the appropriateness of the insurance. Once the business is placed, the unauthorized insurer cannot hold out to either the agent licensee or the client that it is willing to renew the risk and the agent licensee cannot renew the risk with the unauthorized insurer without first determining that they are unable to place it in the authorized market and without being directed to do so (unsolicited) by the client.

Where FICOM staff find evidence that an agent licensee is placing risks on an ongoing basis with an unauthorized insurer, staff will likely recommend enforcement action to stop that activity.

6. If the insurer is not authorized in British Columbia, is it incorporated or continued in a jurisdiction (the “home” jurisdiction) that has a strong regulatory framework?

There is a presumption that clients are put at undue risk if they are placed with an insurer that originates from a jurisdiction that does not regulate insurers under a strong regulatory framework. At the minimum staff of this office would expect that the home jurisdiction require that the insurer:

- Be licensed with the home jurisdiction's insurance regulator (and that regulator is charged with maintaining an effective, fair, safe, and stable insurance market in the home jurisdiction);
- Have at all times adequate ongoing capital;
- Be solvent and expected to remain solvent;
- Adhere to standards set for the quality of assets, liabilities, reserves and reinsurance;
- Maintain valid financial statements prepared in accordance with generally accepted standards that are subject to independent financial audits;
- Maintain reserves established by regular actuarial reviews by accredited actuaries using acceptable standards;
- Be subject to ongoing scrutiny by the home regulator, including audits, examinations and inspections that allow that regulator to get the information needed to properly form an opinion on the financial strength of the insurer;
- Operate at all times in compliance with the legislative requirements and market conduct regulations in any jurisdiction in which it does business and exercise the necessary knowledge, skills, and integrity in dealing with its customers;
- Comply with standards for corporate governance, including standards for ownership and control of the insurer; and
- Have a board of directors that is acceptable to the home regulator and that is required to provide suitable prudential oversight of the insurer.

The regulatory regime should ensure that the regulator not only regulates the insurer for the business it does in its home jurisdiction but also the business it does outside its home jurisdiction. FICOM staff will look at whether the jurisdiction observes, in both law and in practice, the core principles of insurance supervision that are promoted by the International Association of Insurance Supervisors in considering whether a jurisdiction has a strong regulatory framework.

7. Is the unauthorized insurer currently financially solvent and expected to remain solvent?

Agent licensees should not use any unauthorized insurer that they do not have reason to believe is solvent. Solvency includes adequacy and quality of capital and liquidity and having control over financial assets. FICOM staff will look to whether the insurer would meet Canadian standards for solvency.

8. Are there sufficient assets accessible by a court of law in British Columbia to cover the expected obligation?
9. Can the unauthorized insurer be expected to handle claims and disputes fairly?
10. Will the unauthorized insurer appear in court in British Columbia and not use jurisdictional defences or have clients sign unfair contracts or waivers? Has the insurer undertaken to have a power of attorney designated in this province for acceptance of service or suit?

Generally, it can be expected that if the insurer is authorized elsewhere in Canada, but not in British Columbia, it would be more likely to appear in court in British Columbia and satisfy any action imposed by the courts.

11. If FICOM staff have to approach the primary regulator of the unauthorized insurer for assistance in enforcing compliance or for cooperation, can we expect that jurisdiction to be amenable to the approach?
12. Is there reason to believe that the unauthorized insurer has operated in any other jurisdiction in a manner that has been, or can reasonably be expected to be, prejudicial to the interests of insureds or in contravention of that jurisdiction's legislative framework? Guidance will be taken from section 165(2)(b) of the FIA.

OTHER REQUIREMENTS OF SECTION 76

- **Maintaining Records:**

Agent licensees are required under section 76 to maintain records of the particulars of any contract placed with an unauthorized insurer and must produce those records to this office or to the Commissioner of Income Tax on request.

- **Payment of Premium Tax:**

An insured who takes out a contract of insurance with an unauthorized insurer is required to pay the insurance premium tax on that contract. There are also federal taxes which may be payable. Contact the Commissioner of Income Tax for more information.

- **Adjustment of Claims:**

Unauthorized insurers are not permitted to inspect, appraise or adjust any loss on an insurance contract in this province unless:

- The contract was placed in accordance with section 76;
- The premium tax has been paid; and
- The unauthorized insurer has sought and received written consent from the Superintendent to adjust, inspect or appraise the loss.

In seeking the consent of the Superintendent, the unauthorized insurer should be aware that the Superintendent will typically require that the insurer:

- Provide an undertaking to the Superintendent that it will appear in court in the province with respect to the claim;
- Agree to honour any order imposed by the court system;
- Appoint an attorney in the province to accept service; and
- Use an adjuster that is appropriately licensed with the Insurance Council of British Columbia to appraise, inspect or adjust the claim.

The Superintendent may also require the insurer to establish sufficient assets in Canada for settlement of the claim. (It should be noted that agent licensee's who place risks with unauthorized insurers should not be holding back premiums to use to settle any claim on the policy. Nor should they be adjusting or otherwise assisting in the determination of the amount of any loss on a policy placed with an unauthorized insurer as this would constitute unauthorized insurance business on the part of the agent.).

CONCLUSION

Where FICOM staff obtain evidence that an unlicensed agent or unauthorized insurer is actively attempting to establish an ongoing business relationship with an agent licensee for the purpose of insuring risks in this province, or where this office receives a complaint about business placed with an unauthorized insurer, staff will investigate to determine if enforcement action should be taken.

Accordingly, whenever an agent places a British Columbia risk with an unauthorized insurer or otherwise uses an unauthorized insurer in dealing with a British Columbia resident, the agent should be able to demonstrate that the business was placed in observance of the legislative requirements stipulated under section 76. The agent should also be able to show that he/she did adequate due diligence to determine that the insured wouldn't be placed at unreasonable risk by insuring with that insurer and that the agent provided adequate advice and disclosure to the client.

At the Financial Institutions Commission, we issue interpretation bulletins to provide technical interpretations and positions regarding certain provisions contained in the *Financial Institutions Act* and Regulations. While the comments in a particular part of an interpretation bulletin may relate to provisions of the law in force at the time they were made, these comments are not a substitute for the law. The reader should consider the comments in light of the relevant provisions of the law in force at the time, taking into account the effect of any relevant amendments to those provisions or relevant court decisions occurring after the date on which the comments were made. Subject to the above, an interpretation or position contained in an interpretation bulletin generally applies as of the date on which it was published, unless otherwise specified.

If you have any questions with respect to the contents of this Information Bulletin, please contact:

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APPENDIX 1

Exceptions

76 (1) Despite section 75,

(a) any person may require insurance to be placed by a borrower as security for a loan,

(b) any person may

(i) adjust a loss,

(ii) prosecute or maintain a writ, action or proceeding, or

(iii) perform an obligation

under or arising out of a contract of insurance that was made or issued in British Columbia at a time when the person was authorized to carry on insurance business, and

(c) an insurance agent licensed under Division 2 of Part 6 who

(i) does not, directly or indirectly, solicit the resident for the insurance contract, and

(ii) is authorized by the resident to effect the insurance contract, may negotiate or procure an insurance contract between a resident of British Columbia and an insurer prohibited by section 75 from carrying on business in British Columbia.

(2) An insurance agent licensed under Division 2 of Part 6 who, under subsection (1) (c), procures or negotiates a contract of insurance must keep a record showing the particulars of the contract and at the request of the Commissioner of Income Tax or of the commission, must provide the record to the Commissioner of Income Tax or commission as requested.

(3) If

(a) the sum imposed by way of tax under section 4 of the *Insurance Premium Tax Act* in respect of an insurance contract lawfully made under subsection (1) (c) has been paid,

(b) the insurer described in subsection (1) (c) has notified the commission that it proposes to make an inspection for the purpose of the insurance contract or to adjust or appraise a loss under the contract, and

(c) the commission has given written approval to the proposed activity by the insurer,

the insurer may make the inspection or adjust and appraise the loss.

(4) The approval referred to in subsection (3) (c) is valid for all necessary inspections, adjustment and appraisals during the period specified in the approval.

(5) The commission may suspend, cancel or refuse to issue an approval referred to in subsection (3) (c) if an insurer contravenes a provision of this Act.