

# Report on the Application of the Act respecting the distribution of financial products and services

MAY 2015

Québec 

# Report on the Application of the Act respecting the distribution of financial products and services

MAY 2015



This document is printed on completely recycled paper, made in Québec, containing 100% post-consumer fibre and produced without elemental chlorine.

Report on the Application of the Act respecting the distribution  
of financial products and services

Legal deposit – May 2015  
Bibliothèque et Archives nationales du Québec  
ISBN 978-2-550-73201-3 (Print)  
ISBN 978-2-550-73202-0 (PDF)

© Gouvernement du Québec, 2015

*Jacques Chagnon  
Speaker of the National Assembly of Québec  
Parliament Building  
Québec (Québec) G1A 1A4*

*Dear Sir,*

*Pursuant to section 580 of the Act respecting the distribution of financial products and services (CQLR, chapter D-9.2), I am pleased to send you my report on the application of this Act, for tabling in the National Assembly.*

*Yours truly,*

A handwritten signature in black ink, appearing to read 'Carlos Leitão', with a stylized, cursive script.

*Carlos Leitão  
Minister of Finance  
May 2015*



---

## MESSAGE FROM THE MINISTER

*The financial industry is of vital importance to the Québec economy. It accounts for nearly 5% of total employment in Québec and the wages and profits that it generates account for nearly 7% of Québec's GDP. Moreover, it heightens the financial security of Quebecers by protecting their assets. The financial sector is thus contributing significantly to growth in the Québec economy and the betterment of its population.*

*For this reason, it is important to ensure that oversight of stakeholders in the industry is adequate in order to maintain public trust in financial product and service offerings and to constantly update such offerings to reflect changing markets.*

*The Act respecting the distribution of financial products and services (ARDFPS) plays an essential role in this respect. It mainly governs individuals authorized to distribute certain products and services in the financial sector, i.e. personal insurance, general insurance, claims adjustment, and financial planning. The regulations adopted pursuant to the Act also structure the professional code of ethics of mutual fund dealer representatives and scholarship plan dealer representatives. They also regulate the operations of insurers when they distribute specific products without resorting to the services of representatives.*

*The environment in which stakeholders in the financial sector have developed has changed significantly since the adoption 15 years ago of the ARDFPS. For example, it is now possible to buy almost everything online and information has never been so accessible and abundant. This new world poses new challenges that legislators could not anticipate in 1998.*

*The past 15 years of experience have enabled us to pinpoint enforcement problems. The harmonization of the mutual fund dealership sector, the compensation of the consumers of financial products and services and distribution without a representative are key topics that demand thorough reflection in order to update oversight of this segment of the financial sector. The Autorité des marchés financiers has already conducted public consultations on these questions. This report takes stock of the consultations.*

*Oversight of the distribution of financial products and services must enable the industry to adapt to current conditions and be sufficiently flexible to facilitate its ongoing development. The ARDFPS should only impose the minimum regulatory burden necessary to maintain adequate safeguards for individual investors in order to allow the efficient operation of the vital financial services industry.*

*This report is meant to be a diagnostic tool and a tool for collective reflection to enhance the current legal framework by ensuring Quebecers access to financial products and services and the advice that they need, while enabling*

---

*all industry players to benefit from it. I therefore encourage the industry and anyone interested to comment on the proposals presented in this report and to respond to the questions that the report raises.*

A handwritten signature in black ink, appearing to read 'Leitão', with a stylized, cursive script.

**Carlos Leitão**  
**Minister of Finance**

---

## TABLE OF CONTENTS

<b>INTRODUCTION.....</b>	<b>1</b>
The purpose of this report .....	1
 <b>CHAPTER 1 .....</b>	 <b>3</b>
<b>Description of the oversight of the distribution of certain financial products with or without a representative .....</b>	 <b>3</b>
<b>Context.....</b>	<b>3</b>
Overview of the industry .....	3
Objectives of the <i>Act respecting the distribution of financial products and services</i> .....	5
Changes in the legislation since 1998 .....	6
The Act respecting the Agence nationale d'encadrement du secteur financier (S.Q. 2002, chapter 45).....	6
The Act to amend the Securities Act and other legislative provisions (S.Q. 2004, chapter 37) .....	7
The Act to amend the Securities Act and other legislative provisions (S.Q. 2006, chapter 50) .....	7
The Act to amend the Securities Act and other legislative provisions (S.Q. 2007, chapter 15) .....	8
The Act to amend the Securities Act and other legislative provisions (S.Q. 2008, chapter 7) .....	8
The Real Estate Brokerage Act (S.Q. 2008, chapter 9).....	8
The Act to amend the Securities Act and other legislative provisions (S.Q. 2009, chapter 25) .....	8
The Act to amend various legislative provisions principally to tighten the regulation of the financial sector (S.Q. 2009, chapter 58).....	9
The Act to amend various legislative provisions mainly concerning the financial sector (S.Q. 2011, chapter 26).....	9
The Act to amend various legislative provisions mainly concerning the financial sector (S.Q. 2013, chapter 18).....	9
The Canadian context .....	10
Summary .....	10

---



<b>CHAPTER 2.....</b>	<b>13</b>
<b>Trends in the realm of distribution .....</b>	<b>13</b>
Consultations conducted by the Autorité des marchés financiers ..	13
Online distribution of insurance .....	13
Distribution without a representative.....	15
 <b>CHAPTER 3.....</b>	 <b>19</b>
<b>Oversight of the representative .....</b>	<b>19</b>
Special cases .....	21
Mutual fund and scholarship plan representatives .....	21
Employees of insurers .....	23
Claims adjusters employed by an insurer.....	24
Independent representatives.....	25
 <b>CHAPTER 4.....</b>	 <b>27</b>
<b>Compensation in the event of fraud .....</b>	<b>27</b>
 <b>CONCLUSION .....</b>	 <b>31</b>
 <b>APPENDIX 1 .....</b>	 <b>33</b>
Summary of the recommendations.....	33
 <b>APPENDIX 2.....</b>	 <b>35</b>
Summary of the consultation questions.....	35

---

## INTRODUCTION

The public can acquire financial products and services in different ways, each of which has advantages and drawbacks. The public has always relied on representatives to acquire many products, in particular complex products such as securities or certain types of insurance, but also in cases where it is difficult to ascertain needs. The advice that representatives offer is an unquestionable advantage, a very valuable calling card.

In order to preserve the added value that the representative's contribution represents in the acquisition of a financial product and, accordingly, enhance the attraction for the public of this method of acquisition, the industry has displayed receptiveness to the rigorous oversight of representatives.

The Act respecting the distribution of financial products and services (CQLR, chapter D-9.2) (ARDFPS) mainly governs individuals and firms authorized to distribute certain products and services in the financial sector in the realms of insurance of persons, damage insurance, claims adjustment and financial planning. The regulations adopted pursuant to the Act also structure the professional code of ethics of mutual fund dealer representatives and scholarship plan dealer representatives. They also govern the supply of certain insurance products pertaining to goods that distributors sell, as an accessory, in conjunction with the sale of such goods. The Autorité des marchés financiers (the Authority) is responsible for its administration.

A representative who wishes to distribute such products and services in Québec must first obtain a certificate from the Authority authorizing him to practice in the appropriate discipline(s). In the same way, firms must register with the Authority.

### **The purpose of this report**

The *Report on the Application of the ARDFPS* seeks to ascertain to what extent this act continues to satisfy the needs of the public and the distribution industry and to propose enhancements, if need be.

---

The report has four chapters.

Chapter 1 presents the current context and historical background and describes the oversight of the distribution of financial products and services by the ARDFPS.

Chapter 2 examines trends in the realm of distribution and the attendant consultations that the Autorité des marchés financiers conducted.

Chapter 3 examines the oversight imposed on representatives in Québec and identifies possible solutions for optimizing and simplifying it. .

Chapter 4 focuses on Québec's compensation mechanism in the event of fraud.

An appendix presents summaries of the recommendations and the consultation questions.

---

## CHAPTER 1

### DESCRIPTION OF THE OVERSIGHT OF THE DISTRIBUTION OF CERTAIN FINANCIAL PRODUCTS WITH OR WITHOUT A REPRESENTATIVE

#### CONTEXT

##### Overview of the industry

The financial industry is of vital importance to the Québec economy. It accounts for nearly 5% of overall employment in Québec.<sup>1</sup> In addition, the salaries and profits that it generates account for nearly 7% of Québec's GDP.<sup>2</sup> Beyond its direct contribution to the economy, it plays a number of important roles. The industry makes available to Québec businesses the funds necessary to finance their growth. What is more, it enables Quebecers to save and thereby enhance their financial security. It also allows them to protect their assets and income against unforeseen events. The financial sector is thus contributing significantly to growth in the Québec economy and the betterment of its population.

In order to fully assess the impact of the measures to be proposed, the profile of the segment of the industry that the Act respecting the distribution of financial products and services (ARDFPS) covers according to the number of professionals and firms in each sector is presented on the following page. It should be noted that a number of representatives work in more than one sector.

---

<sup>1</sup> Institut de la statistique du Québec, *Emploi salarié et rémunération de l'industrie des services financiers, Canada et provinces – Édition 2014*, May 2014, p. 19.

<sup>2</sup> Institut de la statistique du Québec, *PIB et indice de concentration géographique de l'industrie des services financiers, Canada et provinces, données provisoires 2013*, June 2014, p. 20.

---

**TABLE 1****OVERVIEW OF THE INDUSTRY**

AS OF SEPTEMBER 5, 2014

Intermediary	Number of representatives	Number – firms and insurers
<b>Representatives attached to a firm</b>		
Representatives in insurance of persons	6 589	2 813
Group insurance representatives	2 982	1 569
Damage insurance brokers	6 536	885
Financial planners attached to a firm	4 058	745
Mutual fund dealer representatives	23 356	78
Scholarship plan dealer representatives	585	12
Claims adjusters attached to an independent firm	745	127
<b>Representatives attached to an insurer registered as a firm</b>		
Representatives in insurance of persons	3 414	23
Group insurance representatives	763	16
Damage insurance agents	4 603	62
Claims adjusters attached to an insurer	2 185	65
<b>Independent representatives</b>		
Representatives in insurance of persons	2 748	NA
Group insurance representatives	750	NA
Damage insurance brokers	99	NA
Independent financial planners	368	NA
Independent claims adjusters	12	NA
<b>Distribution without a representative</b>		
Distributors	NA	5 736 (distributors)

Source: Autorité des marchés financiers, September 2014.

### **Objectives of the *Act respecting the distribution of financial products and services***

The ARDFPS was adopted in 1998. As Bernard Landry noted when Bill 188 was adopted in principle, its main objective was to modernize and broaden provisions respecting consumer protection. The ARDFPS was to establish a new, modern, fair competitive framework to ensure the supply of diversified financial products and services. It sought to simplify the regulatory framework and to impose only a strictly necessary burden to allow for the efficient operation of the financial services industry and, in particular, the insurance sector.

Moreover, in keeping with a worldwide trend at that time, another objective of the Act was to complete decompartmentalization by allowing deposit-taking institutions to sell insurance.

The ARDFPS replaced the Act respecting market intermediaries and partly the Securities Act (CQLR, chapter, chapter V-1.1) to oversee persons authorized to distribute insurance products, certain securities products (scholarship plans, investment contracts, mutual fund units) and to exercise the professions of financial planner and claims adjuster.

The Bureau des services financiers, whose board of directors mainly comprised industry representatives, was established at the same time to act as a regulatory and oversight body. It also acted as a public information centre and as an outlet for the submission of complaints. It has since been integrated into the Autorité des marchés financiers.

The ARDFPS established the Chambre de la sécurité financière (CSF) and the Chambre de l'assurance de dommages (ChAD). The chambers determine the professional codes of ethics applicable to representatives who are members of the chambers. Except in the case of financial planners, the chambers also determine the rules governing the professional development of their members. Furthermore, a discipline committee has been established in each of the chambers. It handles all complaints formulated in respect of a representative for breaches of the rules of professional conduct. The provisions governing the chambers are based on the Professional Code.

The ARDFPS introduces the notion and the concept of the firm and the independent representative. All legal persons must register as firms in order to distribute through representatives the financial products and services that their representatives are authorized to offer. The representatives may also register as independent representatives if they are not attached to a firm. The firms and the representatives may be multidisciplinary, i.e. be authorized to practice more than one sector governed by the ARDFPS, i.e. insurance of persons, group insurance, damage insurance, claims adjustment and financial planning.

The Act is noteworthy, in relation to the regulations in the other Canadian provinces, in that it imposes on representatives of the financial sector, except the representatives of securities dealers, oversight based on the model of the professional corporations with chambers that ensure compliance with the rules of professional conduct and the rules governing professional development.

The Act also regulates distribution without a representative. Under this system, a distributor, within the framework of its operations that are not in the insurance field, may offer, as an accessory, on behalf of an insurer insurance coverage pertaining to goods that it sells.

The Act has also established the Fonds d'indemnisation des services financiers (FISF), which grouped together in 1999 the three compensation funds then in force in insurance of persons, damage insurance and financial planning.

### **Changes in the legislation since 1998**

Since it was assented to in 1998, the ARDFPS has been amended several times: in December 2002 (2002, chapter 45), in December 2004 (2004, chapter 37), in December 2006 (2006, chapter 50), in November 2007 (2007, chapter 15), in May 2008 (2008, chapter 7, and 2008, chapter 9), in June 2009 (2009, chapter 25) (2009, chapter 58), in November 2011 (2011, chapter 26) and in June 2013 (2013, chapter 18).

### **The Act respecting the Agence nationale d'encadrement du secteur financier (S.Q. 2002, chapter 45)**

The most important reform of the Québec financial sector since the ARDFPS was assented to was carried out in the wake of the tabling of the report of the Québec Task Force on Financial Sector Regulation, entitled *A Streamlined Regulatory Structure for Québec's Financial Sector* (the Martineau report). The task force, whose seven members are active and recognized in the Québec financial industry, had a mandate to analyze the regulation of the Québec financial sector and make recommendations aimed at enhancing the sector.

The task force concluded that the oversight framework at the time was too complex, consumers had trouble grasping it, the administrative burden was excessive, and registrants complained about it. In response to the task force's report, the government decided to simplify the structure by assembling in a single body most facets of regulation of the financial sector, although it preserved the two chambers.

On December 11, 2002, the Act respecting the Agence nationale d'encadrement du secteur financier was assented to. It established a single regulatory body intended to administer all of the legislation governing the regulation of the financial sector in the realms of insurance, securities, deposit-taking institutions, and the distribution of financial products and services. The Agence replaced the Bureau des services financiers, the Commission des valeurs mobilières du Québec, the Inspector General of Financial Institutions and the Régie de l'assurance-dépôts du Québec, and assumed the management of the Fonds d'indemnisation des services financiers.

In the distribution sector, the establishment of the Agence, which was renamed the Autorité des marchés financiers shortly thereafter, led to a transition from regulation by a body run primarily by industry representatives, to government oversight.

The Act established a harmonized complaint handling system and a dispute-resolution process. Accordingly, each supplier of financial products and services has, since then, had to adopt a policy concerning the handling of complaints and claims and the settlement of disputes. What is more, the Act has added in the ARDFPS an obligation for an insurance representative to consider the client's specific needs when insurance is supplied.

### **The Act to amend the Securities Act and other legislative provisions (S.Q. 2004, chapter 37)**

On December 17, 2004, the Act to amend the Securities Act and other legislative provisions was assented to. The Act introduced changes in particular to the governance of the two chambers. In addition, the Agence nationale d'encadrement du secteur financier changed names, becoming the Autorité des marchés financiers (the Authority).

### **The Act to amend the Securities Act and other legislative provisions (S.Q. 2006, chapter 50)**

Bill 29, assented to on December 14, 2006, empowers the Authority to accompany with restrictions or conditions the registration of a representative or a firm in a securities sector.



### **The Act to amend the Securities Act and other legislative provisions (S.Q. 2007, chapter 15)**

Bill 19, assented to on November 9, 2007, empowers the Authority to suspend the certificate of a representative who fails to abide by his obligation to engage in ongoing training.

### **The Act to amend the Securities Act and other legislative provisions (S.Q. 2008, chapter 7)**

Bill 64, assented to on May 28, 2008, harmonizes the penalty scheme with that of other financial sector legislation, thereby making it more stringent, in particular as regards fines, administrative penalties and the limitation periods. The Authority obtained the power to determine through regulation the amounts of penalties and the conditions governing their imposition for failure to fulfil an obligation to file a document. Moreover, the bill made provision for the establishment of a compensation committee in the Authority. The committee, comprising three members appointed by the Minister, would have been responsible for ruling on the eligibility of claims submitted to the Fonds d'indemnisation des services financiers (FISF) and determining the amount of the compensation to be paid, in accordance with the regulation. The provisions concerning the committee were adopted but were never put into force.

### **The Real Estate Brokerage Act (S.Q. 2008, chapter 9)**

Bill 73, assented to on May 28, 2008, established new rules on the regulation of mortgage brokerage dealings, thereby abrogating the provisions concerning mortgage brokerage for which provision was made in the ARDFPS, but that were not in force.

### **The Act to amend the Securities Act and other legislative provisions (S.Q. 2009, chapter 25)**

Bill 8, assented to on June 17, 2009, transferred to the *Securities Act* the regulation of securities sectors previously covered by the ARDFPS to enhance the harmonization of Québec's regulation with that of the other Canadian provinces and territories. However, complete harmonization is hard to achieve insofar as the Act stipulates that the provisions concerning the FISF and the CSF continue to apply. Mutual fund dealer representatives and scholarship plan dealer representatives are still members of the CSF although they are subject to the Securities Act.

Among the other legal provisions, the Authority was empowered to determine by regulation the other circumstances under which a client may rescind an insurance contract or an annuity contract established by an insurer and any purchase of such contract, or the circumstances under which a client may cancel such a contract or purchase and the conditions and terms of the annulment or the cancellation.

**The Act to amend various legislative provisions principally to tighten the regulation of the financial sector (S.Q. 2009, chapter 58)**

Bill 74, assented to on December 4, 2009, gave jurisdiction to the Bureau de décision et de révision (BDR) as regards the ARDFPS. Furthermore, it amended certain provisions in the ARDFPS pertaining to distribution without a representative and harmonized the offence system in the Act with that stipulated in the Securities Act and the Derivatives Act (CQLR, chapter I-14.01). The administrative penalties and fines that may be levied pursuant to the statutes have been increased.

**The Act to amend various legislative provisions mainly concerning the financial sector (S.Q. 2011, chapter 26)**

Bill 7, adopted on November 30, 2011, allowed the chambers to ask the BDR to penalize a firm for a breach of the legislation. Similarly, the bill empowered the Authority to ask the BDR to penalize a representative. What is more, the bill accorded new order-making power to the BDR. As for the decisions of the disciplinary committee of a chamber, the bill stipulates that an appeal may only be lodged once a decision has been handed down on the penalty and not at the time of the decision concerning guilt. It also amended certain provisions concerning the governance of the chambers.

**The Act to amend various legislative provisions mainly concerning the financial sector (S.Q. 2013, chapter 18)**

Bill 31, assented to on June 14, 2013, enhances the governance of the CSF by increasing the number of independent directors. It also empowers the Authority to take the necessary steps to ensure that the professional liability insurance policies of the representatives cover gross negligence in order to better protect consumers.

## The Canadian context

There is no statute in the rest of Canada equivalent to the ARDFPS since sectoral legislation usually governs the distribution of the products that it regulates. The only legislation that might be similar to the Act is the *Insurance Brokers Act* in Ontario that directly covers distribution but only for damage insurance brokers.

In the realm of securities, the other provinces have opted for a system of self-regulatory organizations (SRO). An SRO is a cluster of stakeholders in an industry that monitors all of its members by adopting rules governing conduct, ethics and commercial practices and by implementing control, monitoring and surveillance systems in order to maximize consumer trust in the industry.

The Investment Industry Regulatory Organization of Canada (IIROC) is the self-regulatory organization recognized by all of the provinces and territories. It oversees investment brokers and all of the operations conducted on stock exchanges and debt securities markets in Canada, including Québec.

In the realm of mutual fund dealing, the Mutual Fund Dealers Association of Canada (MFDA) is the SRO recognized in Canada, except in Québec.

There is no Canadian SRO for distributors in the insurance sector. However, in Ontario, it is the Registered Insurance Brokers of Ontario (RIBO) that acts as the self-regulatory organization for damage insurance brokers.

It is noteworthy that only in Québec are financial planners regulated by legislation. Elsewhere in Canada, the Financial Planners Standards Council (FPSC), a non-profit organization, offers Certified Financial Planner (CFP) accreditation to individuals who have taken the training program, passed the examinations, acquired the requisite experience, adhered to the code of ethics and engaged in ongoing training.

In the other provinces, claims adjusters must be certified but are regulated by the same statute as insurers. The degree of a claims adjuster's personal liability depends on the provincial statute that regulates the adjuster. The *Alberta Insurance Act*<sup>3</sup> goes so far as to stipulate that an illegal act committed by a claims adjuster employed by an insurance company is deemed to have been perpetrated by the insurer.

## Summary

The ARDFPS has responded well to the industry's and the public's needs. In particular, it has helped to sustain consumer confidence in the industry

---

<sup>3</sup> Insurance Act (chapter I-3), Alberta.

despite the fraud cases that have occurred over the past decade. The industry is efficient and competitive. On the other hand, the current system is beginning to show signs of losing impetus and no longer adequately satisfies the needs engendered principally by the new technologies. If nothing is done, the regulatory framework risks becoming inadequate and outmoded. Both the industry and the public could suffer as a result. The time has, therefore, come to review it.

We will examine three themes in this report, i.e. trends in the realm of distribution and the consultations conducted by the Authority in this respect, the twofold oversight of representatives, and the compensation of consumers in the event of fraud.



---

## **CHAPTER 2**

### **TRENDS IN THE REALM OF DISTRIBUTION**

The public prefers to acquire financial products through a representative. The direct distribution of products through financial institutions is confined to simpler products such as deposits. This preference reflects the added value of the advice that representatives provide when the time comes to acquire “complex” products. Moreover, the representatives have ensured that they maintain their competitive advantage by enhancing requirements concerning training and ethics for the industry overall.

However, more and more people acquire financial products online. The availability of information and the convenience of online acquisition no doubt explain the growing appeal of this method.

#### **Consultations conducted by the Autorité des marchés financiers**

In recognition of the problems that technological innovation is creating for the financial sector and the numerous challenges in respect of regulatory adaptation that such innovation poses, the Autorité des marchés financiers (the Authority) has conducted public consultations concerning the online distribution of insurance and distribution without a representative.

#### **Online distribution of insurance**

Online shopping has experienced tremendous growth in recent years. Now the phenomenon is extending its reach to the distribution of financial products. Unfortunately, neither the Act respecting the distribution of financial products and services (ARDFPS) nor other legislation governing the financial sector deal specifically with this increasingly popular method of acquiring products. It is, therefore, time to examine the relevance of adapting legislation to this new reality.

The online distribution of consumer goods does not usually require specific provisions to protect consumers. The usual obligations respecting trade and competition are sufficient. What about the distribution of financial products and services? Must we impose a specific legal framework and if so, which one? Must we impose the placing online of certain information and specific document formats or let each supplier determine the contents of its site according to its assessment of what the public wants? Must we prohibit the distribution of certain overly “complex” products? Must we impose intervention by a certified representative or only require that the client be

---

afforded access to such a representative? Essentially, the question that arises is: can we allow the industry to engage in self-discipline and assume that it will satisfy consumers' needs or must we intervene and impose ways of doing business?

The Authority conducted a consultation on online insurance distribution from February 24 to May 24, 2012. At that time, in Canada the Canadian Council of Insurance Regulators (CCIR) published a report focusing on the same questions. *Electronic Commerce in Insurance Products* stems from the deliberations of a committee managed by the Authority. Although it broaches essentially the same topics, the Authority's consultation adjusts the contents to the specific components of Québec regulations.

The Electronic Commerce Committee of the CCIR received 25 proposals from industry organizations representing insurers, agents and brokers, and responses from insurers who responded in their own names. No consumer group expressed itself, although the opinions of such groups were sought.

Below are the CCIR's key recommendations stemming from the consultation.

- It is incumbent upon the consumer to select the product that he wishes to purchase and the manner in which he does so.
- It is incumbent upon online insurance suppliers to ensure that a consumer who purchases an insurance product makes an enlightened decision by providing him with the necessary information, in a comprehensive, timely manner. The supplier must give the consumer access to the appropriate advice and inform him of the importance of such advice.
- The information that enables the consumer to verify the service supplier's identity and ensure that the supplier is registered with the regulating authority must be permanently, readily, directly accessible on the websites of all suppliers that distribute insurance products online.
- The communication of information on the suppliers' websites must include all information that is important to decision-making and comply with all legal obligations.
- Before they conclude the contract, the suppliers should present to the consumer a summary of the information provided on the proposal form.
- The suppliers should offer the consumer a copy of the proposal and the contract in a format that can be reproduced and archived.
- It is incumbent upon the suppliers to use systems on which consumers can rely.
- In accordance with the applicable legislation, it is incumbent upon the suppliers to protect the consumers' personal information. Insurers should

establish secure, efficient systems to offer consumers the possibility of designating and changing beneficiaries by electronic means.

It is in the insurers' interests to properly select the products that they offer online to ensure that they are adapted to this distribution channel. They would have to assume the cost of a poorly adapted distribution method. Furthermore, the representative's advice would always be indicated for certain products and for consumers who prefer to rely on a professional. Insurers should be in a position to determine the method of distribution best suited to the different products that they offer. The regulations must, therefore, grant them sufficient flexibility.

In short, in order to distribute its products online, the industry must make this method of acquisition attractive to the public. What is more, certain requirements seem desirable and might underpin a flexible regulatory framework that would assign certain responsibilities to the product's distributor and afford the latter sufficient leeway to adapt the method of distribution to the clientele's needs.

### PROPOSAL 1

- Draw on the recommendations of the Canadian Council of Insurance Regulators to put in place a flexible legal framework that will enable insurers to offer their products online.

### Distribution without a representative

Distribution without a representative is a distribution regime described in Title VIII of the ARDFPS. Under the regime, an insurer may offer insurance products through a distributor who, in the context of his activities that are not in the field of insurance, offers, as an accessory, an insurance product that relates solely to goods sold by the person or secures a client's adhesion in respect of such an insurance product. The Act also identifies certain products that are deemed to qualify for this type of distribution: travel insurance, vehicle rental insurance, where the rental period is less than four months, credit card and debit card insurance, vehicle replacement insurance, debtor life, health and employment insurance, and investor life, health and employment insurance.

The Authority conducted a public consultation on distribution without a representative from November 26, 2010 to February 25, 2011. The consultation paper indicated the rules, provided a profile of the market and 14 recommendations, which responded to six questions identified by the Authority, on which interveners were asked to comment.



Six recommendations focused on the distribution guide. The Authority proposed in the recommendations the establishment of a guide template that includes all compulsory information. The information would be more or less the same as what the current regulations require but would be presented more clearly and in a language adapted to the public's general level of understanding. The guide would also be shorter and would not contain superfluous information that dilutes the information that is essential to enlightened decision-making by the client. The number of products offered by a single guide would be limited, the exclusions, limitations and restrictions would be highlighted, and the Authority would demand that the insurance confirmation be a separate element of the guide. The Authority also proposed facilitating access to the guides by making them available on its website.

Two recommendations proposed the extension of the contract cancellation period from 10 to 30 days. According to the Authority, this time limit would enable the consumer to review his purchasing decision and ascertain if a conventional product would better suit him. Against a backdrop of telemarketing, the consumer would have the time to receive documentation and consult it before the deadline expires.

Two recommendations were intended to make insurers responsible for compliance with the obligations of their distributors. Insurers should, therefore, adopt supervisory systems and confirm the coherence between the goods sold and the insurance product offered.

Three recommendations focused on distributors. The Authority proposed the development of a specific inspection program for distributors to ensure that they fulfil their obligations. It also wished to create a public registry to enable consumers to confirm that distributors are authorized to offer them products. Moreover, it wished to establish telemarketing call scripts to ensure their compliance with the requirements of distribution without a representative.

One recommendation proposed making it compulsory to disclose the remuneration clearly and in writing in all instances, instead of only when the remuneration exceeds 30% of the premium paid, as is the case now, in order to eliminate the avoidance tactics that certain distributors engage in.

The Authority received 18 briefs, in which opinions differ greatly. Stakeholders in distribution without a representative obviously advocate a less strict approach through guiding principles that would afford insurance suppliers greater leeway over the means of complying with regulations. The different groups of certified representatives want very strict oversight and would like to reduce to a minimum reliance on this distribution method.

One of the weaknesses of distribution without a representative is that it subjects to an array of rules persons who do not have any tie to the financial sector and who act as distributors only in a manner accessory to their main activity related to the product insured. While subjection to an array of rules is the norm in the financial sector, it is fairly uncommon in the other sectors, which engenders a number of practical difficulties.

Another significant weakness of distribution without a representative is that it makes a person shoulder most of the responsibility for distribution who is not necessarily able to assume such responsibility. Furthermore, the recommendation<sup>4</sup> of the Authority that makes insurers accountable for the fulfilment of their distributor's obligations stems directly from this problem and would have the effect of shifting responsibility for distribution to an entity that is able to better assume it.

---

<sup>4</sup> AUTORITÉ DES MARCHÉS FINANCIERS, *Document de réflexion et de consultation sur la distribution sans représentant*, November 2010, p. 11, Recommendation 7, Rendre les assureurs imputables du respect des obligations de leurs distributeurs :

“Given that distributors are not individuals who possess a certificate issued by the Autorité that authorizes them to act in the damage insurance or insurance of persons sector, that they are regulated neither by the Chambre de l'assurance de dommages nor by the Chambre de la sécurité financière, and that they offer insurance products on behalf of an insurer, the latter should be held more extensively accountable for the breaches of its distributors.

By making insurers accountable for the fulfilment of the obligations of their distributors, the insurers will be obliged to do what is necessary to ensure that their distributors conform to the legislation, in particular by establishing supervisory procedures.” [TRANSLATION]

One way to remedy the two shortcomings in the system could be to confirm the role of the distributors as mandataries of the insurer. The measure would make the insurer aware of its responsibilities and would make it possible to apply the regulations to the insurer instead of the distributor. Against this background, it would undoubtedly be possible to review overall oversight of distribution without a representative. The rules might resemble those governing online distribution. Accordingly, regardless of the method of distribution, consumers would have access to the same tools to make enlightened decisions.

### **PROPOSAL 2**

- Establish a legislative framework for distribution without a representative that applies directly to insurers, which must ensure that the mandataries (now called distributors) abide by the rules.

---

## CHAPTER 3

### OVERSIGHT OF THE REPRESENTATIVE

The industry's desire to raise the level of professionalism of representatives led to the adoption of a regulatory system comparable to that of professional corporations. This approach, which has its advantages, also created more responsibilities. Both the Autorité des marchés financiers (the Authority) and the chambers exercise regulatory powers over representatives. They also directly or indirectly exercise supervisory authority and authority to impose sanctions over representatives.

Indeed, the Act respecting the distribution of financial products and services (ARDFPS) regulates both the representative and his firm. In Québec, the representative is governed by a chamber according to a model that draws inspiration from the professional corporations and must abide by its code of professional conduct. Pursuant to such oversight, the representative is responsible for his acts, whether he is independent or an employee. The firm on whose behalf the representative acts also monitors the representative since pursuant to the ARDFPS the firm is responsible for the actions of the representatives attached to it.

Oversight of ethical conduct by a chamber thus offers the added advantage of extra protection for consumers under the distribution with a representative regime in Québec. This means that representatives are personally responsible for the services they provide to consumers. Where a representative acts on behalf of a firm, his personal responsibility is in addition to that of the firm.

While this approach has helped raise the level of professionalism of representatives in general, it is more cumbersome than the approaches adopted in the rest of Canada. It entails additional costs, whether in contributions or an increased administrative and regulatory burden.

Twofold oversight also spawns some degree of confusion, sometimes even a possible incoherence as regards the firm's and the representative's responsibility and each one's conduct. Indeed, since the firm is responsible for the actions of its representatives, it follows that it must be able to impose on them practices and policies. This can result in a situation in which the practices or policies contravene the firm's code of ethics.

The same confusion can exist from the standpoint of the responsibilities of oversight bodies. When the Authority inspects a firm, it must also consider the actions of the representatives through whom the firm acts and the firm's responsibility to the representative. Conversely, a chamber that investigates a representative must also look at the firm's conduct. It is difficult to apply dual oversight without creating confusion from the standpoint of each one's responsibility and monitoring of them. As will be seen later on, the potential

---

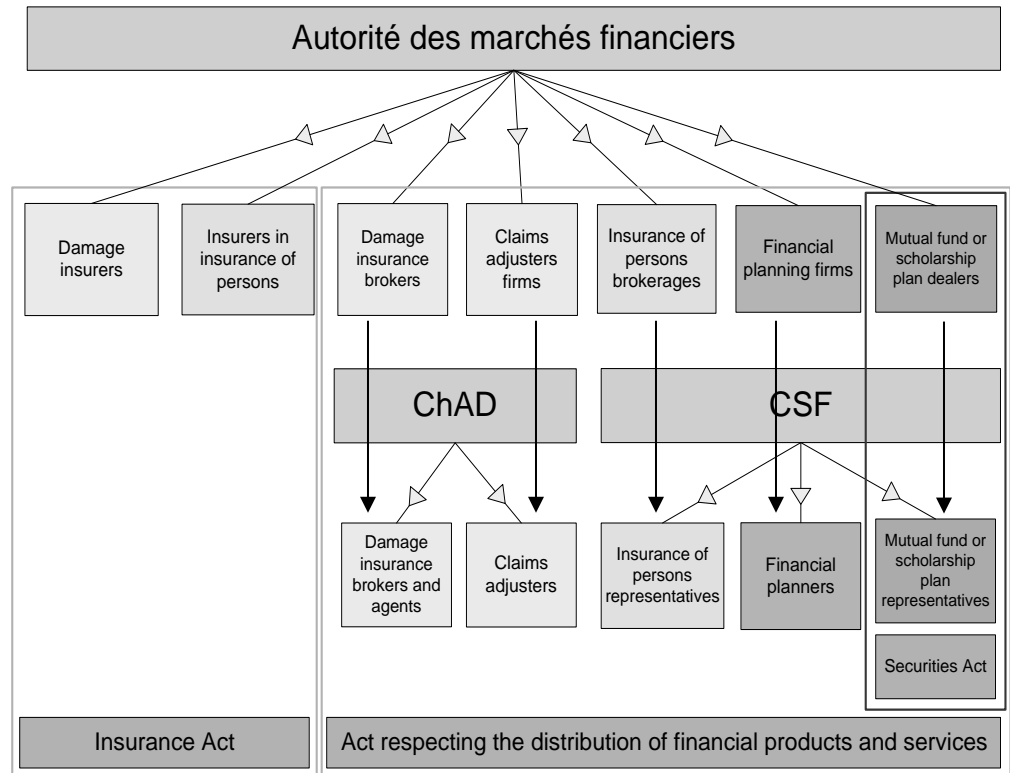
for conflict is even greater when the firm is a financial institution that otherwise has obligations toward its clients to engage in sound commercial practices.

This twofold oversight structure raises several issues:

- a heavier regulatory and pecuniary burden for industry participants;
- duplications in the fields of jurisdiction of regulatory bodies;
- the obligation for financial institutions, and firms, to deal with several oversight bodies;
- a degree of confusion among consumers about the role of each regulatory entity;
- difficulty finalizing harmonization of the group savings plan brokerage sector with the rest of Canada.

### **PROPOSAL 3**

- Examine all approaches to ease the regulatory and financial burden of registrants, while maintaining adequate oversight of the distribution of financial products and services.

**ILLUSTRATION 1****CURRENT OVERSIGHT STRUCTURE****Questions**

- A. In your view, do the advantages of twofold oversight outweigh the costs engendered?
- B. If not, what type of oversight do you propose?

**Special cases**

The advantages and disadvantages of the twofold oversight structure vary with the sector concerned, and are discussed in this chapter.

***Mutual fund and scholarship plan representatives***

An ongoing effort has been made for a number of years to harmonize the securities field, in response to the desire of provincial and territorial governments to minimize the difficulties that can ensue from having several different jurisdictions in Canada. That effort has, of course, been fueled by

constant pressure from the federal government to regulate this strategic sector. Despite the unanimous decision of the Supreme Court in 2011, which confirmed the provinces' exclusive power to regulate securities trading, the federal government continues to exert pressure and is now promoting a project to create a "federal-provincial" securities commission. Consequently, harmonizing Québec legislation with that of the rest of Canada continues to be a priority.

In all Canadian provinces except Québec, mutual fund dealers and representatives are subject solely to securities regulatory organizations having recognized the Mutual Fund Dealers Association of Canada (MFDA) as a self-regulatory organization. The current regulatory system in Québec limits the ability to harmonize the Québec model with that in the rest of Canada. This results in an additional cost for the sector, since a number of brokers working in Québec carry out their activities elsewhere in Canada.

In the context of the harmonization of securities regulations in Canada, the Authority held several consultations that led to the coming into force on September 28, 2009 of Regulation 31-103 respecting Registration Requirements, Exemptions and Ongoing Registrant Obligations. The regulation completed the necessary harmonization in respect of the registration of brokers and their representatives in order to implement the securities passport system. However, oversight of the mutual fund dealing sector has not yet been fully harmonized. The existence of two totally different oversight models complicates the harmonization of the rules applicable to mutual fund dealers and their representatives.

The Authority conducted consultations in 2007 and 2010 by proposing that the MFDA not be recognized as a self-regulatory organization (SRO) in Québec but to adopt by regulation the MFDA's rules compatible with the legislation and regulations in force in Québec. Under this model, the Chambre de la sécurité financière would continue to oversee the discipline and the ongoing training of mutual fund representatives working in Québec whether or not their broker is a member of the MFDA.

Not everyone agrees on this solution. Indeed, brokers doing business both in Québec and elsewhere are advocating full harmonization through the recognition of the MFDA. Otherwise, they maintain, no savings or simplification will be possible. In the case of independent brokers doing business solely in Québec, the change of structure might be important and the consequences could be decisive, especially for those with limited resources.

Were the MFDA to be recognized, the clients of Québec brokers would be covered by the Investor Protection Corporation (IPC), the MFDA's compensation fund. The IPC covers the losses that investors sustain in the event of the bankruptcy of their broker, which can stem from claims from defrauded clients. This option would possibly lead to changes in the Fonds d'indemnisation des services financiers (FISF) since brokers working in

Québec contribute to it. Under such a scenario, should both IPC and FISF coverage be kept or would IPC coverage be enough?

**Questions**

- C. What type of oversight should the government consider in the special case of mutual fund and scholarship plan dealing?
- D. Were the MFDA to be recognized, should FISF coverage be kept in addition to IPC coverage?

***Employees of insurers***

One of the consequences of the twofold oversight structure is the potential for conflict between the rules a firm seeks to impose on representatives acting on its behalf and the rules imposed by the chambers. The potential for conflict will generally be greater when the firm is an insurer and the representative is its employee. Indeed, the insurer's interest in imposing its own rules of conduct will be much greater in the case of an employee given the threat to its reputation that it incurs. In addition, under the Act respecting insurance, insurers must follow sound commercial practices, described in the AMF guidelines. According to international trends, the guidelines respecting commercial practices will become increasingly important. The potential for regulatory conflict can only grow.

Moreover, consumers' expectations of representatives and claims adjusters who are employed by an insurer are not the same as expectations with respect to other representatives. While consumers are entitled to expect to receive the same quality of advice concerning the suitability of products to their needs, they cannot expect the representative to shop around for the most advantageous of all available products. Only representatives who act on behalf of several insurers also offer consumers the advantage of being able to shop around for the most advantageous product.

Thus, in the case of an insurer's employees, the advantages of twofold oversight do not appear to be as great for consumers as the disadvantages for the industry, with respect to the potential for conflict over legislation and oversight.

**Question**

- E. What type of oversight should the government consider in the special case of insurers' employees?



### ***Claims adjusters employed by an insurer***

The subjection of claims adjusters in the ARDFPS is a different matter. Since they do not offer products or financial services, it is surprising that they should be regulated by a distribution law.

What is more, it is important to properly distinguish the activities of claims adjusters employed by the public and the activities of claims adjusters employed by or under contract to an insurer. Claims adjusters employed by the public act as intermediaries or offer second opinions to consumers who wish to obtain assistance in the management of their claim with the insurer.

When the insurer employs or gives a contract to a claims adjuster, the latter essentially performs a function directly linked to the insurer's activity. He does not offer a service. He performs a task on behalf of the insurer. While an insurance representative provides the client with a service that is separate from the product that he sells on behalf of the insurer, namely, the assessment of the client's needs and the recommendation of adequate products, the claims adjuster does not provide any service to the client: he certifies the claim, analyzes the contents of the policy and establishes on behalf of the insurer the compensation to which the insured party is entitled. It is the insurance contract that protects the client. The twofold oversight of these employees of the insurer can thus lead to especially complex situations that are complicated both for the adjuster and for the insurer.

#### **Question**

F. What type of oversight should the government consider for claims adjusters employed by insurers?

### ***Independent representatives***

A representative attached to a firm engages in his activities under the responsibility of the firm that employs him although he is personally responsible for his actions pursuant to the oversight by the chambers to which he is subject. This is not exactly the case for independent representatives since they are not attached to a firm. Thus, independent representatives experience twofold oversight directly, because they are subject to the same regulations and oversight as firms, as well as to the chamber's oversight of ethical conduct. The regulatory burden seems relatively heavier, since it must be borne by a single person.

#### **Question**

G. What type of oversight should the government consider for independent representatives?



---

## CHAPTER 4

### COMPENSATION IN THE EVENT OF FRAUD

Fraud perpetrated by a member of the representatives industry or involving it creates more victims than we think. There are, of course, those who lose money, but there are also thousands of honest, competent representatives who lose the trust of their clients and the public.

It is in order to guard against this collateral damage that industries for which public trust is vital establish compensation funds. The industry ascertains to what extent it wishes to guard against a loss of trust that will affect all of its members.

Governments acknowledge the obvious benefits for the industry but also for the public and often contribute to the success of such funds by making participation in them compulsory. Accordingly, several funds or other compensation mechanisms were initially set up based on entirely voluntary participation, which was subsequently imposed by regulation.

The Act respecting market intermediaries established the Fonds d'indemnisation en assurance de personnes within the Conseil des assurances de personnes, the Fonds d'indemnisation en assurance de dommages within the Conseil des assurances de dommages, and the Fonds d'indemnisation des planificateurs financiers for financial planners who are holders of a certificate issued by the Inspector General. The board of directors of the funds comprised one director appointed by the Minister and six directors appointed by the Conseil, three of whom were chosen from among the holders of certificates and three others from among individuals who, because of their activities, were likely to contribute in a specific manner to the resolution of problems inherent in the exercising of the activity of a market intermediary.

When the Act respecting the distribution of financial products and services (ARDFPS) was adopted, the three funds were merged to establish the Fonds d'indemnisation des services financiers (FISF) with the objective of maintaining the public's trust in representatives and firms by compensating the victims of fraud, fraudulent practice and misappropriation of funds. The management of the FISF was entrusted to a board of directors comprising seven members appointed by the Bureau des services financiers, itself managed by a board of directors two-thirds of whose members are industry representatives.

---

At the time of the establishment of the Autorité des marchés financiers (the Authority) in 2004, primarily for the purpose of offering the public and the industry a single outlet in the realm of the regulation of the financial sector, the FISF was integrated into the operations of the Authority and management of the fund was, consequently, transferred from the industry to a public body.

The FISF is the only fund of its type in Canada. Indeed, there are other compensation funds but they are managed by the industry and cover losses stemming from a firm's insolvency. The Investor Protection Corporation of the Mutual Fund Dealers Association of Canada (MFDA), and the Property and Casualty Insurance Compensation Corporation for casualty underwriters are but some examples. While the FISF is effective and the current system is working well, it has been subject to criticism in the wake of the financial scandals that have occurred in Québec in recent years.

At the request of the Minister of Finance at the time, the Authority conducted a public consultation from December 9, 2011 to March 9, 2012. The consultation notice included 22 questions and was accompanied by a reference guide on the protection mechanisms offered in Québec and in Canada. The Authority sought the opinion of market stakeholders on seven questions:

- the role of compensation in the array of measures aimed at protecting the consumers of financial products and services;
- the responsibility of consumers and representatives;
- the basic objective pursued by compensation;
- consumers' approach to compensation;
- responsibility for the management of compensation mechanisms for the victims of financial frauds;
- the products, representatives and acts covered by the compensation fund;
- funding of the compensation fund and cost mitigation measures.

The Authority received 34 briefs, some of them substantial.

The main problem related to the FISF stems from the fact that it only covers conduct that falls within the limits allowed by the certificate or the registration of the intermediary who acted fraudulently. Moreover, this is the most frequent reason for refusing compensation. It places a needless burden on the consumer's shoulders. Since the finance sector is changing constantly and products are increasingly numerous and complex, a consumer can experience certain difficulties in accurately ascertaining the products and services that the intermediary is, in fact, authorized to offer him. Accordingly,

one solution to this problem would be to provide protection to consumers as soon as they do business with a properly certified intermediary or one who is registered in one of the disciplines covered by the FISF, even if the claim concerns conduct that falls outside the acts allowed by the certificate or the registration accorded by the Authority.

Another problem raised with respect to the compensation system might be resolved according to the solution(s) adopted. For example, the fact that an investor who purchases a mutual fund from a representative of a mutual fund dealer is protected by the FISF but that a consumer who purchases the same product through a representative of an unrestricted-practice dealer is not protected poses a problem of fairness. Were the MFDA to be recognized in Québec and were we to rely essentially on its fund in the event of bankruptcy, as is the case for securities dealers, this incongruity would vanish.

The purpose of the fund is to maintain public trust in the distribution industry. However, the fact that the fund is managed by a public body instead of by the industry may give the impression that the consumer will be compensated whether or not the person responsible for the harm is registered. The nuance is important when it is a question of determining the compensation coverage and managing the public's expectations. It is difficult to understand why a public body agrees to compensate one fraud victim but not another one. On the other hand, it is quite understandable that an industry is willing to compensate the victims of a fraud perpetrated by one of its members but not the victims of a fraud perpetrated by someone else. Should management of the fund be reviewed?

The establishment of a committee that represents the industry in the Authority would be a solution that would make it possible to preserve the advantage of a single outlet that the consolidation in the Authority of oversight functions affords while putting, to some extent, the management of the fund in the hands of the industry.

The establishment in the Authority of a committee to rule on the eligibility of claims and determine the amount of compensation to be paid was introduced in 2008 by Bill 64. Indeed, the bill made provision for the establishment of a compensation committee comprising three members appointed by the Minister that would report to the latter on its activities every year. The provisions were never put into force since they did not seem to adequately respond to several problems related to the FISF. We might consider changing the committee's composition to make it more representative of the industry.

One other possibility would be to draw inspiration from it to establish a committee in the Authority to review decisions. The committee could be made up of members from the industry and would be responsible for reviewing at the request of consumers the Authority's decisions concerning compensation.

### **PROPOSAL 4**

- Make provision for a consumer to be compensated when he is the victim of a fraud perpetrated by a certified representative even if the claim concerns the sale of products that the representative was not authorized to offer.

### **PROPOSAL 5**

- Call upon industry representatives in the decision-making process of the Fonds d'indemnisation des services financiers.

---



## CONCLUSION

The current legislation has achieved its objective of protecting the public. However, it would be desirable to update it to take account of changes in the market. Oversight of intermediaries could also be simplified. In this respect, the reform that follows this report may be more or less sweeping and will take into account the comments that the report elicits.

---





---

## APPENDIX 1

### Summary of the recommendations

#### PROPOSAL 1

- Draw on the recommendations of the Canadian Council of Insurance Regulators to put in place a flexible legal framework that will enable insurers to offer their products online.

#### PROPOSAL 2

- Establish a legislative framework for distribution without a representative that applies directly to insurers, which must ensure that the mandataries (now called distributors) abide by the rules.

#### PROPOSAL 3

- Examine all approaches to ease the regulatory and financial burden of registrants, while maintaining adequate oversight of the distribution of financial products and services.

#### PROPOSAL 4

- Make provision for a consumer to be compensated when he is the victim of a fraud perpetrated by a certified representative even if the claim concerns the sale of products that the representative was not authorized to offer.

#### PROPOSAL 5

- Call upon industry representatives in the decision-making process of the Fonds d'indemnisation des services financiers.
-



---

## APPENDIX 2

### Summary of the consultation questions

#### Questions

- A. In your view, do the advantages of twofold oversight outweigh the costs engendered?
  - B. If not, what type of oversight do you propose?
  - C. What type of oversight should the government consider in the special case of mutual fund and scholarship plan dealing?
  - D. Were the MFDA to be recognized, should FISF coverage be kept in addition to IPC coverage?
  - E. What type of oversight should the government consider in the special case of insurers' employees?
  - F. What type of oversight should the government consider for claims adjusters employed by insurers?
  - G. What type of oversight should the government consider for independent representatives?
-



