FAIR Canada Canada's Investor Rights Advocate | Promoteur des droits des investisseurs

July 25, 2024

Financial Services Regulatory Authority of Ontario (FSRA)
Submitted via the FSRA website

Re: FSRA's Consultation on Rule 2024-002 - Total Cost Reporting Rule (Proposed Rule)

FAIR Canada is pleased to provide comments in response to the above-referenced Consultation.

FAIR Canada is a national, independent, non-profit organization known for independent and thoughtful commentary on public policy matters. Our work includes advancing the rights of investors and financial consumers in Canada through:

- Informed policy submissions to governments and regulators
- Relevant research focused on retail investors
- Public outreach, collaboration, and education
- Proactive identification of emerging issues.[1]

A. We Support FSRA's Proposed Rule

In April 2023, the Canadian Council of Insurance Regulators (CCIR) adopted new cost and performance reporting guidance (the Insurance Guidance) for individual variable insurance contracts (IVICs). At the same time, the Canadian Securities Administrators (CSA) adopted new rules to improve existing annual cost and performance reporting for investment funds (together, the TCR Enhancements).[2]

The Insurance Guidance aims to ensure that policyholders, like mutual fund unitholders, receive ongoing cost and performance information for their IVICs in an easy-to-understand format specific to their holdings. While the Insurance Guidance may help promote consistent regulatory standards and best practices across Canada, it is not legally binding.

[1] Visit www.faircanada.ca for more information.
[2] CCIR Individual Variable Insurance Contract Ongoing Disclosure Guidance and Amendments to National Instrument 31-103 Registration Requirements, Exemptions and Ongoing Registrant Obligations and to Companion Policy 31-103CP Registration Requirements, Exemptions and Ongoing Registrant Obligations – Total Cost Reporting for Investment Funds and Segregated Funds, April 20, 2023.

If approved, FSRA's Proposed Rule would make the key elements of the Insurance Guidance legally binding in Ontario and ensure that investors owning IVICs receive their first enhanced annual reports for the year ending December 31, 2026, similar to mutual fund owners. It will also address concerns about the lack of any requirement for insurers to provide ongoing, easily understandable reporting about the costs of owning an IVIC.

Consistent with the principles of fairness and transparency, consumers should be able to see all the costs associated with investing and how those investments are performing. The Proposed Rule will provide IVIC owners with more transparent, accessible, and complete cost and performance information, helping them assess their investments better and achieve their financial goals.

Strengthening Ontario's regulatory framework in this way will also increase accountability, help prevent unfair practices that could harm consumers, and boost consumer confidence. We urge other provincial and territorial regulators with rule-making powers to consider a similar approach.

B. Exceptions Should be As Narrow as Possible

1. Where Historical Information is Not Available

The Proposed Rule includes an exception in section 2(2) for insurers who have not maintained historical information before the rule takes effect. The exception addresses situations where the insurer does not possess and cannot, with reasonable efforts, obtain information about deposits and withdrawals, the change in the value of investments in the IVIC (for reasons other than deposits and withdrawals) or the owner's rate of return. Under the Proposed Rule, the insurer must provide the information for any period it possesses or can reasonably obtain.

Given the importance of historical performance information, the exception should be as narrow as possible. We support the current wording, which addresses situations where obtaining the information is impossible (e.g., data loss due to a change in IT systems) or where obtaining it would require unreasonable efforts.

We are concerned, however, with the lack of guidance or clarity regarding "reasonable efforts." Each person or institution will have its own sense of what this means. We recommend that FSRA provide clear guidance about what would be considered reasonable efforts.

FAIR Canada also agrees that the insurer should notify the insured if certain information is missing from the statement and specify which information. We also strongly support the requirement that the insurer provide an attestation to FSRA detailing their efforts to obtain the information and explaining if they did not try to obtain it. The attestation is critical to limit potential abuses of the exception and ensure it is only used when genuinely needed.

We agree that the exception should not apply to IVICs issued after the Proposed Rule comes into force. We see no reason such contracts should not maintain and report historical information from the issuance date. Insurers know the historical reporting expectations in the Insurance Guidance and the Proposed Rule and should be prepared to maintain and report this information for new IVICs.

2. Should there be Additional Exceptions?

FSRA is seeking feedback on whether additional exceptions to the Proposed Rule are appropriate. These would be based on circumstances that some insurers believe could result in the costs of complying with the Proposed Rule outweighing the benefits to investors. Specifically, they suggest there should be additional exceptions from having to report historical information relating to deposits, withdrawals, growth/loss, and personal rate of return (historical performance information) based on the date when the contract was first issued when one of the following change events occurs:

1. there is a change in the tax status (e.g., an IVIC was held in an RRSP account and is now held in an RRIF account)
2. where there is a change in the owner of the IVIC
3. where the IVIC holder switches securities dealers

The justification for providing an exception in these circumstances is that it would align with the performance reporting done by securities dealers in similar circumstances for clients holding mutual funds. In the case of mutual funds, the performance reporting period would be reset based on the date when one of these three change events occurred. It would also be consistent with current practice by some insurers (but inconsistent with the Insurance Guidance).

While we support the principles of harmonization and minimizing undue costs where appropriate, the benefits are often in the eye of the beholder. We must also be mindful of important distinctions between IVICs and Mutual Funds. Further, the desire for harmonization should not come at the expense of ensuring investors have the information they need to make informed decisions. In the case of IVICs, we believe that certain fundamental differences in the product may justify a different approach compared to mutual funds. These differences come into play, particularly when the IVIC's owner changes, or the investor who purchased the IVIC switches securities dealers.

IVICs differ from mutual funds in many ways, including that the contract owner does not own the mutual funds within the segregated fund. Instead, the insurer owns the segregated fund assets. Moreover, the value of segregated fund assets serves as the benchmark upon which the value of the IVIC is derived. This contrasts with mutual funds, where the investor holds a direct ownership interest in the fund. That Segregated Funds may have mutual funds is an insufficient justification for not providing historical performance information from the contract's date. In the case of an IVIC, this information relates more to the value of the contract than it does to the individual funds that may have been held in the segregated

funds associated with the contract. The fact that the contract may continue after these change events reinforces this difference.

The change in owner scenario is an example of why a different approach to performance reporting may be justified. When the IVIC owner changes, the new owner typically knows the previous owner (e.g., a spouse or relative). Historical performance information from the IVIC's inception is critical for the new owner. It allows them to see how the contract has performed over time and make informed decisions about any changes to the segregated funds that determine the value of the IVIC's benefits. Restarting reporting from the change date would eliminate this crucial information, providing only a limited snapshot of the contract's performance. In contrast, mutual fund holders sell into the market to unrelated parties, so it is reasonable to restart reporting based on the date the new owner acquired the mutual fund.

Similarly, when there is a change in securities dealer, we believe insurers should report historical performance information from when the IVIC was first issued. In the securities sector, a new securities dealer is legally required to assess whether the products in the client's portfolio remain suitable based on the client's needs and goals and the products' attributes. The dealer may recommend selling some of the mutual funds and buying others. We also note that performance reporting reflects the value of advice from the dealer, so when the dealer changes, it is appropriate to restart the reporting to represent the start of that relationship with a new securities dealer.

Conversely, we understand there is no suitability obligation in the insurance sector. Although there is guidance on IVIC suitability,[3] there is no requirement to re-assess the segregated funds in the IVIC when the securities dealer changes. Some dually licensed individuals selling mutual funds and insurance products may evaluate suitability in this scenario. However, we understand that because IVICs are insurance products, there is no legal obligation to comply with the securities law suitability requirement. Again, this is an important distinction that must be considered when considering additional exceptions.

Finally, it is essential to remember that the assets in a segregated fund do not necessarily have to be mutual funds. The value of an IVIC is tied to the market value of the assets in the segregated fund, which could be real estate funds. For example, the Great-West Life Real Estate Fund is a segregated fund that invests in diverse properties.[4] This suggests that IVIC reporting should not necessarily replicate mutual fund reporting.

While we support consistent disclosure, IVICs are not mutual funds. Substantial differences may warrant distinct reporting requirements following one of the change events. Stated differently, harmonization should not obscure the fundamental differences between these products. Where there is a change in the owner or securities dealer, the Proposed Rule should require insurers to report performance information from the date the IVIC was first issued.

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[3] Canadian Life and Health Insurance Association, Reference Document: IVIC Suitability Needs-Based Sales Practices, October 2016.
[4] Great-West Life Real Estate Fund.

We also agree with FSRA that those seeking these additional exceptions should demonstrate the costs and challenges in complying with the Proposed Rule and justify the need for such exceptions. The principles of fairness and transparency should be paramount when considering additional exceptions. Consumers deserve clear, complete information about their financial products. If FSRA is considering any further exceptions, we request they be published for comment.

C. Provincial Rules for IVICs Should be Harmonized Where Possible

The CCIR expects each member jurisdiction to adopt the Insurance Guidance by local guidance or regulation. To date, both FSRA and the Autorité des marchés financiers (AMF) have taken steps to incorporate the Insurance Guidance into a rule.

In November 2023, the AMF published for comment a draft regulation about information to be provided to IVIC owners. In July 2024, the AMF issued a second consultation that proposes only two exceptions. The first exception is similar to the exception in section 2(2) of the Proposed Rule. That is, where providing performance information would be too difficult or impossible for an insurer to obtain the information. The AMF also proposes one further exception in the case of a change in the registered tax status. As proposed, the AMF would permit insurers to report historical performance information from the date of the change instead of from the contract date.

We believe that the AMF has reached the appropriate conclusion. However, regardless of the final approach adopted by the AMF, we would encourage FSRA and the AMF to work together to develop a consistent and harmonized approach in their respective rules. A unified approach will help to:

- Ensure IVIC owners across Canada receive the same type and quality of information regardless of where they live. This consistency makes comparing different contracts and providers easier, leading to less confusion and more informed decision-making.
- Simplify compliance for insurers operating in multiple jurisdictions, leading to lower costs for both consumers and insurers.
- Facilitate more effective oversight and monitoring of the insurance industry. When reporting is standardized, regulators can more easily identify trends, risks, and issues.

D. FSRA Needs to be Able to Grant Exemptions to its Rules

FSRA's approach to cases where insurers cannot provide historical information differs from the approach in the Insurance Guidance. The Insurance Guidance allows insurers to request a full or partial exemption from specific expectations or to provide the required information in a different format. In contrast, the exception is in the Proposed Rule itself because FSRA lacks the statutory authority to grant exemptions from its rules.

We encourage the Ontario government to consider giving FSRA the power to grant exemptions from its rules. Including exceptions in a rule requires FSRA to anticipate every possible need. This is difficult because the insurance industry constantly changes, and unexpected issues may arise.

The ability to grant exemptions would give FSRA the flexibility to tailor the exemption to the specific situation and respond to developments not foreseen when the rule was drafted. It would also be more efficient than amending the rule to accommodate unexpected circumstances. Finally, the authority to grant exemptions would align FSRA with the Ontario Securities Commission, which has the statutory authority to grant exemptive relief from securities law requirements on a case-by-case basis.

We caution, however, that any grant of exemptive relief should carefully consider consumer interests. Under the Ontario *Securities Act,* the exemption must not be prejudicial to the public interest.[5] We would support a similar public interest requirement for FSRA.

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Thank you for considering our comments on this important issue. We welcome any further opportunities to advance efforts that improve outcomes for consumers. We intend to post our submission on the FAIR Canada website and have no concerns with FSRA publishing it on its website. We would be pleased to discuss our submission with you. Please contact Jean-Paul Bureaud, Executive Director, at jp.bureaud@faircanada.ca or Tasmin Waley, Policy Counsel, at tasmin.waley@faircanada.ca.

Sincerely,

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FAIR Canada | Canadian Foundation for Advancement of Investor Rights

[5] Securities Act, R.S.O. 1990, c. S.5, s. 80.