February 23, 2023

Mr. Huston Loke
Executive Vice President, Market Conduct
Financial Services Regulatory Authority of Ontario (FSRA)
25 Sheppard Ave West, Suite 100
Toronto, ON M2N 6S9

Submitted by email to: huston.loke@fsrao.ca

Re: Amendments to the Unfair or Deceptive Acts or Practices Rule for Deferred Sales Charges

Dear Huston:

The CLHIA is pleased to respond to the FSRA consultation regarding the draft amendments to the Unfair or Deceptive Acts or Practices Rule related to changes for deferred sales charges (DSCs) in individual variable insurance contracts.

The requirements for currently held contracts with DSCs are generally appropriate. The industry is in the process of making adjustments to its segregated fund products to comply with the requirement as of June 1, 2023.

We agree that it is appropriate to provide protections to existing DSC contractholders. Insurers intend to take an approach for existing DSC contracts which will result in the fair treatment of customers.

The CLHIA supports the stated goal of harmonizing the DSC ban among all CCIR jurisdictions.

Our detailed comments regarding each of the proposed amendments follow.

About CLHIA

The CLHIA is a voluntary association whose member companies account for 99 per cent the life and health insurance business in Canada. These insurers are significant contributors to Ontario and its economy. They provide financial security to about 11.1 million Ontarians and make over $50 billion in benefit payments (of which 90 per cent goes to living policyholders as annuity, disability, supplementary health, or other benefits with the remaining 10 per cent going to life insurance beneficiaries). In addition, life and health insurers have more than $380 billion invested in Ontario's economy. A large majority of life and health insurance providers are licensed to operate in Ontario, with sixty-two headquartered in the province.

Amendment 1 – Deferred Sales Charges – Issuing and Changing Individual Variable Insurance Contracts

Definition of DSC

The definition of a DSC is quite expansive and consideration should be given to making it much more streamlined. In our view, greater simplicity would result in more clarity and make application of the definition easier. A principles-based approach should be applied.

The meaning of a DSC is sufficiently captured in s. 1(1)(vii.1)(i) and sections (ii) and (iii) of the definition could be removed. There is no need to include a long list of many different terms that may be used to describe a DSC.

The list of types of fees and charges that will not be considered a DSC is helpful, but this should not be framed as an exhaustive list.

More clarity is required about what is intended to be captured by section 1(1)(vii.1)(iv)(d) which states that a DSC does not include "a market value adjustment the insured is required to pay that is calculated based on changes in interest rates, but not based on compensation an agent received with respect to the investment."

It is our understanding that section 1(1)(vii.1)(iv)(d) is not intended to apply to the situation where there is a separate guaranteed interest annuity investment option offered as part of an individual variable insurance contract and a consumer decides to cash out before the end of the agreed fixed term (for example, 1, 2, 3, or 5 years). This makes sense because we understand banks are not restricted from charging market value adjustments, nor is it a harmonization matter with the mutual fund industry. To provide better clarity, we request that section 1(1)(vii.i)(iv)(d) be removed entirely or the words "but not based on compensation an agent received with respect to the investments" be removed.

Similar to the approach taken by the Autorité des marchés financiers in commentary related to the draft *Regulation respecting the prohibition on charging certain fees from holders of individual variable insurance contracts relating to segregated funds*, we would also appreciate clarification that the DSC definition will not extend to insurance products other than individual variable insurance contracts. For example, guaranteed interest annuity options offered separately from an individual variable insurance contract, or segregated funds offered under a universal life insurance policy.

Replacement Individual Variable Insurance Contracts

It is appropriate to permit new DSC contracts when they involve replacing a current DSC contract such as for conversions from RRSPs to RRIFs, LIRA to LIF or transferring ownership. It would be helpful to clarify that DSC schedules will not be permitted to re-start upon a transfer but only be allowed to continue for the remaining time in the original schedule.

In some situations, a replacement contract may contain terms and conditions that are "similar" but do not replicate in exact form the contract that is being replaced. To be flexible and clearly accommodate what we understand is the general intent of section 11(2), it would be helpful for the rule wording to permit issuing a replacement individual variable insurance contract on "similar terms and conditions" rather than the "same terms and conditions".

Amendment 2 – Deferred Sales Charges – Deposits to Pre-June 1, 2023 Individual Variable Insurance Contracts

Transfers of existing contracts to a non-DSC option

To the extent it is practical, insurers are working to switch additional deposits after June 1, 2023 under existing DSC contracts to a different sales charge option such as front-end load 0 (FEL-0) or no-load. Consumers will be provided prior notice of the change and permitted to select another available sales charge option instead if they want to.

In order for insurers to apply a different sales charge option (default sales charge option) to these deposits, paragraph 12(3) would require them to send beforehand to contract owners a notice detailing all the sales charge options available and MERs. To our knowledge, this was not required on the mutual fund side where an automatic switch approach was applied. There are circumstances on the segregated fund side where paragraph 12(3) would make the notice unnecessarily complicated and detailed. For example, where the default sales charge option is a no-load option or FEL-0 option with the same or a more favourable MER, it would be in the best interest of consumers to keep the notice simple and concise. An insurer applying a default sales charge option after prior notice of the change to consumers is taking a fair treatment of customers approach. It ensures a smooth and equitable transition for all consumers. Consequently, it would be preferable for the notice requirement wording to be more general.

There will likely be some operational challenges with meeting the June 1, 2023, deadline for some DSC contracts and providing notice in advance. We provide additional comments on implementation timelines below.

To allow for operational efficiency and due to the short timelines associated with this initiative, the industry would like flexibility to provide notice to current contractholders about either continuation of DSC or the transfer to FEL-0 or no-load as part of the regular six-month communication to clients at the end of June.

It should be noted that in some cases, insurers have already notified their customers and sales forces of the expected changes to DSC. It is important that the new requirements not be given retroactive application or deemed to apply to notices provided before publication of either the draft or final rules. In all situations, insurers are approaching the changes taking a fair treatment of customer approach.

Continuing DSC contracts

We understand that insurers are permitted to continue to receive deposits on a DSC basis if the insurer cannot remove DSC as a sales charge option. It would be helpful for FSRA to state affirmatively that DSC is permitted to continue where no other contractual option is permitted.

For a legacy contract, it may not be possible to switch the sales charge option without a complete overhaul of these older contracts and the systems that administer them. In this context, the exception for DSC contracts should extend to contracts administered on a legacy system. A practical approach should be taken which recognizes the need to administer contracts in an efficient way since these older contracts are often favourable to the contractholder with features that are no longer offered. We expect these circumstances to be limited.

Paragraph 12(4) which requires the insurer to provide an explanation of the DSC to a consumer prior to making a DSC contribution should not be an ongoing obligation but a one-time obligation. Alternatively, there should be a different one-time obligation for PAC contributions, or an annual notice or reminder requirement. Contractholders who wish to continue contributing to the contract under the DSC option should be provided notice about the DSC fees.

Harmonized Approach to Implementation

The CLHIA is supportive of FSRA adopting a harmonized approach to implementation with other provincial jurisdictions. Insurers plan to implement the changes in the most efficient way possible by adopting a national approach.

Implementation Timeline

Insurers are working towards making product changes in advance of June 1, 2023 and there is quite a tight deadline from an operational perspective. Generally speaking, we believe an implementation timeline of 18 to 24 months should be allowed following publication of a final rule requirement. In this context, should implementation challenges arise, we request that a flexible and principles-based approach be applied related to compliance with the June 1, 2023 deadline.

Thank you for the opportunity to comment on this important regulatory change for the industry.

Sincerely,

Lyne Duhaime
Senior Vice President, Market Conduct Policy, and Regulation

cc. Erica Hiemstra, Head Insurance Conduct, Market Conduct, FSRA
Chris Caldarelli, Senior Policy & Technical Lead Policy, Market Conduct, FSRA