Guideline G8

ADVISOR SUITABILITY: Screening, Monitoring and Reporting

This Guideline has been approved by the Board of Directors of the Canadian Life and Health Insurance Association Inc. (CLHIA). Member Companies are expected to adopt this CLHIA Guideline having regard to the company's structure, products and business processes, including distribution channels. Member Companies are urged to incorporate this Guideline into the company's ongoing compliance program.

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1. INTRODUCTION

Advisor suitability is central to the industry's overall goal of treating the customer fairly.

Suitability means a lot of things but, at its core, it focuses on a single question: Does the advisor's conduct indicate a willingness and ability to provide customers with sound advice about life and health insurance products and services? Answering this question requires insurers to consider, on an on-going basis, a wide range of factors that can affect the performance of advisors and give rise to potential risks to the consumer.

Insurers maintain compliance systems that are reasonably designed to ensure that each advisor representing the insurer complies with relevant statutory and licensing requirements. This includes initial screening and on-going monitoring of advisors for suitability and reporting advisors who are not suitable. More generally, the practices described in this Guideline are central elements in a comprehensive strategy for managing reputation risk and treating customers fairly.

2. PURPOSE

This Guideline sets out a framework and describes practices to assist companies in establishing and maintaining a system for screening, monitoring and reporting advisors.

3. SCOPE

The practices described in this guideline are applicable to all licensed life and/or accident and sickness advisors regardless of the type of insurance product they are selling or the distribution channel in which they operate. The practices can also be used, as appropriate, in situations involving distribution by incorporated advisors.

In the event of any conflict between the provisions of this Guideline and any applicable law, the law takes precedence over the Guideline to the extent of the conflict.

4. DEFINITIONS

“Advisor” means any person or entity licensed by a Canadian province or territory to sell life insurance or accident and sickness insurance. For greater clarity, ‘advisor’ in this Guideline refers to "agent" or "representative" and similar terms commonly used in the industry.

"Monitoring" is an on-going process for managing identified risks and identifying additional risk in advisors.

"Screening" is a one-time process for initially assessing the suitability of an advisor and identifying compliance risk related to the advisor.

5. RESPONSIBILITIES OF COMPANIES

Insurers should have comprehensive policies and procedures for screening, monitoring and reporting. Among other things, the policies and procedures should describe the criteria an insurer will use for making decisions about enhancing the level of scrutiny and managing identified risks.

Generally, insurers will take a risk-based approach in determining when and how to implement specific practices. Section 10 of this Guideline describes the continuum of risk that may occur for a number of factors.

Many of the decisions an insurer is required to make about an advisor's suitability entail the balancing of interests. On the one hand, insurers need to effectively investigate concerns about an advisor so that decisions about suitability are fair and based on accurate information. On the other hand, insurers need to protect customers from any potential harm that might result from following the advice of an advisor who is not suitable. In the end, decisions should be guided by the overriding objective of treating the customer fairly.

If an insurer has reasonable grounds to believe that advisor acting on its behalf is not suitable, the insurer should report this to the applicable provincial or territorial regulator(s).

If an insurer has reasonable grounds to believe that an advisor is not suitable, the insurer should not enter into or maintain a contract with that advisor.

Where an insurer learns of facts that give rise to concerns or questions about the suitability of an advisor, the insurer should carefully assess the risk and take steps to clarify and effectively manage that risk.

6. DELEGATION OF DUTIES

Insurers in a contractual relationship with an agency that provides services to assist agents in the distribution of insurance may delegate some or all functions related to screening and monitoring to that agency. For example, an insurer operating in the Managing General Agency (MGA) channel may rely on the MGA to confirm that the agent’s licence is valid when placing business.

In situations where an insurer delegates a screening or monitoring function, the insurer retains responsibility. Accordingly, insurers who delegate screening or monitoring functions should take reasonable steps to ensure that the delegate is capable of carrying out these functions and is, in fact, carrying out the functions.

In Quebec, when the distribution of insurance is performed by a licensed firm, some of the practices described in this Guideline are statutorily prescribed obligations of the firm.

Insurers should not delegate reporting functions.

7. SCREENING

Effective screening practices should provide reasonable grounds to believe the advisor is suitable. This picture should be used to make informed decisions about contracting and, if the insurer decides to enter into a contract with the advisor, subsequent monitoring.

Insurers, or their delegates, should use the CLHIA Advisor Screening Questionnaire when making an initial assessment of the suitability of an advisor.

As noted in Section 5, if screening reveals reasonable grounds to believe an advisor is not suitable, the insurer should not enter into a contract with the advisor.

Screening may reveal issues with an advisor who is otherwise suitable. In these situations, the insurer should use the screening information to make decisions about risk-based monitoring that effectively manages the risk created by these issues.

Exclusive reliance on self-reporting by the advisor will not generally be sufficient for effective screening. To verify the information in the self-reports and obtain additional information that might be relevant to assessing the advisor's suitability, insurers should make inquiries with other insurers with whom the advisor has or has had contracts and/or with references provided by the advisor. Among other things, previous employers and insurers should be asked about the grounds for any employment or contract terminations and compare the information collected with that provided by the advisor. Regulatory databases for licensing and disciplinary decisions should also be checked to confirm the accuracy of self-reported information.

8. MONITORING

Monitoring practices generally provide a more targeted picture of the advisor's business practices and sales activities. The information gathered in monitoring is intended to help the insurer manage potential risks identified in screening and/or find information that indicates a problem may be developing.

Where signs of potential problems are detected, insurers should use this information to make informed decisions about heightening scrutiny and/or initiating investigations of the advisor.

For greater clarity, whereas effective screening practices will generally be consistent from one advisor to the next, monitoring practices are more likely to vary depending on the insurer's assessment of the risk presented by an advisor.

9. REPORTING

The intent of reporting is to advise regulators and other appropriate parties in a timely manner of concerns about an advisor's suitability.

As noted in Section 5, decisions about what to report, to whom and when need to take into consideration the fair treatment of both the advisor and the public. In making decisions about reporting, however, the overriding objective should be to mitigate risk to the public.

Decisions about reporting will reflect three general sets of circumstances.

1. Reporting of concerns at an early stage to industry stakeholders who inquire about the advisor in the process of conducting their own screening.

2. Notifying regulators of concerns where the insurer intends to maintain the contract, generally with heightened monitoring.

3. Notifying regulators of concerns and a decision to terminate the contract.

10. FACTORS RELATED TO SUITABILITY

The following types of information and related considerations should be taken into account by an insurer when assessing the suitability of an advisor.

In some instances, a single incident may be serious enough that it would provide the insurer with reasonable grounds for believing that the advisor is not suitable. In other instances, it may be necessary to detect a “pattern” of actions before deciding there is sufficient evidence to warrant investigation or heightened scrutiny. (A “pattern” means that the incidents are not isolated and there is reason to believe they are evidence of the advisor’s regular method of conducting business.)

10.1 Criminal Convictions

Past criminal activity may be evidence of heightened risk. The assessment of risk will vary depending on the type and seriousness of the crime, the number of convictions and how recently the activity occurred.

It should be noted that for offences committed under the *Youth Criminal Justice Act* or similar previous legislation such as the *Young Offenders Act* (repealed in 2003), that are self-reported by the advisor, the risk of subsequent offences may be lower.

10.2 Unresolved Criminal Charges

Potential risk presented by unresolved charges is heightened due to the facts that the charges may be more recent and additional criminal activity may come to light. Accordingly, decisions about the suitability of an advisor who is currently facing criminal charges should generally be delayed until such matters are resolved.

10.3 Disciplinary Actions by Regulators

An advisor who has been fined or had a licence sanctioned or revoked by any regulatory body for contravention of by-laws and rules, or provincial or territorial insurance acts or regulations, should be investigated to determine whether, based on information available to the insurer, the advisor is suitable.

Sanction or revocation of a licence by a regulatory body should generally be regarded as evidence of high risk.

10.4 Unresolved Charges or Investigations by Regulators

As is the case for unresolved criminal charges, the lack of resolution of a regulatory action increases risk. Accordingly, decisions about the suitability of an advisor who is currently charged or under investigation by any regulatory body should generally be delayed until such matters are resolved.

10.5 Financial Health

The financial health, or lack thereof, of an advisor can influence how that advisor manages his or her dealings with customers. Advisors experiencing financial difficulties may be distracted and unable to give customers the attention they require or they may recommend products the customer does not need. In more extreme situations, the advisor may be motivated to misappropriate the customer's funds.

Insurers should take reasonable steps to ensure they are able to accurately assess the advisor's financial health.

An advisor who is an undischarged bankrupt should be treated as a high risk. Insurers should be familiar with all relevant details of the situation before deciding to issue or continue a contract with an advisor who is an undischarged bankrupt.

Where there is evidence that bankruptcy (either discharged or conditionally discharged) led to the advisor engaging in unacceptable sales practices, this should be treated as a high risk.

Insurers should be familiar with all relevant details of the previous bankruptcy and its effect on the advisor's sales practices and enhance scrutiny of transactions to protect customers from the risk of unacceptable sales practices.

Advisor debt should be carefully assessed with attention paid to the amount of debt, the reasons for the debt and changes in the debt profile.

10.6 Licensing Requirements

Specific licensing requirements vary from jurisdiction to jurisdiction across Canada and may be updated or increased at any time.

(i) Valid licence

The advisor must hold a valid licence for the products he or she is selling and satisfy all the licensing requirements of the jurisdiction issuing the licence. For advisors holding a non-resident licence, this includes ensuring compliance with any requirements that exceed those of the advisor's home jurisdiction. Related to this, where an advisor shares his or her commission with another person, the advisor should ensure that person is licensed.

(ii) Errors and omissions insurance

Errors and omissions insurance, including fraud coverage, is mandatory for advisors in many provinces. Monitoring should routinely confirm that advisors are complying with regulatory requirements. Even where it is not required, having adequate coverage, including fraud, is a prudent business practice and an important safeguard for customers. An advisor's unwillingness or inability to secure coverage should be treated as a sign of potential risk.

(iii) Continuing education

Continuing education is mandatory for advisors in Alberta, British Columbia, Manitoba, Ontario, Quebec and Saskatchewan. Even where it is not required, a commitment to continuing education is a sign of professionalism and an important safeguard for customers. An advisor's unwillingness to take continuing education courses may be a sign of potential risk.

10.7 Statutory Compliance

Advisors should have written policies and procedures that describe how they comply with a number of statutory requirements beyond insurance regulation. These include privacy, anti-money laundering/anti-terrorist financing, FATCA, telemarketing rules and anti-spam laws. In addition, many insurers have corporate policies that may be more restrictive than current insurance regulation. Some common examples relate to rebating and trafficking insurance (or viatical settlements). If an advisor does not have written policies and procedures in these areas, this may be an indication that the advisor is either unaware of his or her responsibilities or not clear about practices that address them and should be treated as a risk.

10.8 Sales Practices

A number of specific sales practices are evidence that an advisor may not be suitable. These practices are described in Appendix 1.

Insurers should be responsive to any signs that an advisor may be engaging in any of these practices. Investigations and the reassessment of risk should be done in a timely manner to protect customers. Where practices are inadvertent or well-intended, education of the advisor may be sufficient to prevent further risk. Where the investigation turns up evidence of a more serious problem, the insurer should take appropriate action to mitigate the risk as quickly as possible.

10.9 Sales Trends

Trends in sales can provide indirect evidence about the appropriateness of product recommendations and other advice. Patterns that fall outside accepted norms (e.g., unusually low levels of conservation or persistency) or suddenly change (e.g., shifts in products or client profiles) may be evidence of heightened risk. Changes in the type of client an advisor is serving or the types of products recommended may be evidence of heightened risk, especially if there are no signs the advisor has received additional training.

Appendix 1

Unacceptable Sales Practices

1. Fraud

Intentional deception or misrepresentation which an individual knows to be false or does not believe to be true and is made knowing that it may be detrimental to the other party and that it could result in some unauthorized benefit to the advisor, or some other person.

2. Misappropriation of Client Funds

Taking money or other property received from the client and using it for any purpose other than that specified by the client.

3. Forgery

Knowingly making a false document with intent that (a) it will in any way be used or acted upon as genuine, to the prejudice of a person, or (b) some person will be induced, by the belief that it is genuine, to do or to refrain from doing something.

4. Money Laundering/Terrorist Financing

Money laundering is the processing of criminal proceeds to disguise their illegal origin. Terrorist financing is the collection or distribution of funds with the intent or knowledge that the funds will be used by a terrorist or to carry out a terrorist act.

5. Privacy or Confidentiality

Any transmittal of personal information, whether intentional or unintentional, for purposes other than those consented to by the individual described by the information.

6. Conflict of Interest

Intentionally failing to provide to customers disclosure of business relationships with insurers and all conflicts of interest or potential conflicts of interest associated with a transaction or recommendation as set out in the CLHIA Reference Document: Advisor Disclosure.

7. Tied Selling

Making the purchase of one product conditional on the purchase of another product.

8. Premium Rebating

A promise or agreement for the premium to be paid for a policy in a lesser amount than the premium set forth in the policy, or paying (or *offering* to pay) a rebate of the whole or part of the premium stipulated by the policy, or any consideration or thing of value intended to be in the nature of a premium rebate, except to the extent permitted by law.

9. Inducements

Making, or offering to make, any payment of money or gift of value, directly or indirectly, to convince a customer to purchase insurance except to the extent permitted by law.

10. Replacements

(i) Undisclosed and/or Systematic Replacements

Failure to provide full and fair disclosure to the customer and insurer as required by provincial and territorial laws or systematic internal or external replacements that are detrimental to the customer.

(ii) Twisting

Persuading a customer to terminate a policy solely for the purpose of selling another policy

without regard to possible disadvantages to the customer. It can also involve using the values,

either through loans or through the re-direction of dividends, of one policy to purchase another.

(iii) Churning

Initiating, for personal gain, transactions so that the volume or frequency of trades is excessive

in view of the character of the account and the customer's personal objectives.

11. Misrepresentation and Disclosure

(i) Holding Out

Intentional misleading of the customer using any media (e.g., business cards, websites, social media, etc.) in regard to credentials or designations or authority, or the ability to provide advice

or service.

(ii) Unfair or Deceptive Statements

Failure to provide full and accurate disclosure so the customer can make an informed decision about the purchase of a product or service.

(iii) Illustrations

Unauthorized changes by an advisor to company-provided illustrations, or manipulation by an advisor of software beyond its defined parameters to create an unreasonable expectation about the benefits or advantages of the policy.

It is expected that all advisors will follow CLHIA Guideline G6 *Illustrations* or G15 *Guaranteed*

Withdrawal Benefit (GWB) Illustrations as appropriate on the use of illustrations for life insurance and/or IVICs with guaranteed withdrawal benefit features.

12. Misrepresentation to the Company

Failure of the advisor to provide full, complete and accurate information to the insurer.

13. Improper Paperwork

Any practice that thwarts, intentionally or unintentionally, the evidentiary intent of a signature.

This includes but is not limited to the use of presigned forms, signature witnesses made at a time other than when the customer signs the document, and improper initialing of error corrections. Where the transaction is conducted and evidenced electronically, a similar standard applies. Delays in delivering policies may be a sign of sloppiness and can create a risk for clients as the delay lengthens the period between the time the policy was explained and whey it is available for review.

14. Product-Client Suitability

Failure to consider the customer's needs, ensure fair treatment and make appropriate recommendations. More generally, failure to follow the steps described in CLHIA Reference

Document: Needs-Based Sales Practices.

15. Undue Influence

Encouraging a customer to act on a recommendation in a situation where the advisor knows or ought to know that the customer is unable to understand the character, nature, language or effect of the transaction or proposed transaction.

16. Coercion

Compelling a customer, through the use or threat of physical force, to act on a recommendation.

17. Incompetence

Any lack of technical or general knowledge or judgment required to carry out sound business practices and make recommendations based on needs-based sales practices.

18. Fronting

Submission of an application for insurance and receipt of commission by a licensed advisor on behalf of an unlicensed person who solicited the sale. Also, submission of an application by a licensed advisor on behalf of another licensed advisor who does not have a contract with the insurer to whom the application is submitted. More generally, fronting is allowing another person to solicit business and submit it to an insurer under the advisor's name.

19. Trafficking in Insurance and Stranger Owned Life Insurance

Trafficking

(i) Facilitating the sale of a customer’s insurance policy to a third party that holds itself out

as a purchaser of life insurance policies, except to the extent permitted by law.

Stranger Owned Life Insurance

(ii) Facilitating a customer's application for a stranger owned life insurance ("STOLI") policy.

STOLI is generally considered to be an act, practice or plan to initiate a life insurance policy in order to obtain a loan, advance or other payment with the intent of transferring the right to receive a death benefit to a third party, usually an investor, who, at the time of policy origination, has no insurable interest in the insured. STOLI is generally not considered to be:

a) Appropriate recourse financing of needed life insurance; or

b) Life insurance purchased by the insured in good faith to meet a personal, business, or charitable need.

ADVISOR MONITORING PROCEDURES

Monitoring should be risk-based and aimed at identifying areas that require greater scrutiny. There is protection in having a "reasonable system" in place to detect problems. This does not mean that all problems will be detected but rather that there are reasonable controls in place. The ultimate goals are to "Know Your Advisor" and be in a position to identify and escalate problems as early as possible, including signs that

- the Advisor lacks expertise in recommending product or services
- the Advisor's patterns of sales including the proportion of business placed with insurers, the type and face amount of insurance sold have changed. For example, according to CLHIA, "for IVIC transactions, the incidence of deferred sales charges, surrenders within six months and excess withdrawals may all be signs of heightened risk."
- an Advisor is holding out in a manner that misrepresents/overstates his/her expertise
- Needs-based selling has not taken place (high lapse rates, poor persistency, low placement rate). Another red flag is "over-concentration." This is difficult to detect when an Advisor splits his business among MGAs. Evidence that an Advisor favors certain insurers exclusively or certain products or concepts should lead the overseer/auditor to review the book, ensuring that the Advisor performs appropriate needs analyses and sales appear to be appropriate.

When you detect serious issues, you are obliged to report to the affected insurers. **See Investigating and Reporting.**

Check licensing and E&O.

- Check Advisor licensing and E&O with each piece of submitted business. This means ensuring that the Advisor is licensed where the customer (owner) resides as well as where the application was signed, so that the Advisor can provide post-sale service without licensing concerns.
- Spot-check both license and E&O in a sampling of the Advisor base at regular intervals to deter and detect situations where Advisors cancel or lose their coverage or licenses.

Monitor for Inappropriate Sales Practices - See Advisor Oversight Checklist (The Advisor Oversight Checklist is an optional tool. It is intended to assist in identifying the risks associated with any advisor and to narrow down the field of concerns. It can be used when you are auditing or closely overseeing an Advisor for any reason, but should be modified to suit the circumstances).

According to CLHIA, **"**The objective is to look for trends in the advisor's business that would indicate that products purchased by clients are not meeting their needs." We cannot oversee Advisors' sales for suitability of advice or product choice, but we can query sales if we have reason to question the appropriateness of the sale, given available facts**.**

Many of the following sales practices are very difficult to detect. However, complaints and the observations by new business and customer service staff can lead to detection. In other instances, spot checks and random reviews may uncover problems. Finally, where detection is difficult, training staff and providing tools to Advisors create reasonable compensating controls.

The list provided below is not exhaustive, nor is the presence of one or several red flags in any sale conclusive evidence of a market conduct problem. Instead, these issues separately or together might indicate problems that bear investigation and perhaps remediation. Certain red flags are noted specifically in the guidance provided in this section, because of the heightened risk associated with them.

While monitoring sales and in-force service, we may identify any of the following:

- **Criminal behavior –** regardless of whether it is in relation to the sale of insurance.
- **Poor needs analysis or failure to assess product-client suitability –** According to CLHIA Guideline G8, "a pattern of poor analysis of consumer needs, or making sales with no regard for the suitability of the product to the consumer. Agents should ensure that they have made a diligent and business-like effort to identify and analyze the consumer's needs, objectives and financial circumstances so that appropriate product recommendations are made to the consumer.
  Fraud – deception intended to mislead which causes another to take an action based on misinformation.
- **Misappropriation of client funds** – theft of funds for personal use.
- **Forgery** – "The creation of a false written document or alteration of a genuine one, with the intent to defraud" (thefreedictionary.com). This includes filling in blank spaces on signed forms. Forgery is one form of fraud.
- **Money laundering** – "Transferring property or proceeds of any property with intent to conceal the true origin and ownership of such property and knowing that all or a part of that property was obtained or derived directly or indirectly as a result of a criminal or drug offense." (CLHIA Guideline G8).
- **Selling without a licence or otherwise violating the terms and conditions of a licence.**
- **Improper use of sales associates and assistants -** (It is important to know what services any sales associates or assistants provide to the Advisor and to determine whether licensing is required, if there is client contact, if the individual fills out any forms required by the insurer, provides advice of any kind to the customer or acts in any other manner that might require an insurance license and appointment).
- **Problems with non-face-to-face selling -** (Selling insurance without personal contact poses some challenges. Unless the Advisor knows the customer and has already verified identification, there are AML requirements that still must be satisfied. The possibility of fraud is also greater. The possibility of poor communications and failure to ensure that the customer understands what is being proposed increase. Finally, there are licensing considerations. The Advisor should be licensed in the province where the customer resides in addition to where the sale was made in order to ensure that ongoing service can be provided without regulatory concerns). Advisors typically do not ask for permission to engage in these types of sales. If it becomes apparent that an Advisor is engaging in regular non-face-to-face selling, contact the Advisor, discuss the methods employed and arrive at an agreed-upon, written process that the Advisor must follow, which addresses licensing, anti-money laundering requirements, privacy considerations and ongoing service considerations. If the insurer requires notification of the arrangement, forward this immediately. Treat anyone who engages in regular non-face-to-face sales as a higher risk and monitor the business closely.
- **Fronting – "**Fronting occurs when a licensed agent submits an application for insurance and collects a commission on behalf of an unlicensed individual who has sold the policy. Fronting also occurs when an advisor places business with a carrier on behalf of a licensed agent who does not have a contract with the

carrier receiving the business." (CLHIA Reference Document on the Role of MGAs). (Check applications and forms for different handwriting and ink, particularly if the signature of the selling agent doesn't correspond with the writing and ink on the rest of the application. Also note when the Advisor's sales are not his usual).

- **Selling without the required liability insurance -** (Because it is possible to cancel an E&O policy at any time, do regular spot checks of licenses and E&O coverage).
- **Breach of privacy or confidentiality laws or rules -** (Watch for evidence of sloppy information management).
- **Violation of holding out laws or rules,** which consists of "intentional misleading of the consumer through business cards, stationery, advertising, or other means, in regard to credentials or designations or authority, or the ability to provide advice or service. (CLHIA Guideline G*). On a risk basis and on a spot check basis, look at websites, LinkedIn and other social media sites, sample business cards. Look for evidence that the Advisor is using non-licensed names or overstating credentials.
- **Failure to disclose a material conflict of interest** (Pay attention to Advisors' outside business activities and target markets and review disclosures and practices of Advisors identified as high risk).
- **Tied selling –** this means making the purchase of one product contingent on the purchase of a second product. It is very rare in traditional insurance sales and is more associated with sales of insurance by banks.
- **Premium rebating and other inducements,** which consists of "making an agreement for premium to be paid for a policy in a lesser amount than the premium set forth in the policy, or paying (or offering to pay) a rebate of the whole or part of the premium stipulated by the policy, or any consideration or thing of value intended to be in the nature of a premium rebate, except to the extent permitted by law. (CLHIA Guideline G8). (Rebating of commissions is allowed in mutual fund sales and generally prohibited by the provinces for insurance sales, so some Advisors may be unaware of or insensitive to the different rules. Rebating is also used to support fraudulent sales. Many insurers do not allow rebating even where it is allowed legally. Treat any advisor who makes a habit of rebating as a higher risk.
- **Undisclosed replacements -** Replacements are a suitability issue and undisclosed replacements represent an effort to avoid detection. Treat these seriously from the first instance.
- **Indiscriminate systematic replacements -** (A replacement rate over 20% should trigger inquiries, since it is likely much higher if the Advisor splits business among MGAs; 30% or more is typically seen as "systematic replacement" and should be investigated. Replacements can be very costly for customers and unless there is a compelling reason for replacement, one would question the appropriateness of the sale. Replacements are and will continue to be a suitability issue and a regulatory hot button).
- **Twisting – "**The act of inducing or attempt to induce a policy owner to drop an existing life insurance policy and to take another policy that is substantially the same kind by using misrepresentations or incomplete comparisons of the advantages and disadvantages of the two policies." This is illegal in most jurisdictions and prohibited by all insurers. (From IRMI Risk and Insurance Glossary). According to CLHIA Guideline G8, twisting consists of "the unethical act of persuading a client to terminate a policy solely for the purpose of selling another policy without regard to possible disadvantages to the client. It can also involve using the values, either through loans or through the re-direction of dividends, of one policy to purchase another.
- **Churning –** creating transactions for the purpose of generating commissions, contrary to the customer's best interests. According to CLHIA Guideline G8, "Churning occurs when an agent, exercising control over the volume and frequency of trades, abuses a client's confidence for personal gain by initiating transactions that are excessive in view of the character of the account and the client's personal objectives. Churning is generally confined to securities and commodities, but can occur with annuity-type contracts as well.

- **Poor disclosure, material non-disclosure, including failure to provide the required written disclosures -** Where red flags or concerns are present, review the Advisor's written disclosure and talk to the Advisor to determine causes).
- **Language barriers and use of unqualified translators -** (Many insurance companies have rules about who can act as a translator in insurance sales because of concerns about conflicts of interest (if the Advisor or a beneficiary of the policy translates), whether the translator is actually qualified to accurately translate complex insurance terms and whether the customer fully understands the recommendations being made. An Advisor who does business in a target market where the MGA does not have the ability to read and understand the customer's language must be treated as high risk).
- **Misuse of, or material changes to, company-provided illustrations** – According to CLHIA Guideline G8, this consists of "unauthorized material changes by an agent to company-provided illustrations, or manipulation by an advisor of software beyond its defined parameters to create an unreasonable expectation. It is expected that all agents will follow CLHIA Guideline G6 on the use of life insurance illustrations. Advisors should present information about a product accurately, honestly, completely and in clear language. All relevant information necessary to enable the client to make an informed decision about insurance needs and the product being recommended should be available.
- **Incomplete comparisons** – CLHIA Guideline G8 defines this as "providing incomplete comparisons of policies with the intent to convince a client to lapse or surrender a policy."
- **Coercion or undue Influence -** CLHIA says "the objective is to look for evidence that an advisor has, through undue influence, persuaded a client to purchase products or services that are not suited to his or her needs. Two common situations that are often associated with vulnerability and undue influence are age and native language. Evidence that an advisor is placing a disproportionate amount of business or a sudden increase in business with either of such groups may be a sign of heightened risk." CLHIA indicates that the presence of a needs analysis is a good mitigant. Pay attention to Advisors who claim special credentials for dealing with the elderly, or who seem to specialize in these sales. The reputation risk associated with any abusive practices is very real. Be alert to possible predatory or coercive sales practices.
- **Inappropriate leveraging -** Look for financial fact-finding documentation. Under the CAILBA Advisor Code of Conduct, an Advisor may recommend leveraging only when it is appropriate to do so. See the Code for details. Treat anyone who recommends leveraging regularly as a high risk, since E&O carriers report that leveraging is a source of a significant percentage of claims made against advisors.
- **Material misrepresentation or omissions** when presenting information to a prospect or customer.
- **Misleading statements to an insurer.**
- **Incompetence –** this can be evidenced by such things as ongoing problems completing applications and other requirements and failure to understand products or identify and highlight risks inherent in recommendations.
- **Lack of trustworthiness -** Untrustworthiness seems like a catch-all category but in fact, it is very common to find that an accumulation of even small offenses over a period of time leads to the view that an Advisor is not trustworthy. You must report all contract terminations for cause where the reason is untrustworthiness.
- **Commission-sharing with an unlicensed individual -** Non-compliant commission-sharing can indicate fronting or other forms of fraud as well as inappropriate compensation for referrals. Remember that referral arrangements should consist of a flat fee paid for each lead or prospect, regardless of whether a sale eventually occurs. These payments cannot be contingent upon a sale and cannot be a percentage of the commission earned unless the payment is being made to another licensed individual. Any effort by an Advisor to convince you to pay commission out where it does not appear to be warranted should be investigated.

- **Unnecessary delay in delivering policies or failure to deliver policies -** These situations are often uncovered through consumer complaints. Be aware of the costs associated with non-delivery of policies.
- **Trafficking in insurance policies, where prohibited by law -** Also known as Stranger Owned Life Insurance ("STOLI"), Investor Owned Life Insurance ("IOLI"), Life Settlements or Viatical Settlements, the purchase of new or existing insurance contracts by individuals and entities that have no connection to or insurable interest in the insured is generally prohibited. According to CLHIA, MGAs should bear in mind that the policies of individual life insurers in Canada as they relate to viaticals are generally more restrictive than statutory prohibitions. **Watch for Advisors who**
    - specialize in the sale of one type of product, which is then converted to another shortly after sale
    - have constant change of ownership requests for customers

      are the subject of gossip by other Advisors, who may have been approached to join in the "program," since so many of these incidents have been detected by word of mouth.
- **Poor file management and record-keeping -** Be on the lookout for Advisors who can't demonstrate that they consistently do things a certain way. Keep in mind the following:
    - Customer files should contain enough information to demonstrate that a needs-based sale took place. Files should contain copies of the material that (or detailed notes on what) was provided to the customer. If the file is not complete, ask whether material was provided and why it was not retained. Flag any Advisor who has demonstrated poor file maintenance for a follow up review.
    - Files should be exclusively insurance files, so if you find that dealer material is merged into some Advisors' insurance files, this should be flagged.
    - For privacy purposes, if more than one insurer's application is taken, separate files should be maintained. Insurers performing audits should not have access to other files.
    - Agent files should never contain original insurance policies. These must be provided to the customer immediately upon receipt.
    - While Advisors are required to verify client ID in keeping with federal AML laws, unlike the rules around the sale of mutual funds, there is no requirement to retain actual copies of the customer's personal ID in insurance files. Much of the information contained on that personal ID must be retained, however.
    - Look for records that are overdue for destruction.

Monitor Segregated Fund and Other Investment Product Sales

Needs assessment is required for segregated funds because they are life insurance products. When reviewing segregated fund sales, you should be able to find the reason why the customer purchased an insurance-based product rather than some other investment. Given the large market for these products and the manner in which they are sold, rather than attempting to establish "suitability" when you review, it is much easier and more productive to be on the lookout for inherently inappropriate or unsuitable sales.

In Saskatchewan, an approved investment funds course must be taken before an Advisor can sell segregated funds and an Advisor with less than two years' experience must be supervised by a more senior Advisor, which includes oversight of segregated fund sales. Watch out for 2 additional problems:

- **Parking funds in Money Market during the free look period or deferring an initial investment allocation -** If there are any complaints or other evidence that an Advisor does not have a good system for ensuring that money is moved out of Money Market as soon as the free look period ends or for ensuring that the customer makes a decision on where to place the funds, the matter should be investigated thoroughly. This is a surprisingly common and very expensive error.

- **Evidence of market timing -** Market timing is as inadvisable in segregated funds as it is in mutual funds. Unfortunately, there is no clear rule against market timing in segregated funds. Evidence of market timing should be thoroughly investigated and dealt with regardless. Be on the lookout for Advisors whose books contain numerous limited powers of attorney that allow them to move substantial blocks of money among segregated funds

Ongoing Oversight of Advisor "Financials" including:

- Garnishments
- Conservation/persistency
- Debt
- Bankruptcy or insolvency.
- Urgent or repeated calls for commission payment or advances.

Monitoring an Advisor's financial status can be a way to detect when an Advisor might be "going off the rails." It is also generally easier to detect financial difficulties than to detect some unacceptable sales practices. Having financial problems can make some Advisors prone to some unacceptable sales practices including undisclosed conflicts of interest, failing to do needs-based selling and becoming the target of money launderers and other fraudsters. It is important to distinguish between financial problems that arise as a result of improper sales practices and those that arise as a result of such things as marital breakup, but financial problems, regardless of cause, can lead some Advisors into problems with customers and insurers. Treat anyone whom you detect as having financial difficulties as a high risk and discreetly but consistently monitor the sales and service practices.

Additional Financial Monitoring Procedures

- Retain a vendor to provide ongoing reports on an Advisor's status.
- Request credit checks on all existing Advisors
  - when they request a contract with a new insurer, or
  - when their licenses are renewed, or
  - annually.
- Request retail reports on already-contracted Advisors when concerns arise.

Suggested Policies and Procedures for insolvent advisors

- Do not offer contracts to insolvent Advisors or those with a history of bankruptcy and poor financial practices.
- Order a credit check on all Advisors seeking contracts and a yearly credit check on your existing Advisors.
- Where you identify concerns about an Advisor during the course of monitoring, order a credit check.
- Make compliance with the CAILBA Advisor Code of Conduct a contract condition and ensure that Advisors know that they must inform you immediately if they make a consumer proposal or file for bankruptcy.
- Train staff to recognize and escalate situations that demonstrate an Advisor may be in financial difficulty.
- Notify the carriers as soon as you become aware that an Advisor has made a consumer proposal or declared bankruptcy.

Other Concerns

According to CLHIA, “there are a number of intangibles that relate to the advisor's overall ability to provide professional advice. Some of these indicators may relate to business practices (e.g., being slower to respond to requests) or knowledge of insurance (e.g., asking questions about matters of basic understanding). Similarly, changes in mood, physical appearance, engagement and the like may be evidence of more serious problems.” Escalate these concerns to insurers as soon as you recognize that they are not temporary and that they represent an Advisor suitability issue.