

**RISK FINANCING
CANADIAN SUPPLEMENT**

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March 2004**

Introduction and Foreward

Risk Financing – Canadian Supplement

The Canadian Risk Management Diploma is an educational diploma sponsored and issued by the Risk and Insurance Management Society (RIMS). The course texts which are currently utilized discuss material from a U.S. perspective.

The following supplements are intended to augment and replace certain portions of the Insurance Institute of America's ARM 56 texts (© Insurance Institute of America) with Canadian material for those subject areas where practices, legislation and regulation differ between the two countries.

Over the time that the designation has been offered in Canada, a desire for Canadian content has emerged. While in a perfect world, a Canadian textbook would be the ideal, the following supplements are intended to augment and replace certain portions of the Insurance Institute of America's texts with Canadian material for those subject areas where practices, legislation, and regulation differ between the two countries.

Instructors and students may choose to read the supplemental material as a stand alone volume or they may choose to specifically replace sections of the U.S. based material in the applicable Canadian supplemental section(s). For the ease of the instructor or student, the material is cross-referenced to the texts both in a cross referencing guide and at the beginning of each supplement section.

While the material is Canadian, it is acknowledged that practices and legislation may vary in each province or territory. Sources for additional material are provided to assist the instructor and the student locate additional information specific to their geographical region.

Finally – things change. The author and those who reviewed the draft have taken steps to ensure that the material is current at the time of writing, but readers are cautioned that there may be a “best before” date limitation on the material in the supplements.

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Vancouver, B.C.
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Risk Financing – Canadian Supplement

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Overview of the Financial Services Sector and its Regulation in Canada

This section is in addition to “*Convergence of Insurance with Other Financial Services*”, pp. 1-23 & 1-24 and replaces “*Regulatory and Accounting Issues*”, pp. 11-30-11-32, *Risk Financing*;

Regulation & Solvency

The Canadian federal government and the provinces and territories share jurisdiction over insurance regulation in Canada. Property and casualty insurers can be incorporated under either level of government, depending on the areas in which they operate and their ownership. The federal government supervises approximately 75% of property and casualty insurers, and currently there are 190, for which the federal government is responsible.

Federal authorities look after the solvency of companies incorporated federally as well as Canadian branch operations of firms incorporated outside Canada. Provincial and territorial authorities are responsible for the solvency of provincially incorporated insurers, for reviewing and interpreting insurance contracts, and for licensing and supervising agents and adjusters.

The Department of Finance Canada is responsible for advice to the federal government on the economic and financial affairs of Canada. It oversees all government initiatives affecting the economy and monitors external factors that may have a bearing on domestic economic performance.

Applicable Legislation

The Finance Minister is responsible to Parliament for statutes respecting insurance and financial services, including:

- *Bank Act*
- *Bank of Canada Act*
- *Co-operative Credit Associations Act*
- *Financial Administration Act*
- *Income Tax Act*
- *Insurance Companies Act*
- *Office of the Superintendent of Financial Institutions Act*
- *Trust and Loan Companies Act*

Incorporation of insurance companies and financial institutions is also the subject of the *Canada Business Corporations Act*.

Canada’s federally regulated financial institutions are governed by four separate acts – *The Insurance Companies Act*, *The Trust and Loan Companies Act*, *the Bank Act*, and *the Cooperative Credit Associations Act*. In general, the legislation is such that banks and central credit unions are precluded from selling insurance to the public from their banking operations and their acquisition and ownership of insurance companies is controlled and monitored. Provincially regulated credit unions have fewer restrictions imposed upon such operations.

Incorporation of Insurers

With respect to insurance companies, a company wishing to incorporate under the *Insurance Companies Act* must apply for letters patent according to a defined process. The authority to incorporate a federally registered insurance company rests with the Minister of Finance, however, in practice this is granted upon recommendation of the Superintendent of the Office of the Superintendent of Financial Institutions (OSFI), the federal regulatory body.

Criteria are established, including minimum capital required, a sound business plan, the owner's track record in the financial services sector, and management skills. A foreign company must also have at least a 5 year successful track record in its home country, proven expertise and an acceptable corporate name. In addition, the provinces and territories must sign off on the marketing plan and the proposed product range, and a chief agent and an actuary, both Canadian residents, and a Fellow of the Canadian Institute of Actuaries (FCIA) must be appointed.

There are regulations governing who may own shares in the company, and companies must be widely held once they get to a certain size, as defined in terms of overall equity. Additional rules apply if the acquirer is a financial institution or if the acquirer is a related company.

Insurance companies must have a minimum of seven directors, with a stipulated number of resident Canadians. Directors are responsible to establish policies related to investments and lending.

Prescribed Activities

Property and Casualty insurers are limited by regulation to a list of "prescribed activities" in addition to the insurance business. These include:

- Provision of safety and risk prevention services
- Services respecting risk management and claims adjustment
- The operation of rehabilitation and training and development centres
- The provision of computer systems to independent insurance brokers and agents
- The provision of support to independent insurance brokers and agents
- The operation of repair and appraisal centres
- Other activities that are reasonably ancillary to the business of insurance carried on by the property and casualty company.

Solvency and Adequacy of Capital

The current legislative minimum capital requirement for the incorporation of domestic insurance companies (both life and property and casualty) is \$10 million. Insurers must satisfy regulators that their policy reserves are sufficient to meet the anticipated requirements of their policyholders. In addition, they must satisfy capital requirements, which is expressed as a minimum percentage by which assets must exceed liabilities. OSFI administers the Minimum Asset Test for federally regulated insurers as well as the Dynamic Capital Adequacy Test (DCAT) which is a formal approach to test the financial strength of the company by projecting its future financial condition under various possible sets of scenarios. It is a risk based approach.

The new test gives greater weight to an insurer's risks in terms of assets, policy liabilities and off-balance sheet exposures, with capital available expressed as a percentage of capital required. The minimum level is 150%.

Canadians are permitted to purchase insurance from insurers not licensed in Canada, however, the extent to which these unlicensed insurers can solicit business in Canada is strictly limited and monitored. In addition, there are additional tax regulations applicable to the purchase of non-admitted insurance.

The Insurance Industry's Role and Consumer Protection

The *Insurance Companies Act* also governs the amounts and types of reinsurance permitted for Canadian regulated insurance companies. The regulations also prescribe the maximum percentage of reinsurance for Canadian regulated insurers, who may not reinsure more than 75% of the risks insured by policies they have issued. In addition, companies may not reinsure more than 25% of their risks with non-approved reinsurers.

The Property and Casualty Insurance Compensation Corporation (PACICC) provides protection to many Canadian policyholders against insurer insolvency. PACICC has guaranteed most insurance policies in Canada since 1988, and PACICC membership is required in all Canadian jurisdictions. The company has a reserve fund of approximately \$30 million and has the power to levy assessments on its members, should an insolvency occur. Foreign insurers with branches in Canada must vest assets in Canada to ensure policyholder protection.

The property & casualty insurance industry in Canada represents more than \$20 billion in premiums. In addition, government owned corporations operate automobile insurance schemes in Quebec, Manitoba, Saskatchewan and British Columbia. These entities earned an additional \$4.1 billion in premiums, or about 27.7% of the Canadian automobile insurance market. In B.C., Saskatchewan, and Manitoba, both collision and third party liability insurance is provided. In Quebec, the government provides only third party liability insurance.

There are just over 200 insurers in active operation in Canada. Foreign owned insurers account for about two-thirds of net premiums earned, and about 16% of net premiums are written by mutual companies, owned by their policyholders.

About 30,000 people are employed by primary insurers in Canada. Insurance intermediaries such as agents, brokers, claims adjuster, appraisers, and other professionals employ over 60,000 people.

Since policies are generally subject to renewal every year, insurance companies generally match their liabilities by investing in short-term, highly liquid investments. About 40% are in non-investment assets such as real and fixed assets, affiliates, accounts receivable, less than one year term deposits, cash and other) and the remaining portion is invested in government and corporate bonds, common and preferred shares, and mortgages.

In 2001, federal legislation reforming the regulatory framework governing the financial services sector (Bill C-8) was proclaimed. The legislation provides for the creation of the Financial Consumer Agency of Canada to enforce the consumer oriented provisions of the federal financial institution statutes. It also requires P & C insurers to be members of a third party dispute resolution system to handle the complaints of consumers and small business regarding their interaction with property & casualty insurance companies.

This new framework maintains the practice of reviewing the regulatory framework every 5 years, to ensure that things are kept up to date.

The Canadian provinces and territories each have legislation which covers the issuance of insurance contracts. The *Insurance Act* and regulations in each province and territory also stipulate the requirements for licensing of adjusters and insurance brokers and agents. Each geographical area has a Superintendent of Insurance or equivalent position, responsible for insurance regulation within the jurisdiction.

While provincial and territorial governments also regulate the solvency of insurers that operate within their boundaries, regulations largely mirror those of OSFI.

Workers' Compensation in Canada – Historical Origins

This section is in addition to “*Workers Compensation and Self-Insurance*” p. 3-5; “*Workers Compensation and Employers Liability Insurance*” pp. 4-16 – 4-17, “*Regulatory Requirements*” pp.7-10 – 7-11 *Risk Financing*.

Workers' compensation schemes have their origins in Germany, Great Britain and in the United States in the late 1800s and early 1900s.

Workers' compensation in Germany was the expression of a new social principle that was traceable to the early Germany labour and trade guilds, which provided disability, sickness and death benefits, with both contributions and administration shared equally by employers and employees. Chancellor Otto Von Bismarck proposed and passed a number of pieces of social legislation between 1884 and 1886 - among them was a compulsory state run accident compensation system financed by both employers and workers.

In Great Britain early jurisprudence in the 1800s made it almost impossible for workers to succeed in law suits against their employers in contract or in negligence. There were practical difficulties for any worker pursuing litigation - paying for his/her medical treatment; securing and paying legal counsel; and finding the necessary funds to survive while waiting for an offer of settlement or a judgment.

The first attempt to deal with these obstacles was undertaken in 1880 with the Employers' Liability Act in Great Britain and in 1886 with the misnamed Workmen's Compensation for Injuries Act of Ontario. Both these laws were still essentially employer liability acts and success still depended ultimately on the finding of fault.

Canada had moved from a primarily agricultural society with forestry and mining activities centered in northern and near northern parts of the country, to a mixed urban industrial, rural and resource-based society. With this shift, there were significant implications for the health and safety of workers and concern about this focused attention not only on compensation for injuries and diseases that were work related, but on measures to attempt to address the emerging health and safety issues.

The first Workmen's Compensation Act in Great Britain was passed in 1897. It placed full responsibility on individual employers to compensate their own workers for work-related injuries. The law was very limited in its application and benefits were very low - but it did prohibit employers from contracting out of its provisions. The common law, with some assistance from the 1880 Employers' Liability Act, continued as an alternative, permitting a worker to sue for damages rather than accept compensation under the 1897 Act.

Meanwhile, in the United States, strong support for no-fault workers' compensation was growing and several state legislatures enacted compensation legislation between 1908 and 1915. Some of these statutes, notably the State of Washington's Compensation Act, set up exclusive state-managed compulsory systems based on collective liability. The majority of states, however, were either served by private insurers or by a combination of the two and there were a number of large self-insurers.

The premier of Ontario, James Pliny Whitney, appointed Mr. Justice William Ralph Meredith, later Chief Justice of Ontario, to head a Royal Commission that was to study workers' compensation schemes and to make recommendations to the government of the day.

The scheme proposed by Mr. Justice Meredith was one in which workers gave up the right to sue their employers - a right that was contingent upon their ability to prove negligence - and, in return, they were guaranteed protection against income loss due to industrial injuries and diseases, irrespective of fault.

The scheme was to be publicly administered, compulsory, and, with the exception of a few large enterprises (notably various levels of government), was to be a collective liability system with payments secured by an Accident Fund. There were provisions to promote health and safety in the workplace and coverage for medical costs, the addition of merit rating, and the introduction of vocational rehabilitation followed very rapidly.

Meredith's view was that "the amount of compensation should have relationship to the earning power of the injured workman" - in other words, it was to be a wage-loss system. The final report was submitted in 1913 and in the spring of 1914 the Act was introduced into the Ontario legislature, received Royal Assent on May 1 and came into force on January 1, 1915. Legislation was enacted in the remaining provinces and territories over the next 60 years.

The one major shift in direction that occurred early on was in the area of permanent partial disability benefits. The Ontario Board, along with other boards throughout the country, came to believe that a compensation system that did not permit any financial recognition of the permanent clinical impairment an individual might have, regardless of his/her earnings capability, produced some unsatisfactory results.

Boards across the country moved to the use of schedules which presumed wage loss based on the nature and degree of the injury regardless of the real impact of the impairment on one's earnings.

Other changes that took place between 1915 and the late 1960s across North America consisted mainly of updating and fine-tuning legislation. Benefits levels were raised - usually to 75% of gross earnings - and the 1960s saw the addition of the term "disablement" added to the definition of accident in order to ensure the compensability of accidents in which there were not 'chance events'. This was to make it quite clear that injuries that developed over time were to be compensated so long as they were work related.

In the early '70s, the British Columbia board moved to an "either/or" system with the worker being given the option of taking either an impairment rating award or a projected loss of earnings award. From the late 1970s through the early 1990s the majority of the boards moved to an earnings-loss system, usually based on 90% of net income, with an additional award being given for the non-economic impacts of the permanent impairment - an impairment award for loss of enjoyment of life. This became known as the "dual award" system. More active and much earlier intervention in vocational rehabilitation and medical rehabilitation have been emphasized in policy and in some legislation, and three provinces have introduced the concept of a time limited right to return to the former employer so long as the worker is able to perform the essential duties of the job or is able to perform some other suitable work.

The structure of most boards has changed, either through policy or through legislation - there is now usually an independent Board of Directors made up of representatives of workers, employers and the public. Different appeal structures have been established with the majority being independent external boards of appeal. These new appeal processes serve to impose an important discipline and accountability on the boards' policy-making and adjudication practices. Some provinces have made provisions for worker and employer advisors to ensure that there is informed representation before adjudicative bodies.

Workers Compensation in Canada today

Today, all 10 provinces and 3 territories have Compensation Boards or Commissions which deal with worker injury compensation, rehabilitation, occupational health and safety, and injury prevention.

Regulation of these boards and commissions falls within provincial/territorial jurisdiction, with the exception of Canadian federal government employees, who fall within the scope of the *Government Employees Compensation Act*. These employees make claims to their provincial boards or commissions, but the actual costs and associated administrative fees are paid by the Government of Canada to the applicable board or commission.

Although there are slight variations in the acts and regulations in each jurisdiction, there are some common principles:

- 1) Compensation is based on a “no-fault” system, where liability of employer and worker does not impact the benefits payable to a worker.
- 2) The plans provide compensation for loss of earnings, medical care, and other related benefits such as lump sums or pensions (in the case of permanent disability) as a result of occupational injuries and diseases.
- 3) Workers who are covered by the scheme generally do not have the right to opt out of the compensation and sue their employer.
- 4) Negligence on the part of the employer may result in fines, specific orders for corrective action, and the board or commission may subrogate from a negligent employer or negligent third party to recover claims paid to an injured worker.

There are reciprocity provisions in the various provincial acts, so that workers who temporarily work outside of their jurisdiction remain covered. The agreements stipulate that workers who work outside of their province of normal work are covered by the authority in their own jurisdiction when working outside of the jurisdiction for up to six months. Workers on extended absence from Canada may need private coverage. Each country has different regulations.

Most employers are required to register with and pay premiums to their respective board or commission. Some exceptions include: volunteer workers and certain categories of self-employed persons.

Funding of Workers' Compensation Boards and Commissions

Premiums are collected from employers on the basis of a percentage of payroll, subject to a maximum compensable annual salary per worker. Each industry has an applicable premium rate, and in many cases the base rate is discounted or surcharged based on that employer's previous loss experience, relative the loss experience of other peer employers in that industry.

All boards and commissions across Canada use some type of retrospective premium rating system, that is, that premiums for the coming year are based on loss history from the previous year(s).

In most jurisdictions, a general contractor or owner may be liable for unpaid premiums of a sub-contractor. It is therefore very important for a general contractor or owner to request a "Clearance Letter" prior to and during services being performed by a sub-contractor to ensure that they do not incur these unexpected costs.

Because there may be an exposure to liability for employers who may be responsible for uninsured sub-contractors or workers from outside Canadian jurisdictions, most Canadian general liability insurance policies include a coverage extension for contingent employer's liability. This endorsement responds where workers' compensation is non-existent or inadequate.

There has been concern and media attention expressed in regards to unfunded liabilities of workers compensation boards and commissions across the country. This has caused many of the boards and commissions to review the adequacy of rates, and in some cases, to change their organizational structure to allow for more transparency of operations.

Rating

Each provincial or territorial authority establishes rating classifications and rates. Sample classes for the purpose of assessment in British Columbia are shown for illustrative purposes:

- Class 1: Primary Resource
- Class 2: Manufacturing
- Class 3: Construction
- Class 4: Transportation and warehousing
- Class 5: Trade
- Class 6: Public services
- Class 7: General Services
- Class 8: Specific provincially regulated airlines, hotels, railways and mining companies
- Class 9: U.S. Owned Railways
- Class 10: Federally regulated railways and airlines
- Class 11: Provincial Crown Corporations and Provincial Government Employees

"The Board classifies all employers and independent operators into classification units. Not all classification units are large enough to have the financial credibility to stand alone for assessment rate making purposes; they must be grouped together to provide an adequate insurance base.

Employers and independent operators are assigned to classification units on the basis of the industry in which the firm is operating. In assigning the classification, some of the factors considered are: the type of product or service being provided, the processes and equipment that are used, and the type of industry with which the firm is in competition. Occupations of individual workers may be reviewed when assigning the classification, but only as an indicator of the type of industry being carried on.

The classification system is based on the principle that the cost of producing a product or providing a service includes the cost of injuries or diseases incurred by the workers doing the work. The system is based on industrial undertaking rather than on occupation or hazard. If a specific product is being manufactured, the classification is the same, regardless of whether the manufacturing is done by the employer's workers or subcontracted out to another firm. A classification therefore includes all occupations within the industry, including officer or clerical staff."

Source: Workers' Compensation Board of B.C. Assessment Manual: Revised March 2003.

References:

Alberta

WORKERS' COMPENSATION BOARD OF ALBERTA
P.O. Box 2415
9912-107 Street
Edmonton AB T5J 2S5

http: www.wcb.ab.ca

British Columbia

WORKERS' COMPENSATION BOARD OF BRITISH COLUMBIA
P.O. Box 5350
Vancouver BC V6B 5L5

http: www.worksafebc.com

Manitoba

WORKERS' COMPENSATION BOARD OF MANITOBA
333 Broadway
Winnipeg MB R3C 4W3

http: www.wcb.mb.ca

New Brunswick

WORKPLACE HEALTH, SAFETY AND COMPENSATION COMMISSION
1 Portland Street
P.O. Box 160
Saint John NB E2L 3X9

http: www.whscc.nb.ca

Newfoundland & Labrador

WORKPLACE HEALTH SAFETY AND COMPENSATION COMMISSION
146-148 Forest Road
P.O. Box 9000, Station B
St. John's NF A1A 3B8

http: www.whscc.nf.ca

Northwest Territories and Nunavut

WORKERS' COMPENSATION BOARD OF THE NORTHWEST TERRITORIES AND
NUNAVUT

P.O. Box 8888
Yellowknife NT X1A 2R3

http: www.wcb.nt.ca

Nova Scotia

WORKERS' COMPENSATION BOARD OF NOVA SCOTIA

5668 South Street
P.O. Box 1150
Halifax NS B3J 2Y2

http: www.wcb.ns.ca

Ontario

WORKPLACE SAFETY AND INSURANCE BOARD

200 Front Street West
Toronto ON M5V 3J1

http: www.wsib.on.ca

Prince Edward Island

WORKERS COMPENSATION BOARD OF PRINCE EDWARD ISLAND

14 Weymouth Street
Charlottetown PEI C1A 4Y1

http: www.wcb.pe.ca

Quebec

COMMISSION DE LA SANTÉ ET DE LA SÉCURITÉ DU TRAVAIL

1199, rue de Bleury
C.P. 6056, Succursale «centre-ville»
Montréal QC H3C 4E1

http: www.csst.qc.ca

Saskatchewan

WORKERS' COMPENSATION BOARD OF SASKATCHEWAN
200, 1881 Scarth Street
Regina SK S4P 4L1

http: www.wcbsask.com

Yukon

YUKON WORKERS' COMPENSATION HEALTH & SAFETY BOARD
401 Strickland Street
Whitehorse YK Y1A 5N8

http: www.wcb.yk.ca

British Columbia Captive Insurance Companies

This section is in addition to “*Captive Insurance Plans*”, pp. 3-18-3-21 and Chapter 9, *Risk Financing*.

Overview of the British Columbia Captive Legislation

In 1987, British Columbia became the first Canadian province to enact legislation for the creation of domestic captive insurance companies. The Insurance (Captive Company) Act is a relatively brief and extremely flexible statute incorporating, by reference, sections from other British Columbia statutes, including the *Company Act*, the *Insurance Act* and the *Financial Institutions Act*.

Three types of captives are permitted:

The Pure Captive

The Pure Captive, or the single parent captive, may insure the risks of its parent, its parent's affiliated corporations (majority owned) and their officers, directors, employees, agents or independent contractors.

The Association Captive

The Association Captive may insure the risks of the members of an association (that has been in existence for over one year), their affiliates, and their officers, directors, members, agents or independent contractors.

The Sophisticated Insured Captive

The Sophisticated Insured Captive is intended to cover a group of insureds who may be unrelated except for their participation in the captive. Where groups of companies do not qualify for a Pure Captive, not being majority owned, the Sophisticated Insured Captive can be utilized. Each member of the group must spend a minimum of CDN \$500,000 in annual premiums and must have "expertise" in insurance matters. The Sophisticated Insured Captive may insure the risks of the group, their affiliated corporations, and their officers, directors, employees, agents or independent contractors.

B.C. captives may write any line of insurance business within the meaning of the Insurance Act except:

- a. Surety insurance, other than reinsurance of surety insurance,
- b. Insurance of motor vehicles, other than fleet insurance by a corporation.

The intent of the legislation is that B.C. captives only insure the risks of their owners and not the risks of the general public.

Regulatory Environment

B.C. captives operate within a provincially regulated climate, with minimal government intervention. Licensing is a relatively simple, speedy process with annual renewals. The regulators review standard indicators of solvency and performance; however, there are no statutory solvency or performance measures that must be met. This approach evaluates each captive on its merits and allows flexibility.

Captive insurance companies formed under the Insurance (Captive Company) Act are given latitude in the scope of allowable investments. There are no set limits, and the regulators examine the portfolio of each captive for prudence in its own unique circumstances.

The minimum level of capitalization for B.C. captives is CDN \$200,000. The amount of capital required is dependent on the insurance program being written, and larger programs will require a larger amount of capital. In addition, the minimum level of reserves to be maintained after initial registration is Cdn \$100,000.

There are fifteen captive insurance companies currently operating in British Columbia.

Fronting

A B.C. captive is a licensed insurance company in the Province of British Columbia. The fact that other provinces do not recognize a B.C. captive as being a licensed insurer presents no more of a problem than it would to a captive domiciled outside of Canada.

In order to reduce uncertainty surrounding regulatory issues faced in these situations, most captive programs that extend outside of British Columbia are 'fronted'. This means that a licensed insurance company is used to issue the policy to the insured, and a reinsurance agreement is entered into between the licensed insurance company and the captive. The fronting company can, and in most cases does, provide other services to the insured, such as loss adjusting and reporting, policy issuance, and assistance in premium rating. The fronting company can also participate in the program as an excess insurer, providing insurance above the limits that the captive wishes to retain for its own account.

For U.S. exposures, a B.C. captive would be considered a non-admitted carrier and would be in the same position as any other captive in the eyes of the various state regulators. Therefore, to avoid regulatory problems, it is advisable to front U.S. exposures.

Fronting services come at a cost, which typically varies from 5% to 12% of the gross premium. It may be possible for the captive to write direct policies covering risks domiciled in other provinces; however, this is subject to some degree of uncertainty. The operating protocol of the captive must be designed and followed with the utmost care and attention. If a program is written direct, the other services typically provided by a fronting company must still be obtained, and the applicable costs taken into account.

If there are significant exposures in the Province of British Columbia, there is a distinct advantage to a B.C. captive as that portion of the policy that applies to British Columbia risks can be written direct by the captive, and fronting fees would not apply to the premium attributable to those risks. In practice, most captive programs are fronted, irrespective of where the captive is domiciled.

Auto Insurance in Canada

This section is in addition to “*Business Auto Insurance*”, p. 4-16 *Risk Financing*; Chapter 12, *Essentials of Risk Financing Vol. 2*.

In Canada, individual provinces and territories prescribe the regulations and conditions applicable to the selling of auto insurance.

Provinces and territories utilizing private insurance:

- Alberta
- Ontario
- Yukon
- Northwest Territories
- Nunavut
- New Brunswick
- Nova Scotia
- Prince Edward Island
- Newfoundland and Labrador

Provinces and territories utilizing a combination of government and private insurance

- British Columbia
- Saskatchewan
- Manitoba
- Quebec

In British Columbia, Saskatchewan and Manitoba, the government insurer provides the basic/required minimum auto insurance policy and private and government insurers both sell enhancements or top-ups to the basic policy. In Quebec, injury claims are covered under a government compensation scheme; automobile and property damage claims in Quebec, and bodily injury claims arising from accidents outside Quebec, are covered by private insurers. In the provinces and territories which are served by private-sector insurance companies, all automobile insurance policies contain standard terms and conditions. Each provincial or territorial government, however, sets its own minimum limits for the amount of liability coverage that drivers must buy and its own standards.

Car insurance coverages and policy conditions are legislated by the government in each province and territory. However, there are numerous choices of limits, deductibles and optional coverages available so coverage can vary between individual insured persons. Although there are differences in rules and coverages among provinces, the basic principles remain the same. There are also agreements between governments which may alter the settlement process.

In those provinces where government insurers provide the basic compulsory coverages, insured persons do not receive a printed policy; the vehicle registration itself is evidence of insurance. If additional optional coverage is purchased from private non-government insurers, an extension policy will be issued.

British Columbia

Since 1974, the Insurance Corporation of British Columbia, (ICBC) has been providing basic Autoplan coverage (compulsory insurance) for all motor vehicles licensed and insured in the province. A valid license plate number is the policy number.

Basic Autoplan coverage provides five main types of coverage:

- Third party legal liability coverage (basic \$200,000)
- No-fault accident benefits
- Underinsured motorist protection
- Hit and run/and uninsured motorist coverage
- Inverse liability coverage

Optional higher limits of coverage and physical damage coverage are available.

Saskatchewan

Saskatchewan Government Insurance (SGI) was created in 1945 and operates the province's compulsory auto insurance program.

The insurer provides compulsory third party liability coverage of \$200,000 (with optional higher limits) and a choice of no-fault or tort injury benefits coverage.

Up until 1995, a tort system for injury coverage was in place. In 1995, the program introduced an option for no-fault coverage, and offers customers a choice of tort or no-fault schemes. Under the tort scheme, injured drivers may sue for pain and suffering and for non-defined benefits. People who do not own vehicles may make a choice and the default choice is no-fault.

Physical damage coverage and optional higher limits of liability coverage are available from the corporation and private insurers.

Manitoba

Manitoba Public Insurance is a provincial crown corporation which has provided compulsory third party liability coverage since 1971.

The program provides basic third party liability coverage of \$200,000 with optional higher limits.

The program provides personal injury protection for all Manitoba residents, whether they own the vehicles or not. The most current plan is a no-fault scheme and was introduced on March 1, 1994. There are defined benefits with an option for extra income protection.

Physical damage coverage is available from MPI and from private insurers.

Quebec

Victims of auto accidents resident in Quebec are compensated by the government insurer, the Société de l'assurance automobile du Québec, whether or not the accident occurs in Quebec. Injured drivers may not sue for pain and suffering or for amount in excess of no-fault benefits.

Accident victims who do not reside in Quebec are entitled to compensation only to the extent that they are not responsible for the accident, unless otherwise agreed between the Société de l'assurance automobile du Québec and authorities of the victims' place of residence; additional compensation may be available from their own insurers.

The compulsory minimum limit of third party liability coverage required in the province is \$50,000 with respect to property damage claims within Quebec and to personal injury and property damage claims occurring outside of Quebec.

Alberta

Coverage in Alberta is provided by private insurers. \$200,000 is the statutory minimum third party liability limit required and is available for any one accident; however, if a claim involving both bodily injury and property damage reaches this figure, payment for property damage would be capped at \$10,000.

Claimants have the right to sue for pain and suffering and for economic loss in excess of no-fault benefits.

Northwest Territories/Nunavut

\$200,000 is the statutory minimum third party liability limit required and is available for any one accident; however, if a claim involving both bodily injury and property damage reaches this figure, payment for property damage would be capped at \$10,000.

Claimants have the right to sue for pain and suffering and for economic loss in excess of no-fault benefits.

Ontario

Coverage in Ontario is provided by private insurers. \$200,000 is the statutory minimum third party liability limit required and is available for any one accident; however, if a claim involving both bodily injury and property damage reaches this figure, payment for property damage would be capped at \$10,000.

Medical payments are mandated at \$100,000/person (\$1 million if injury "catastrophic"), including rehabilitation, excluding health insurance plans; attendant care \$72,000 (\$1 million if injury "catastrophic").

Claimants have the right to sue for pain and suffering if the injury meets certain defined thresholds; however a deductible applies. Lawsuits are allowed only if injured person dies or sustains "permanent serious" disfigurement and/or impairment of important physical, mental or psychological function; the court is directed to assess damages, then deduct \$15,000 (\$7,500 if Family Law Act claim).

Claimants have the right to sue for economic loss in excess of no-fault benefits; the injured person may sue for 80% of net income loss before trial, 100% of gross after trial; also for medical, rehabilitation and related costs when the injury is catastrophic.

New Brunswick

Coverage in New Brunswick is provided by private insurers. \$200,000 is the statutory minimum third party liability limit required and is available for any one accident; however, if a claim involving both bodily injury and property damage reaches this figure, payment for property damage would be capped at \$20,000.

Claimants have the right to sue for pain and suffering and for economic loss in excess of no-fault benefits.

Nova Scotia

Coverage in Nova Scotia is provided by private insurers. \$200,000 is the statutory minimum third party liability limit required and is available for any one accident; however, if a claim involving both bodily injury and property damage reaches this figure, payment for property damage would be capped at \$10,000.

Claimants have the right to sue for pain and suffering and for economic loss in excess of no-fault benefits.

Prince Edward Island

Coverage in Prince Edward Island is provided by private insurers. \$200,000 is the statutory minimum third party liability limit required and is available for any one accident; however, if a claim involving both bodily injury and property damage reaches this figure, payment for property damage would be capped at \$10,000.

Claimants have the right to sue for pain and suffering and for economic loss in excess of no-fault benefits.

Newfoundland and Labrador

Coverage is provided by private insurers in Newfoundland and Labrador, however, Newfoundland does not require the purchase of Accident Benefits coverage. Uninsured claimants would rely upon the provincial health care plan for medical expenses and would have no income benefits if unable to work. The coverage is provided as an option by private insurers. For some individuals and under certain circumstances, other types of insurance such as disability and accident insurance may be available at lower cost than the equivalent optional car insurance.

\$200,000 is the statutory minimum third party liability limit required and is available for any one accident; however, if a claim involving both bodily injury and property damage reaches this figure, payment for property damage would be capped at \$20,000.

Claimants have the right to sue for pain and suffering and for economic loss in excess of no-fault benefits.

Yukon

Coverage in the Yukon is provided by private insurers. \$200,000 is the statutory minimum third party liability limit required and is available for any one accident; however, if a claim involving both bodily injury and property damage reaches this figure, payment for property damage would be capped at \$10,000.

Claimants have the right to sue for pain and suffering and for economic loss in excess of no-fault benefits.

Points of Note – Regional Variations

In Quebec and Ontario, the policyholder's own insurer compensates them directly for the share of the damage caused to their vehicle (including contents) and for the loss of use of the vehicle, for which another driver would be legally responsible. Under "direct compensation -- property damage," policyholders deal with their own, not the other person's, insurer. This speeds up the payment process. If an identified motorist is responsible for the collision, the person sustaining damages collects from their own insurer regardless of whether or not they have purchased physical damage coverage for their own car. There are rules, however, for Direct Compensation to apply. The collision must occur in your home province; there must be at least one other identified vehicle involved in the crash causing the loss; and that other vehicle must also be insured by an insurer which is licensed in that province or which has signed a special agreement. If these conditions can't be fulfilled, then the policyholder's collision insurance must be utilized whether or not they are at fault.

Non-renewal (Ontario): In Ontario, insurers must file with the government regulator a list of conditions under which they will not renew a policy; this doesn't give them much room to make allowances for special circumstances. In those provinces having government car insurance plans, a contract is not issued for the basic coverages since everyone must purchase these before they can obtain vehicle licence plates or renewals.

If economic loss exceeds the no-fault accident benefits of the injured person's policy, they may have the options to sue the person responsible for the accident. This will depend on where the accident happened; lawsuits are permitted everywhere except Manitoba and Quebec. In Saskatchewan, injured persons may recover only with respect to gross income losses that exceed a specified amount. In Ontario, the ability to sue for Loss of Income is subject to conditions: an injured person can sue for medical, rehabilitation and related costs only when injury is very serious (catastrophic, as defined by law).

Persons injured in motor vehicle accidents can sue for pain and suffering except in Saskatchewan, Manitoba and Quebec, where such lawsuits are not permitted. Ontario allows suits only if the injured person "dies, or sustains permanent serious disfigurement and/or impairment of important physical, mental or psychological function" (the court assesses damages and a deductible applies).

In non-governmental jurisdictions, there may operate an assigned risk pool, so that drivers not perceived as ideal risks may still continue to receive coverage. The regulators in each jurisdiction determine which insurers participate in accepting sub-standard risks, the applicable rates, and the amount of coverage to be provided. In government jurisdictions, coverage is generally available to all drivers who remain qualified to drive.

Self-Insurance

In non-government auto insurer jurisdictions, provincial regulators may grant status as a self-insurer for third party liability insurance to organizations. The organization must apply to the regulator for such status and must provide satisfactory and appropriate evidence of sufficient financial status to be able to pay claims. This generally involved providing the regulator with financial statements and detailed actuarial information regarding past losses.

Claims must be adjusted in accordance with the regulations of the jurisdiction by appropriately licensed and qualified personnel.

Implications for Risk Management

Risk managers may become involved in purchasing vehicle insurance and settling claims across multiple jurisdictions. It is important that they understand the regulations with respect to licensing and insurance in each jurisdiction in which the company operates and that risk financing alternatives are consistent with the guidelines in the jurisdiction.

If insurance is purchased, a broker familiar with products in the jurisdiction should be utilized. If the risk manager is purchasing excess or umbrella coverage, care should be taken to ensure that underlying coverage has been written on the appropriate policy form.

If vehicles are registered and operated outside of Canada, the risk manager should acquaint themselves with the requirements in each jurisdiction. It is important to note that statutory minimum limits of coverage in the U.S. are often far less than in Canada, where, all provinces and territories (except for Quebec which has a different scheme) have statutory minimum limits of \$200,000 per claim.

As the most likely source of a large liability judgement for most companies is as a result of a vehicle accident, the limits of coverage selected should be a measure of the exposure to loss. Recent judgements in the jurisdiction as well as the use of the vehicle fleet can assist in assessing the risk and the limits required.

Canadian Regulation of Insurance Contracts

This section is in addition to “*Conditions*” p. 4-24; “*Regulatory Filings*”, pp. 7- 14- 7-15 *Risk Financing*; “*Statutory Modifications*”, pp. 163-164, *Essentials of Risk Financing Vol. 2*.

In Canada, the content of insurance policies (both property/casualty and life/health) sold within the jurisdiction is regulated by provincial and territorial legislation. Each jurisdiction has a statute which prescribes the content of insurance policies, classes of insurance to be underwritten, and includes regulations governing the sale of insurance within the jurisdiction.

Each province and territory has a regulatory body overseeing the administration of insurance and insurance contracts within the jurisdiction. Generally, the position responsible is referred to as “Superintendent of Insurance” or some other similar title. This regulator is responsible for monitoring the solvency of provincially and territorially registered insurance companies, and ensuring that insurance statutes and regulations in the jurisdiction are followed by licensed insurers.

In most jurisdictions, the superintendent of insurance or equivalent is also responsible for prescribing the regulations governing the licensing of insurance brokers, agents, and independent insurance adjusters.

The regulator is also generally responsible for the collection of provincial and territorial taxes which may be applicable to insurance contracts. Taxation is discussed in a separate supplement. Note that insurance contracts and applicable premiums are exempt from the federal Goods and Services Tax (G.S.T.) but are subject to the Harmonized Sales Tax (H.S.T.) and the Quebec Tax.

The provincial and territorial insurance acts are each unique, however, there are a number of similar elements.

These include:

- Definitions and interpretation
- Powers of the Superintendent
- How premiums are to be paid and refunded
- Notice of cancellation which must be provided to the Insured
- Rules respecting action taken against an insurer
- Statutory conditions to be contained in insurance policies
- Subrogation, pro-rating, and contribution by more than one insurance policy
- Rules respecting disputes between insurer and insured
- Limitation periods for legal action against insurers

In some cases, there may be a separate statute or regulations which govern the issuance of automobile liability policies, and accident benefits, or in jurisdictions with no-fault accident schemes, the regulations may deal specifically with no-fault benefits.

Generally speaking, the language contained on individual property and casualty insurance policy forms is substantially less regulated than in the U.S. The one type of insurance contract

document which is very uniform in Canada is the Standard Automobile Owner's liability policy or SPF1 as it is commonly known in most jurisdictions.

Rates and policy wordings for coverages other than auto do not generally need to be filed with Canadian provincial regulators, however, the language in the policy wording must not conflict with the applicable statutes. For the purposes of monitoring insurer solvency, the amount of reinsurance ceded on a per-risk and a portfolio basis must be reported to regulators periodically, as dictated.

In jurisdictions with non-government auto schemes, there may be a risk pool which serves to provide universal access to auto liability coverage for drivers with a poor loss record. The superintendent in the jurisdiction will prescribe which risks or which share of risks need to be assumed by each insurer writing automobile liability insurance in the jurisdiction.

In Canada, mortgagees can generally be protected by a Standard Mortgage Clause, which enables a mortgagee to continue to benefit from a fire insurance policy, even if the primary policyholder may have breached the policy conditions.

Canadian Provincial/Territorial Statutes Respecting Insurance Contract Regulation

<u>Jurisdiction</u>	<u>Statute</u>	<u>Website</u>
British Columbia	<i>Insurance Act</i>	www.qp.gov.bc.ca
Alberta	<i>Insurance Act</i>	www.gov.ab.ca
Saskatchewan	<i>Saskatchewan Insurance Act</i>	www.gov.sk.ca
Manitoba	<i>Insurance Act</i>	www.gov.mb.ca
Ontario	<i>Insurance Act</i>	www.e-laws.gov.on.ca
Quebec	<i>Loi sur les Assurances</i>	http://publications.quebec.gouv.qc.ca
New Brunswick	<i>Insurance Act</i>	www.gnb.ca
Nova Scotia	<i>Insurance Act</i>	www.gov.ns.ca/legi
Prince Edward Island	<i>Insurance Act</i>	www.gov.pe.ca/law/statutes
Newfoundland & Labrador	<i>Insurance Contracts Act</i> <i>Insurance Companies Act</i>	www.gov.nf.ca/hoa/sr
Yukon	<i>Insurance Act</i>	www.canlii.org/yk/sta
Northwest Territories	<i>Insurance Act</i>	www.canlii.org/nt/sta
Nunavut	<i>Insurance Act</i>	www.canlii.org/nv/sta/cons

Canadian Provincial/Territorial Insurance Regulators

Canada

Deputy Superintendent of Insurance & Pensions
Department of Insurance Canada
L'Esplanade Laurier, East Tower, 15th Floor
Ottawa, Ontario K1A 0H2
(613) 990-8010; fax (613) 993-6782

British Columbia

Superintendent of Financial Institutions
Ministry of Finance & Corporate Relations
1050 West Pender Street, Suite 1900
Vancouver, B.C. V6E 3S7
(604) 660-2947; fax (604) 660-3170
www.fic.gov.bc.ca

Alberta

Superintendent of Insurance
Alberta Finance
402 Terrace Building
9515 – 107 Street
Edmonton, Alberta T5K 2C3
(780) 427-8322; fax (780) 420-0752
www.finance.gov.ab.ca

Saskatchewan

Superintendent of Insurance
Office of the Superintendent of Insurance
1871 Smith Street
Regina Saskatchewan S4P 3V7
(306) 787-7881; fax (306) 787-9779
www.saskjustice.gov.sk.ca

Manitoba

Superintendent of Financial Institutions - Insurance
Financial Institutions Regulations Branch
Manitoba Finance – Consumer and Corporate Affairs Division
405 Broadway Avenue, Suite 1115
Winnipeg, Manitoba R3C 3L6
(204) 945-2542; fax (204) 948-2268
www.gov.mb.ca/cca/firb

Ontario

Superintendent and CEO
Financial Services Commission of Ontario
5160 Yonge Street, 16th Floor, Box 85
North York, Ontario M2N 6L9
(416) 590-7120; fax (416) 590-7070
www.ontarioinsurance.com

Quebec

Superintendent of Insurance
800, Place d'Youville, 9th Floor
Quebec City, Quebec G1R 4Y5
(418) 528-9140; fax (418) 528-2791

New Brunswick

Superintendent of Insurance
Department of Justice
P.O. Box 6000 Centennial Building
670 King Street, Room 477
Fredericton, new Brunswick E3B 5H1
(506) 453-2512; fax (506) 453-7435
www.gov.nb.ca

Prince Edward Island

Superintendent of Insurance
Department of Provincial Affairs & Attorney General
P.O. Box 2000
105 Rochford Street
Charlottetown, Prince Edward Island C1A 7N8
(902) 368-4564; fax (902) 368-5283
www.gov.pe.ca/oag

Nova Scotia

Superintendent of Insurance
Business and Consumer Services
Financial Institutions
Maritime Centre, 8 North
1505 Barrington Street, P.O. Box 2271
Halifax, Nova Scotia B3J 3C8
(902) 424-6331; fax (902) 424-1298
www.govins.ca/enla/fin/super.htm

Newfoundland & Labrador

Assistant Deputy Minister
Superintendent of insurance
Department of Government Services and Lands
P.O. Box 8700
St. John's, Newfoundland A1B 4J6
(709) 729-2571; fax (709) 729-4151
www.gov.nf.ca/gsi

Northwest Territories & Nunavut

Superintendent of Insurance
Department of Finance
Division of Taxation and Assessment
4922 – 48th Street
Yellowknife, Northwest Territories X1A 3S3
(867) 873-7308; fax (867) 873-0325
www.gov.nt.ca

Yukon

Superintendent of Insurance
Department of Justice
P.O. Box 2703
Whitehorse, Yukon Y1A 2C6
(867) 667-5257; fax (867) 667-3609
www.gov.yk.ca

Accounting and Tax Implications of Risk Financing

This section is in addition to “*Financial Accounting Issues*” and “*Tax Issues*”, pp. 8-19-21; and replaces “*Financial Accounting and Tax Implications of Finite Risk Plans*” pp. 10-14-10-21 *Risk Financing*.

Accounting

Accounting is a process for recording and reporting an organization’s activities and operating results.

There are several different accounting systems which vary by purpose and according to who uses the accounting information. These are: GAAP accounting, managerial accounting, and tax accounting.

GAAP Accounting

The Canadian Institute of Chartered Accountants (CICA) prescribes the accounting principles upon which accounting of public companies is reported. In Canada, this is typically generally accepted accounting principles (GAAP).

These procedures are detailed, but must be carefully observed for the following reasons:

- The audience relying on the accounting information is large and diverse
- Most people relying upon public accounting statements do not have access to an organization’s internal records
- Public accounting information is published for many diverse types of organizations.

For risk financing, GAAP accounting tries to ensure that, for example, all organizations report transactions with their captive insurers, reserves for incurred-but-not-reported claims, and self-insurance deposits, in ways that are consistent among organizations, and relatively well understood by all.

Managerial Accounting

Managerial accounting aims to provide the organization’s management with the information needed to solve particular problems or make specific decisions. Accepted procedures for managerial accounting are much more flexible than GAAP – partly because the internal audience for managerial accounting information is limited and relatively sophisticated and partly because managerial accounting is intended to answer a variety of highly specialized questions.

Tax Accounting

Tax accounting is used to determine the amount of tax that the organization must pay. The taxpayer may wish to attempt to reduce or project and control the amount of tax that it must pay. For government, the corresponding purpose is to be sure that every taxpayer pays all taxes owed or to at least project and control the amount of taxes it collects.

The rules for tax accounting depend largely on the statutes and regulations that are applicable in each circumstance. Corporations are subject to different rules than those applicable to partnerships and individuals. Frequent variations and revisions make tax accounting its own

specialty and complicate substantially the task of analyzing the various alternatives that the organization may be considering.

Accounting Principles Most Relevant to Risk Financing

The accounting principles embodied in GAAP most relevant to risk financing are:

- Recognizing and measuring only events that have definite financial consequences
- Matching an organization's revenues with its expenses in each accounting period
- Allocating an organization's revenues and expenses to its specific activities, departments, or assets
- Reporting results conservatively so as not to overstate the organization's performance or otherwise mislead those for whom the accounting report is intended
- Serving the organization's goals, such as increasing the organization's net cash flows or decreasing or postponing its income tax payments

Procedures for Using Specific Risk Management Techniques

Long Term Capital Investments

Risk management activities for an organization might entail acquiring or disposing of physical assets over a long period. A short-term asset is technically one that is normally fully used up within one year of its acquisition; all other assets are long term assets.

When an organization acquires a capital asset, it normally makes a cash disbursement equal to the purchase price, either as a lump sum payment, or series of installment payments. The purchase changes the internal composition of assets, but not the aggregate value of the organization's assets.

Accounting procedures for such transactions are designed to match a portion of the purchase price of a long-term asset to each of the accounting periods during which the assets will be used. The asset's entire purchase price is not recognized as an expense during the accounting period in which it is acquired – for accounting purposes, this expense is spread over the asset's expected useful life through an accounting allocation process known as depreciation. The amount of depreciation expense charged to each accounting period can be determined in several ways:

- Straight line depreciation
- Accelerated depreciation
- Use depreciation

Whatever depreciation method is used, the portion of the asset's cost recognized as an expense during any year is a tax-deductible business expense for that period. The total amount of all past depreciation expense on a given asset or the **accumulated depreciation** is one measure of the extent to which the total value of that asset has been "used up" by the organization.

In Canada, Canada Customs and Revenue Agency refers to this as the **Capital Cost Allowance** or CCA, which is a tax deduction for business-related capital property that provides for the depreciation of these assets. Businesses can deduct up to a fixed percentage of the

depreciated cost each year. There are approximately forty CCA classes described in the regulations to the *Income Tax Act*. The CCA rate applicable to each class is usually intended to reflect the economic life of the assets of that class. Where the CCA rate is clearly in excess of that required to reflect the economic useful life, it can be considered to be an accelerated CCA. Generally accepted accounting principles define the book value of a depreciable asset as its purchase price minus its accumulated depreciation.

Operating Expenses and Related Income for Risk Management

Expenses associated with operating a risk management department include those normally associated with any department, such as wages and salaries, utilities, and supplies. Those expenses pose no special risk management concerns and usually represent cash outflows and tax deductible expenses in the accounting periods during which they are incurred.

The operation of a risk management department might also generate some incidental income to the organization – principally investment earnings on funds held in reserves. Such investment income must be recognized for accounting and tax purposes.

Funding Arrangements and Tax Deductibility

The accounting and tax implications of the pre-loss funding arrangements are largely determined by whether the funding arrangements involve retention or transfer.

Current expensing of losses – involves few tax or accounting complexities. Funds used to restore currently expensed losses are normally recognized as expenses of the accounting period in which they are paid. The primary exception involves replacing capital assets bought with current funds. The organization may apply CCA to these assets.

Funded Reserves – the funds that an organization allocates to internal reserves for future losses have not been treated as expenses for accounting or tax purposes in the period in which the allocations have been made. The reserve has neither tax nor accounting implications, however, as described previously, the earnings on the funds held in reserve are deemed to be income, which is taxed as any other investment income.

Retained losses have historically been recognized as expenses for tax purposes only after they have occurred and been paid.

Borrowing Arrangements – for accounting and tax purposes, interest payments on borrowed funds for any purpose are considered business expenses, therefore, when an organization borrows money to pay for accidental losses, the related interest payments are tax deductible.

Insurance premiums – generally, payments made to an outside transferee in exchange for the promise of financial protection against accidental losses are tax deductible expenses when incurred. Guaranteed cost insurance premiums are a typical example.

Captive insurance companies – there has been U.S. case law on this point, however, in Canada, insurance premium payments to a captive insurance company are generally deemed to be tax deductible expenses as they are paid. The premium must reflect a measure of the actual risk assumed.

Pools and Reciprocals – in Canada for accounting and tax purposes, pools and reciprocals recognized as regulated entities would receive the same accounting treatment as commercial

insurance. In the case where participants use self-funded risk financing which is not regulated, tax deductibility cannot be claimed in the same manner as commercial insurance premiums.

Risk Financing and Taxation in Canada

Tax laws vary from province to province, federal government to province, state to state, U.S. Federal to state, and country to country. Below are discussed taxation issues which relate to risk financing matters faced by a Canadian organization.

In 1917 the Federal Government passed the Income War Tax Act in order to raise money needed to finance Canada's efforts from World War I. Since 1917 the Act has been amended several times. In 1962, a Royal Commission on Taxation was appointed and by 1967 they had published a report which was highly critical of the existing law and proposed some fundamental changes.

In 1972 the Tax Reform Act was proclaimed and the 1972 Act together with numerous amendments and interpretations remains in effect today. One of the most notable recent changes was the introduction of the Goods and Services Tax, implemented in 1991.

It is very important for risk managers to understand that insurance premium taxes, regulations surrounding captives, and the GST will have an effect upon the organization's bottom line. In order to fulfill their duties, a risk manager may require an accounting professional within or outside of their organization to assist them.

Each province and territory collects a premium tax which is charged and collected on almost every policy of insurance sold within that province or territory. This tax is generally included in the premium charged and is remitted by the insurer to the government imposing the tax. While the applicable statutes should be consulted for specific rules and regulations, the various types of taxes are:

Federal Taxes Applicable to Insurance

Excise Tax This is a tax paid on insurance premiums for business placed outside of Canada. If an insurer is not licensed to write business in Canada, a broker may be required to collect the tax from the insured and pay the tax to CCRA on behalf of the insurer to the government.

Policyholders may be exempted from the tax where coverage is unavailable from domestic licensed markets. Application can be made to CCRA where more than 10 domestic markets have declined to provide coverage.

GST Insurance premiums are GST exempt, as are adjuster's fees and broker commissions. Most other fees charged for the purpose of managing risk are subject to GST.

Corporate Tax Dividends received by public corporations from other corporations are exempt from tax. Corporations may deduct capital losses from capital gains, but not from other income. Corporate tax rates, unlike personal income tax rates, DO NOT increase as income increases, they are fixed

both federally and provincially. Dividends received from subsidiaries may be exempt from taxation.

Lloyd's Tax This tax is included in the premium paid for a Lloyd's Non-Marine Underwriters policy charged to Canadian policyholders. The tax is used to pay such expenses as premium tax, licensing fees, and other costs associated with maintaining the Canadian activities of Lloyd's. The rate varies according to the line of coverage.

Provincial & Territorial Taxes Applicable to Insurance

Premium Tax - Licensed or unlicensed insurance is subject to a provincial tax paid by the insurer to the applicable provincial government. For licensed insurers, this tax is generally INCLUDED in the premium charged to the policyholder and remitted to the government directly by the insurer. For unlicensed insurers, the placing broker generally collects and remits this tax.

Unlicensed premium taxes may be as high as 50%, to compel the purchase of insurance with licensed markets.

Fire Tax This is a premium tax payable to the applicable province specifically for fire insurance and often to fund the office of the Fire Marshall. Additional higher tax rates may apply for unlicensed insurers.

Sales Tax In Ontario, Quebec, and Newfoundland, provincial sales tax is charged on the premium payable to the insurer.

BC Captives Tax BC Captives are licensed insurance companies in BC and are subject to taxation in B.C. In other provinces, they are subject to unlicensed premium tax. B.C. captives are subject to Canadian Corporate Income Tax. As an insurance company, BC Captives are deemed to be a financial institution and therefore do not collect GST from their parent organizations.

Other Canadian Captives All non-Canadian domiciled captives, except B.C. domiciled Captives are classified as unlicensed insurers in Canada. Captives owned by Canadian business which insure Canadian operations are subject to premium tax, the Fire Marshall's tax and Canadian excise tax for offshore captives.

Summary of Provincial/Territorial Tax Rates (For Licensed Insurers)
(As at January 2004)

Jurisdiction	P & C Premium (% of Premium)	Fire Tax Rates	Combined P&C /Fire Tax
Alberta	3.00		3.00
British Columbia	4.40		4.40
Saskatchewan (excl. auto)	4.00	1.00	5.00
Saskatchewan (auto)	5.00		5.00
Manitoba	3.00	1.25	4.25
Ontario (excl auto)	3.00	0.50	3.50
Ontario (auto)	3.00		3.00
Quebec	3.35		3.35
Nova Scotia	4.00	1.25	5.25
New Brunswick	3.00	1.00	4.00
Prince Edward Island	3.50	1.00	4.50
Newfoundland & Labrador	4.00		4.00
NWT & Nunavut	3.00	1.00	4.00
Yukon	2.00	1.00	3.00

Allocation of Premium Between Provinces

When an organization operates in more than one Canadian province and is covered by a single insurance policy, the organization must allocate premium by province to calculate the applicable taxes payable. It is recommended that the calculation be done by the insurer.

U.S. and Foreign Taxation

It is beyond the scope of this supplement to discuss the implications. An expert in the jurisdiction should be consulted for tax planning and tax advice.

Tax Planning

Tax planning is the legal process permitted under the laws of taxation to reduce to amount of taxation payable. This legal process is known as tax avoidance. Tax evasion is the illegal process of avoiding the payment of tax and will involve stiff fines, penalties, and imprisonment. Tax avoidance is legal so long as the means is legal and a tax liability is prevented from arising.

From a risk financing perspective, it may not be possible to avoid paying premium tax on unlicensed insurance, but the amount of premium due may be reduced in some cases through the use of a fronting insurer. This method is not without costs and a fronting fee will be charge.

Licensing and Education of Insurance Brokers in Canada

This section is in addition to “*Types of Intermediaries*”, p. 179-183, “*Insurance Agents/Brokers*”, p. 231 *Essentials of Risk Financing Vol. 2*.

Insurance brokers in Canada are licensed by the applicable province or territory in which they operate. Licensing is generally for either property and casualty insurance or for life insurance. Generally, there are 3 levels of licensing: Level I – deals with basic sales of personal lines products and the broker must be supervised by a Level II agent or broker; Level II – deals with sales of commercial and personal lines products and may countersign policies issued by the insurer; Level III – person licensed as the managing broker in an office.

The individual Insurance Councils or regulatory bodies in each jurisdiction are responsible for the issuance of the brokers license, discipline and suspension, and oversee the requirements for initial training and continuing education.

Licenses are generally issued for a fixed time period (i.e. with expiry date) and must be renewed periodically.

Below is listed a summary of some of the educational programs offered to brokers in Canada.

Fundamentals of Insurance

This course is used as a licensing course in eight provinces. Its content is kept current to reflect changes in the industry. The course is completed with the licensing examination.

Canadian Accredited Insurance Broker (CAIB)

CAIB is a national education program involving four courses of study, covering both technical and applied knowledge, each of which concludes with a comprehensive final exam.

Canadian Certified Insurance Broker (CCIB)

This is the highest designation awarded by the Insurance Brokers Association of Canada. Three examinations are required based on the candidates' working knowledge. There is no formal course of study. Prerequisites are that the candidate must have 5 consecutive years' experience.

Canadian Professional Insurance Broker (CPIB)

The Canadian Professional Insurance Broker (CPIB) is the new senior designation program developed by the Insurance Brokers Association of Canada and its provincial/regional Members Associations. It is specifically designed for property and casualty insurance brokers

Licensing and Qualifications of Independent Insurance Adjusters in Canada

This section is in addition to “*Independent Adjusters*”, p. 230 *Essentials of Risk Financing Vol. 2*.

Many insurance claims are handled by Independent insurance adjusters, who must be licensed in their province or territory of operation. Generally, adjusters who are the full time employees of insurance companies do not require a license.

Alberta

Adjuster’s Certificate - Level 1

Must pass an examination of the Alberta Insurance Council. Must be supervised by a holder of a Level 3 Adjuster’s Certificate of Authority; all claims reports must be approved and countersigned by that holder of a Level 3 Adjuster’s Certificate of Authority.

Adjuster’s Certificate – Level 2

24 consecutive months of claims adjusting experience plus successful completion of six IIC courses for a designation as an Associate of the IIC, of which one course must be C-17 (Claims 1). Must be supervised by a holder of a Level 3 Adjuster’s Certificate of Authority; all claims reports must be approved and countersigned by that holder of a Level 3 Adjuster’s Certificate of Authority.

Adjuster’s Certificate - Level 3

Successfully met Level 2 requirements and:

- a) is an Associate or Fellow of the IIC;
- b) has successfully completed the C-32 (Bodily Injury Claims) and C-46 (Claims 2) courses of the IIC;
- c) and has acted as an adjuster for at least 60 consecutive months within the 10 year period immediately preceding the date of application.

British Columbia

Adjuster Level 1

Must have successfully completed the Council’s adjuster qualification examinations. Must be under the direct supervision of an adjuster – Level 2 or Level 3 who must approve and countersign all reports related to claims adjustment.

Restrictions

Must not engage in any additional employment other than as an adjuster unless the licensee has obtained prior approval of both employers and from the Council to do so.

Adjuster Level 2

Must have 2 years consecutive experience as an insurance adjuster plus 8 courses from the IIC (claims route), or

2 consecutive years experience as an adjuster – Level 1 plus 4 courses from the IIC (Claims route), or 1 year experience as an insurance adjuster and AIIIC designation.

Restrictions

May act as branch managers only if the provincial head office of the firm is managed by an Adjuster – Level 3

Adjuster Level 3

Must have 5 consecutive years as an insurance adjuster plus AIIIC designation (claims route), or 2 consecutive years as an insurance adjuster plus FIIC designation.

Partnerships, corporations, sole proprietors

Adjuster nominee who qualifies for a level 3 licence must be an officer, director or partner of the adjusting firm or head office manager in the province.

Branch Offices must appoint an adjuster – Level 2 or Level 3 to manage each branch of the firm.

Residency

Non-resident adjusters must establish that they are currently licensed in their home jurisdiction. Must pass the Council's Supplementary Exam.

Manitoba

Eligibility Requirements

Must be sponsored and employed by an adjusting firm. Must pass a qualifying examination set by Council with a mark of 75% or higher.

Level 1 – Assistant Adjuster

Within 18 months from date of issue of the Level 1 license must take and pass C11 – Principles & Practices of Insurance or Two General Insurance Essentials (GIE) courses

All Claims reports and correspondence must be approved and countersigned by a Level 4 Adjuster.

Level 2 – Assistant Adjuster

Eligible for Level 2 once the requirements in Level 1 are accomplished. Within three years from the date of issue of Level 2 Licence must take and pass the following IIC Courses:

C11 – Principles & Practices of Insurance
C12 – Insurance on Property (Part I)

C17 – Claims I
C43 – Specialty Lines

All claims reports and correspondence must be approved and countersigned by a Level 4 Adjuster.

Level 3 – Adjuster

Holds or is eligible to hold a Level 2 License. Has successfully completed 4 of the AIC courses. Is sponsored by an adjusting firm and has been employed in a general insurance company or adjusting firm for at least two years.

Level 4 – Independent Adjuster

Holds or is eligible to hold a Level 3 insurance adjusters license and has passed the required courses for Level 3 plus the following IIC courses:

C13 – Insurance Against Liability
C14 – Personal Automobile Insurance
C33 – Insurance on Property (Part II)
C46 – Claims II

Has been employed as an adjuster in a general Insurance Company or an Independent Adjusting Firm for at least 5 yrs. Must be sponsored by an Adjusting Firm.

Level 5 – Adjusting Firm

Maintains an office in Manitoba. For a sole proprietorship – must be operated by a sole proprietor who has attained an Associateship from the IIC; holds a Level 4 license and provides on-site supervision at one of the sole proprietorships office or at one of its offices where it has more than one.

Must designate the sole proprietor as its designated representative and has a minimum of one insurance adjuster with a Level 4 license at each and every office location other than the one supervised by the designated representative who provides on-going site supervision. For a partnership or corporation must have a partner or designated representative who meets the same criteria as that required of a sole proprietor.

Residency

Must be licensed as an insurance adjuster in his jurisdiction of residency and submits a certificate from the licensing authority of that jurisdiction confirming that fact and specifying the level and status of the license.

Has demonstrated eligibility for the license being applied for. Has satisfied all the requirements of the Act and the rules for the issue of license.

New Brunswick

Must be sponsored by an automobile, property, liability licensee or general adjuster licensee who accepts responsibility for the instruction and conduct of the applicant.

Within 12 months must successfully complete at least one course for automobile, property or liability adjuster's license. Within 30 months must successfully complete the courses for an automobile, property or liability adjuster's license.

Restrictions

Cannot adjust an insurance claim in his own right or enter into any correspondence or reports.

Automobile Adjusters Licence

Within 5 years of being issued a student adjuster's license must successfully complete the following course of studies for an automobile adjuster's license:

- C11 – Principles & Practices of Insurance or C81 and C82 GIE
- C13 – Insurance Against Liability
- C14 – Automobile Insurance
- C17 – Claims I

Property Adjusters Licence

Within 5 years of being issued a student adjuster's license must successfully complete the following course of studies for a property adjuster's license:

- C11 Principles & Practices of Insurance or C81 and C82 GIE
- C12 – Insurance on Property (Part I)
- C32 - Bodily Injury or C40
- C46 – Claims II or rewriting licence.

Liability Adjusters Licence

Within 5 years of being issued a student adjusters licence must successfully complete the following course of studies for a liability adjuster's license:

- C11 – Principles & Practices of Insurance or C81 and C82 GIE
- C13 – Insurance Against Liability
- C17 – Claims I
- C33 – Insurance on Property (Part II) or C43 – Specialty Lines

General Adjusters Licence

Must successfully complete the following IIC courses:

- C11 – Principles & Practices of Insurance or C81 and C82 GIE
- C12 – Insurance on Property (Part I)
- C13 – Insurance Against Liability

C14 – Automobile Insurance
C17 – Claims I
C32 – Bodily Injury or C40
C33 – Insurance on Property (Part II) or C43 – Specialty Lines
C46 – Claims II or rewriting licence

Newfoundland

Eligibility Requirements

Resident of Newfoundland and have certificate of Authority showing status and level of adjusters licence in another jurisdiction

Level 1

Must successfully complete the following IIC courses:

C81 and C82 – General Insurance Essentials (Part I & II) or
C11 – Principles & Practices of Insurance

Restrictions

Must work under the supervision of a Level 3 or 4 adjuster
Reports must be countersigned by a Supervisor

Level II

Application for Level II must be made within three years of having Level I certificate. Must have two years experience at Level I and successfully complete the following IIC courses:

C12 – Insurance on Property (Part I)
C14 – Automobile Insurance
C17 – Claims I

Level III

Must have one year experience at Level II and successfully complete the following IIC courses:

C13 – Insurance Against Liability
C33 – Insurance on Property (Part II)
C46 – Claims II
C43 – Specialty Lines

Level IV

Must have one year experience at Level III plus Associateship designation including successful completion of the following IIC courses:

C32 – Bodily Injury, C16 plus Two other IIC courses

Nova Scotia

Level 1 – Probationary Adjuster

Must complete application form endorsed by an officer or partner of a Level V Licensee and submit a fee. Must submit a Level I adjuster agreement. Must successfully complete C11 – Principles & Practices of Insurance. Must be sponsored by a Level V licensee.

Level II – Assistant Adjuster

Holds or is eligible to hold Level I license. Must complete application form endorsed by an officer or partner of a Level V Licensee and submit a fee. Must submit a Level II Adjuster Agreement.

Must successfully complete the following IIC courses:

C12 – Insurance on Property (Part I)
C14 – Personal Automobile Insurance
C17 – Claims I

Level III – Adjuster

Must complete application form endorsed by an officer or partner of a Level V Licensee and submit a fee. Must submit a Level III Adjuster Agreement.

Must successfully complete the following IIC courses:

C13 – Insurance Against Liability
C46 – Claims II

Level IV – Independent Adjuster

Holds or is eligible to hold Level III License. Must successfully complete the following IIC Courses:

C32 – Bodily Injury Claims
C35 – Insurance Against Crime or C36 – Building Construction, Fire Protection, Basic Hazards.

Level V – Partnership or Corporate Adjuster Licence

Must complete application and submit a licensing fee. Must be registered with the Registry of Joint Stock Companies.

NWT & Nunavut

Eligibility Requirements

Candidates must submit a completed application form and appropriate fees. Applicants are required to pass the General Insurance Examination provided by the Insurance Institute of Canada.

Residency

Non-resident applicants who are licensed in another jurisdiction within the last year must submit an original, personal non-resident endorsement, certificate of agent status, or certificate of authority not more than three months old, from appropriate licensing authority in their home jurisdiction.

Ontario

Letter of Authority

Within 30 months of holding the letter of authority the following four IIC courses must be completed successfully:

- C11 – Principles and Practices of Insurance (or both C81 and C82 GIE)
- C14 – Automobile Insurance
- C12 – Insurance on Property (Part I)
- C17 – Claims I

Restrictions

Cannot:

- sign any report or communication addressed to an Insurer
- sign any other correspondence without permission of the employer
- negotiate the settlement of any bodily injury claim
- authorize repairs to property or agree to accept any bill regarding a claim without the consent of the employer

Probationary Adjusters License

Within 30 months of receiving the Probationary Adjusters License, the following four IIC courses must be completed successfully:

- C13 – Insurance Against Liability
- C46 – Claims II
- C32 – Bodily Injury
- C33 – Insurance on Property (Part II)

Full Adjusters License

May be subject to an oral exam at the discretion of the Superintendent of Insurance.

Prince Edward Island

Probationary Adjuster

Must be a grade 11 graduate and resident of P.E.I. Apply to the Superintendent of Insurance with support of three signatures, one of which is a full adjuster.

Within 5 years must successfully complete the following four IIC courses:

C11 – Principles & Practices of Insurance

C17 – Claims I

C32 – Bodily Injury

C46 – Claims II

Plus

Three other IIC courses

Full Adjuster

Must be a resident of P.E.I. and have two consecutive years of experience and have completed the courses outlined under Probationary Adjuster.

Quebec

Minimum Education

Diploma of collegial studies or an equivalent level of education, or High school diploma and a minimum of four years' relevant experience in the last ten years in full-time employment in the area of damage insurance, or attestation of collegial studies in damage insurance recognized in an agreement in such regard between the Bureau des services financiers and a college, and, successfully complete each of the three (3) examinations prescribed by the Bureau.

Training Period

A training period of 45 days in personal-lines damage insurance

and/or

A training period of 45 days in commercial-lines insurance

Each training period must be conducted without interruption under the supervision of the same training supervisor who must have a minimum of 3 years experience.

Saskatchewan

Eligibility Requirements

Must pass the current adjusters' bylaws examination with mark of 75% or higher or equivalent license in another jurisdiction plus a passing mark in the adjusters' bylaws examination. This is applicable to each and every level of licensing.

Level 1 – Probationary License

C11 – Principles & Practices of Insurance

or

Pass a qualifying exam approved by Council with 75% or higher or be licensed for 2 consecutive years or more as an insurance sales person in All classes other than life or must

have been continuously employed as a claims adjuster in an insurance company, agency or adjusting firm for no less than one year.

Sponsorship

Must be sponsored by a Level Five Licensee

Restrictions

Cannot act in supervisory capacity or as a public adjuster; or sign any reports unless countersigned by a Level Four Licensee

Level 2 – Assistant Adjuster

One year licensed as a Level One adjuster and have passed four IIC courses or five or more years experience as a claims adjuster in a general insurance or adjusting company

Sponsorship

Must be sponsored by a Level Five Licensee

Restrictions

Cannot act in a supervisory capacity or as a public adjuster

Level 3 – Adjuster

Eligible for Level Two license plus completion of eight IIC courses of the IIC's Associate Program or two years licensed as a Level Two Assistant Adjuster plus completion of eight courses of the IIC's Associate Program or Ten years experience as a claims adjuster

Restrictions

Cannot act in a supervisory capacity or as a public adjuster

Sponsorship

Same as Level 2

Level 4 – Independent Adjuster

AllC plus two years practical experience in the employ of a Level Five Licensee or AllC plus five continuous years employment as a general adjuster or

Level 5 – Adjusting Firm

Maintain an office in Saskatchewan and have a minimum of one resident Level Four Licensee at each office location who provides on-going on-site supervision

Non-Resident

Non-Resident Eligible for a Saskatchewan Level Four License and satisfied licensing requirements of the Saskatchewan Insurance Act, Regulations and Bylaws.

Sponsorship

Must be sponsored by a Level Five Licensee.

Restrictions

Cannot act as a designated Level Four Licensee.

Yukon

Eligibility Requirements

Candidate must submit a completed application form and appropriate fees. License is granted at the discretion of the Superintendent.

Residency

Non-resident must provide a copy of adjuster's current license and a letter of good standing from licensing jurisdiction.