

FSRA releases Proposed Guidance on Automobile Insurance Rating and Underwriting Supervision

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Law360 Canada (November 14, 2024, 2:40 PM EST) -- The Financial Services Regulatory Authority of Ontario's (FSRA) role in the automobile insurance sector includes a responsibility to ensure that all Ontarians have access to fairly priced automobile insurance. Recently, FSRA introduced its Proposed Guidance: Automobile Insurance Rating and Underwriting Supervision Guidance (Proposed Guidance), which aims to transition the sector to a principles-based regulatory model.

This approach sets out desired consumer outcomes and requires insurers to incorporate these outcomes into their rating and underwriting practices. The Proposed Guidance applies to all insurance companies and their intermediaries providing automobile insurance in Ontario, including those underwriting private passenger automobiles, non-private passenger automobiles and fleet vehicles. The effective date for this Proposed Guidance has yet to be determined.

The Proposed Guidance is structured into four chapters:

- chapters 1 and 2 outline FSRA's standards on fair outcomes for consumers and the characteristics of sound operations, controls and governance required to achieve these outcomes in insurance rating, underwriting, and risk classifications;
- chapter 3 details the process for insurers to pursue accreditation and explains FSRA's approach to proactive supervision; and
- chapter 4, still to be drafted, will outline the filing requirements for accredited and non-accredited insurers.

Fair Consumer Outcomes

Chapter 1 of the Proposed Guidance establishes that insurers are accountable for aligning their rating and underwriting practices with FSRA's intended consumer outcomes for fairness, profitability, and transparency (Fair Consumer Outcomes).



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The key principles of Fair Consumer Outcomes include:

- **Fairness:** Ensuring accurate pricing and underwriting, avoiding unfair discrimination, bias or proxies, providing accessible products and coverages and mitigating unnecessary costs.
- **Balanced Profitability:** Striking an appropriate balance between sustainable growth and profitability while ensuring fair treatment of consumers.
- **Transparency:** Providing clear and timely communications with policyholders to enable informed decision-making.

The chapter also provides FSRA's interpretation of the statutory tests it administers to assess insurers' rating and underwriting practices, reflecting its determination of what best supports Fair Consumer Outcomes.

1. Risk Classification System Provisions

Subsections 3(5), 7(7) and 7.1(1) of the *Automobile Insurance Rate Stabilization Act*, and subsections 412(6) and 415(1) of the *Insurance Act* set out four criteria that FSRA considers when determining whether to refuse to approve all or a part of an insurer's application for automobile insurance rates:

1. the proposed risk classification system or proposed rate is not just and reasonable in the circumstances;
2. the proposed risk classification system is not reasonably predictive of risk or does not distinguish fairly between risks;
3. the proposed rates would impair the insurer's solvency; or
4. the proposed rates are excessive in relation to the insurer's financial circumstances.

The Proposed Guidance indicates that a risk classification will be considered "just and reasonable" and "reasonably predictive of risk and distinguishes fairly between risks" if the rates generated align with Fair Consumer Outcomes.

2. Underwriting Provisions

Subsections 238(4)(d) of the *Insurance Act* provides that underwriting rules shall not be: 1) subjective, 2) arbitrary, 3) bear little or no relationship to the assumed risk or 4) contrary to public policy. The Proposed Guidance states that underwriting rules will generally comply with these requirements if the resulting underwriting decision demonstrates Fair Consumer Outcomes.

Automobile Insurance Rating and Underwriting Operations, Controls and Governance

Guidance

Chapter 2 outlines the characteristics of sound operations, controls and governance with respect to the delivery of Fair Consumer Outcomes in insurance rating, underwriting and risk classifications. It extends to all related processes, products, systems and models, including data governance and model risk management (collectively, OCG). The Proposed Guidance provides standards and best practices in the following areas:

- **Operational risk and risk control:** Insurers are accountable for implementing clear, well-documented, actionable and measurable policies and oversight to manage operational risks.
- **Governance:** Insurers shall establish clear policies outlining governance standards and document roles and responsibilities for monitoring the insurer's ratemaking and underwriting functions.
- **Data governance:** Insurers must ensure that policies related to data usage, governance and controls are appropriate, accurate, complete and timely and will assist in the identification, assessment and management of data risk.
- **Model risk management:** Insurers are responsible for establishing processes for model development, validation, approval and review. They are also accountable for continuous monitoring, prompt implementation of risk controls and the development of tools for model interpretability and explainability.

Accreditation, Proactive Supervision and Assessment Approach Guidance

Chapter 3 outlines FSRA's accreditation model and assessment process. Insurers that demonstrate the delivery of Fair Consumer Outcomes and sound OCG characteristics set out in Chapters 1 and 2 may be eligible for accreditation. Accredited insurers will benefit from streamlined filing processes through the discretion afforded to FSRA under s. 413 of the *Insurance Act*.

The chapter also sets out FSRA's approach to proactive supervision for the rating and underwriting of all insurers, regardless of their accreditation status. This supervision involves collecting information to monitor the market, supervise performance and mitigate adverse consumer outcomes. Insurers are also required to notify FSRA of any material changes to their business, such as changes in strategy, risk appetite or governance.

Public consultation

FSRA is currently seeking public feedback on the first three chapters of its Proposed Guidance, with comments invited by Nov. 15, 2024. The fourth, and final, chapter of the Proposed Guidance is expected to be available for consultation in 2025.

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