

Saskatchewan Government Insurance

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Main points

This year, we looked at the processes Saskatchewan Government Insurance (SGI) uses for managing its sales force. That is, its brokers. We expected SGI would have adequate processes to:

- ◆ determine how many brokers it needs, and to appoint and terminate brokers when necessary;
- ◆ ensure its brokers have operational policies and procedures; and
- ◆ ensure its brokers comply with the signed agreements.

We found that SGI's practices for managing its brokers were adequate. The chapter describes our performance expectations of SGI and our detailed findings.

In this chapter, we also describe the results of our audit of Saskatchewan Government Insurance (SGI) and the companies it owns, Saskatchewan Auto Fund (SAF), and Saskatchewan Government Insurance Superannuation Plan (SGI Plan) for the year ended December 31, 2003. SGI manages SAF and sponsors SGI Plan.

We concluded that the financial statements for SGI, its companies, SAF, and SGI Plan are reliable. They had adequate rules and procedures to safeguard public resources and complied with laws governing their activities.

Introduction

Saskatchewan Government Insurance (SGI) sells property and casualty insurance in Saskatchewan. SGI created a company called SGI Insurance Services Ltd. (SCISL). SCISL sells property and casualty insurance outside Saskatchewan.

SCISL bought Coachman Insurance Company (Coachman) and Insurance Company of Prince Edward Island (ICPEI). SCISL owns all the issued shares of Coachman and 75% of the issued shares of ICPEI. Coachman and ICPEI sell property and casualty insurance including automobile insurance in Ontario and Prince Edward Island, respectively.

SGI also manages the Saskatchewan Auto Fund (SAF). SAF is Saskatchewan's compulsory auto insurance program. SAF receives money from the motoring public and pays claims. SAF does not receive money from, nor pay dividends to the General Revenue Fund.

SGI sponsors the Saskatchewan Government Insurance Superannuation Plan (SGI Plan). The SGI Plan is a defined benefit pension plan (closed to new members in 1978). The SGI Board is responsible for administration of the SGI Plan under *The Pension Benefits Act, 1992*. The primary objective of the SGI Plan is to provide pensions to SGI's retired employees and to the dependants of deceased pensioners and employees. SGI provides day-to-day management of the SGI Plan.

SGI's annual report includes its consolidated financial statements for the year ended December 31, 2003. Those statements report revenue of \$260.6 million, net profit of \$21.2 million, total assets of \$482.3 million, and retained earnings of \$37.5 million.

SCISL's annual report includes its consolidated financial statements for the year ended December 31, 2003. Those statements report revenue of \$52.2 million, net profit of \$1.3 million, total assets of \$127.9 million, and a deficit of \$12.9 million.

Coachman's annual report includes its financial statements for the year ended December 31, 2003. Those statements report revenue of \$32.9 million, net profit of \$0.3 million, total assets of \$87.7 million, and a deficit of \$16.1 million.

ICPEI's annual report includes its financial statements for the year ended December 31, 2003. Those statements report revenue of \$9.5 million, net profit of \$0.7 million, total assets of \$21.8 million, and retained earnings of \$0.2 million.

SAF's annual report includes its financial statements for the year ended December 31, 2003. Those statements report revenue of \$541.3 million, a net increase to the rate stabilization reserve (net profit) of \$11.5 million, total assets of \$990.5 million, and a rate stabilization reserve of \$14.3 million.

The SGI Plan's annual report includes its financial statements. Those statements report contributions from employees totalling \$0.1 million, and pensions and refunds totalling \$3.5 million. At December 31, 2003, it held assets of \$50.7 million and owed accrued pension benefits of \$50.4 million.

Our audit conclusions and findings

Our Office worked with KPMG LLP, the appointed auditor for SGI, SAF, SCISL, Coachman, ICPEI and the SGI Plan using the framework recommended by the *Report of the Task Force on Roles, Responsibilities and Duties of Auditors* (to view a copy of this report, see our web site at <http://www.auditor.sk.ca/>). Our Office and KPMG formed the following opinions.

In our opinion for the year ended December 31, 2003:

- ◆ **the financial statements of SGI, SAF, SCISL, Coachman, ICPEI, and the SGI Plan are reliable;**
- ◆ **SGI, SAF, SCISL, Coachman, ICPEI, and the SGI Plan had adequate rules and procedures to safeguard public resources; and**
- ◆ **SGI, SAF, SCISL, Coachman, ICPEI, and the SGI Plan complied with authorities governing their activities relating to financial reporting, safeguarding public resources, revenue raising, spending, borrowing, and investing.**

In 2003, we decided to examine the adequacy of SGI's processes to manage its brokers to sell its insurance products. We examined SGI's systems and practices for the year ended December 31, 2003. For this part of our work when we use the abbreviation SGI it includes SGI, SCISL, Coachman, and ICPEI.

We concluded that for the year ended December 31, 2003, SGI had adequate processes to manage its brokers. In the next section, we provide information about the scope of our work, the criteria we used to do our work, and our detailed findings.

Broker management

The Saskatchewan Government Insurance Act, 1980 allows SGI to sell property and casualty insurance. SGI relies on a network of approved brokers to sell its insurance products. These approved brokers are SGI's insurance sales force. SGI uses about 330 brokers in Saskatchewan and about 150 brokers outside Saskatchewan to generate premium revenue of over \$240 million for SGI. Some of these brokers also act as issuers of licences for vehicles and drivers in the Province. To ensure its insurance products continue to meet ever-changing needs of the insuring public, SGI works closely with its brokers to obtain advice on the changing needs of consumers.

SGI's mandate is to provide quality and affordable insurance products to the public. To fulfil its mandate, SGI needs to manage effectively its brokers to sell its products. Effective management of brokers helps ensure that brokers provide sound insurance advice to clients and sell insurance within authorized limits. When clients do not receive sound insurance advice, they may not have appropriate insurance coverage. This could result in clients losing confidence in SGI. Also, if brokers submit requests for insurance for imprudent risks or for insurance beyond their authorized limits, SGI will deny insurance coverage. This could result in clients losing confidence in the brokers and SGI.

Effective management of its brokers also helps ensure SGI's insurance products keep pace with changing public needs and SGI knows its insurance risks (i.e., exposure to loss).

Our objective

The objective of the audit was to assess whether SGI has adequate processes to manage its brokers to sell its insurance products. We examined SGI's processes for the year ended December 31, 2003.

Throughout the audit, we followed *The Standards for Assurance Engagements* established by The Canadian Institute of Chartered Accountants.

Our criteria

Auditors use criteria to evaluate the matters that they examine. Criteria are reasonable and attainable standards of performance and control against which auditors can assess the adequacy of systems and practices. To complete our audit, we developed the criteria listed in the Exhibit based upon our review of relevant literature and best practices. SGI agreed with our criteria.

Exhibit

To adequately manage its insurance brokers, SGI needs to have systems and practices to:

- ◆ Determine the number and class of insurance brokers it needs to sell its insurance products.
- ◆ Appoint and terminate brokers when necessary.
- ◆ Regularly ensure the adequacy of brokers' operational policies and procedures.
- ◆ Regularly ensure its brokers comply with the signed agreements.

Our detailed findings

We describe our detailed findings for each criterion below. For each criterion, we set out what we expected (in italics) and what we found.

Determine the number and class of insurance brokers it needs to sell its insurance products

We expected SGI would have processes to:

- ◆ *determine the number and class of brokers it needs and where;*
and
- ◆ *select appropriate brokers.*

Currently, SGI approves only those brokers in Saskatchewan who purchase existing brokers' businesses and new First Nations brokers to operate on First Nations' reserves. SGI has not formally documented how many and what class of First Nations' brokers it needs and where.

SGI, like other insurance companies, looks for ways of spreading its insurance risk. When insurers sell policies in one geographical area, they face the risk of high losses in case of a catastrophe. High losses result in higher premiums. The higher premiums may result in loss of future business to competitors.

To manage this risk, SGI establishes annual targets for spreading insurance risks outside the Province. The targets set out planned increases in out-of-province insurance premiums for the year. Management uses these targets to plan strategies to expand in other provinces. Expansion in other provinces requires SGI to appoint additional brokers in those provinces. SGI could improve how it documents how many and what classes of brokers it needs to meet its expansion targets.

To ensure its brokers can contribute to SGI's objectives, SGI must ensure all new brokers are licensed and their long-term plans are consistent with SGI's plan. SGI must also ensure the brokers have a history of doing business with other insurance companies and have adequately trained staff.

SGI has established a checklist that it uses to select brokers. The checklist requires that brokers are licensed, brokers' staff have adequate training and skills, and the brokers have adequate errors and omissions insurance coverage.¹ We found that SGI generally completed all required

¹ Errors and omissions coverage provides brokers protection against claims arising from negligent acts, errors, and omissions in the conduct of business.

steps when selecting new brokers. Also, SGI interviewed new brokers and assessed new brokers' long-term plans and their current and projected financial results. SGI could improve how it documents its interviews with new brokers, assessments of new brokers' long-term plans, and their history of business relationships with other insurance companies.

Appoint and terminate brokers when necessary

We expected SGI would have processes to:

- ◆ *make security checks and to assess brokers' financial integrity including any necessary credit checks;*
- ◆ *ensure appropriate pay for the brokers;*
- ◆ *ensure a formal signed agreement exists with brokers setting out the role of brokers and SGI; and*
- ◆ *terminate brokers who do not perform as expected or for other reasons.*

SGI has processes for checking the financial integrity of new brokers. SGI reviews new brokers' past financial statements and seeks credit reports from credit agencies. SGI's security checks also include contacting other insurance companies and the Saskatchewan General Insurance Council (the Council that regulates brokers), and reviewing SGI's files for concerns about brokers and their key staff. SGI could improve how it documents in the files its discussion with other insurance companies and the Council. It could also improve how it documents security and integrity checks for new brokers.

SGI uses written agreements to set out the roles and responsibilities of brokers. These agreements set out the brokers' authority to bind SGI, types of insurance policies the brokers can offer, brokers' pay, and brokers' responsibilities for collecting and remitting premiums. The agreements also set out conditions that may result in SGI ending the agreements.

SGI has processes to ensure it pays brokers the rates set out in the brokers' agreements. Also, SGI has processes to take action when brokers do not follow the terms of the agreements.

Regularly ensure the adequacy of brokers' operational policies and procedures

We expected SGI would have processes to:

- ◆ *train brokers about SGI products so that brokers know the insurance products and any coverage limitations;*
- ◆ *ensure brokers have processes to provide prompt notification to the insured about cancellation or non-renewal of existing policies, industry or legislative changes affecting coverage, and any inadvertent cancellation and failure to renew;*
- ◆ *ensure brokers have processes to promptly notify SGI about requested policy cancellation, revision of coverage, inadvertent delays in processing insurance policies, and any fraud, misrepresentation or illegal acts by the insured or brokers' staff;*
- ◆ *ensure brokers follow SGI's insurance policy sales guidelines;*
- ◆ *regularly receive and consider public advice from brokers on SGI's insurance products and their comparability to products offered by other insurers; and*
- ◆ *ensure brokers have adequate errors and omissions insurance coverage.*

To explain its insurance products, SGI provides training to its brokers both in person and through the internet. SGI also provides pamphlets to its brokers that help them explain SGI's insurance products to customers.

To ensure brokers have adequate operational policies and procedures, SGI provides its brokers with manuals. The manuals set out what information the brokers need to gather from the customer, who is eligible for coverage for each type of insurance policy, coverage and deductibles, and how to compute the premium rate. SGI expects its brokers to follow those processes when selling SGI's insurance policies.

In addition, SGI provides its brokers with SGI's insurance policy processing guidelines. These guidelines describe circumstances that brokers must promptly communicate to SGI and the insured. SGI has processes to ensure that brokers promptly inform SGI about cancellation or non-renewal of existing policies.

SGI requires brokers to inform the insured about any industry or legislative changes affecting coverage or any inadvertent cancellation and

failure to renew. SGI annually surveys customers in Saskatchewan who cancelled insurance policies with SGI. SGI uses the results of these surveys to help determine product changes and to evaluate brokers' communication with customers. Management told us that SGI plans to develop similar surveys for its out-of-province customers. In 2003, SGI sold to out-of-province customers insurance products representing total insurance premiums of approximately \$45 million. Also, SGI meets with brokers to discuss SGI's products and suggestions for changing the products.

SGI reviews all insurance applications it receives from brokers. The review process ensures that brokers comply with SGI's policy processing guidelines. In those cases when SGI determines a broker did not fully comply with those guidelines, SGI discusses the non-compliance with the broker and provides guidance on how to handle such applications in the future.

SGI requires its brokers to maintain adequate errors and omissions (E&O) insurance coverage. The Saskatchewan General Insurance Council (Council) is responsible for administering *The Saskatchewan Insurance Act* relating to licensing brokers. The Council requires licensed brokers to maintain a prescribed level of E&O insurance coverage. SGI requires its brokers to provide information about their E&O coverage at the time of their initial appointment. To ensure its brokers maintain the required coverage, SGI reviews regular Council bulletins that list suspended or cancelled brokers for reasons including lack of adequate E&O insurance coverage. To ensure its out-of-province brokers maintained adequate coverage, SGI follows the same practice of reviewing bulletins of the Council or its equivalent in other provinces.

Regularly ensure brokers' comply with the signed agreements

We expected SGI would have processes to:

- ◆ *verify brokers continue to be licensed;*
- ◆ *ensure timely receipts of money and information about policies sold by brokers and to investigate reasons for delays;*
- ◆ *ensure brokers comply with operational policies and procedures;*
- ◆ *ensure brokers submit insurance requests for policies within their limits;*

- ◆ *evaluate the performance of brokers against established performance targets; and*
- ◆ *report regularly to management and the Audit and Finance Committee on the adequacy of the SGI's systems and practices to manage its insurance brokers.*

As stated earlier, SGI regularly reviews bulletins from the Saskatchewan General Insurance Council and its equivalent authority in other provinces and takes necessary action. In those bulletins, the authorities identify brokers who are suspended or no longer have licences.

SGI has processes to identify brokers who do not pay promptly or provide information about policies late. SGI reviews monthly broker reports showing premiums or information past due. SGI acts to collect premiums owing from brokers. We found that generally brokers submitted the required information promptly.

SGI requires its brokers to comply with operational policies and procedures that SGI provides to brokers. SGI has processes to ensure that brokers do so. Upon receipt of an insurance application or changes to an existing insurance policy, SGI reviews the information package. SGI ensures the insurance risks are acceptable and within the broker's limits, premiums are correct, and the application includes all relevant information (e.g., age and condition of property being insured). SGI may not issue an insurance policy if brokers exceed the authorized limit or if the insurance risk is unacceptable.

Annually, SGI sets performance targets for its brokers. These targets include the type of business, sales, loss ratios, and prompt payment of premiums. SGI regularly monitors brokers' performance against these targets. SGI determines brokers' annual bonuses based on this performance evaluation. To help determine if it deals fairly with brokers, SGI does an annual survey of brokers and makes changes to its evaluation process if necessary.

Management receives regular financial and operational reports. Those reports are timely and include relevant information. Management provides the Audit and Finance Committee of the Board of Directors information about broker management on an exception basis only. Management does so because the Board has not established and documented its reporting

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needs for broker management. To ensure the Board receives the information it needs to oversee this part of SGI's operation, it should document and communicate to management its information needs.