



Insuring in Canada

Considerations for International Programs including Canadian Risks

It is a simple fact of life that more and more business operates across multiple territories. Improved technology and the Internet's instant connections mean that global commerce is now routine. Another reality, however, is that countries around the globe all regulate financial transactions, business and taxation within their own borders individually. No two jurisdictions follow the same rules in protecting their public and various stakeholders.

Cross-border commerce means new compliance and regulatory considerations for clients' insurance programs, considerations about which brokers must be well-informed if they are to offer effective advice and assistance. Today there is an ever-increasing pressure for accountability on governance and compliance, and even existing regulations are attracting renewed attention.

In Canada, recent activity by the federal Canada Revenue Agency (CRA), generally responsible for a number of levels of taxation, illustrates this trend. It can no longer be assumed that formerly-acceptable procedures will still satisfy authorities.

In order for an insurance placement to be compliant, the Canadian Excise Tax Act sets out two requirements:

- **that a risk is insured by a Canadian-licensed Insurer** (authorized by the Office of the Superintendent of Financial Institutions - OSFI - or one of the parallel provincial regulators), **AND**
- **that the PRIMARY broker involved is also licenced within the appropriate province.**

Where these requirements are met, Insurers report to OSFI, which provides solvency and reserve supervision while taxes, built into the premiums, are automatically remitted to the government without client involvement. In addition, the client is now automatically protected by the regulations in place in case of Insurer failure.

If both Excise Tax Act requirements are not satisfied, however, clients immediately incur some serious tax and regulatory exposures:

- tax liabilities, at a minimum of 10% federally but with additional, and sometimes substantial, provincial tax levies

- liability for associated penalties and interest
- potential for unlimited legal and accounting expense, as well as consumption of the client's own time
- potential tax challenges on premium allocations between jurisdictions
- potential complication of claims situations or subsequent accounting treatment of settlement amounts
- lack of protection under Canadian system in the event of an Insurer failure
- responsibility to remit provincial sales taxes

For the non-Canadian broker, as well, a failure to point out and address these risks creates an exposure to their own security.

In the past, CRA often did not challenge cross-border placements, or scrutinize broker relationships. Increasing attention on compliance, however, now forces auditors to work to the 'letter of the law' as they must themselves conform. New specialized resource teams within the CRA are better educated about the insurance industry, but also may be called in during other audits to identify situations where placements are not compliant and excise tax could be assessed.

The result has been many new audit challenges. Even where coverage has been written through Canadian-licensed Insurers, placements are considered non-compliant, and so subject to taxes (plus fines and penalties), if the authorities deem the Canadian broker is not primary – that is, is not “*directly retained or instructed by the insured and not through any other broker or agent*”. Auditors look not only at invoicing and premium flow from client to carrier, but also at the records of various communications. Assessments can go back up to four years.

For example: Manufacturer A has a head office in Houston and plants in six other US states. They also have distribution warehouses in Newmarket, Ontario and Trois-Rivieres, Quebec. Their insurance program is written through Insurer A who does not do business in Canada and so has simply accounted for Canadian premises under 'Unnamed Locations'. When the CRA sends Auditor Z to visit Manufacturer A, a question arises about allocated premiums and the coverage is reviewed. Manufacturer A finds themselves facing assessment and compounded penalties, plus mounting auditor and legal fees.

Similarly: Enterprise B is domiciled in Atlanta with several branches, including one large operation in Winnipeg, Manitoba. B's insurance carrier is licensed in both the US and Canada. Carrier B obtains permission from a Canadian broker to show them as broker of record on the policy, and separate documents are issued. There is no contact, however, between the Canadian broker and the client. When Auditor Z arrives for a routine GST audit, he also asks to see the insurance file. Enterprise B is assessed for Excise tax and penalties going back four years; the CFO's first

urgent and irate call goes to their US broker while her assistant is still tracking down the accountant.

In order to avoid exposure, it is strongly recommended that insurance purchasers and Canadian brokers document:

- **Formal appointment of the Canadian broker possessing the appropriate licences, markets and expertise, on the Canadian portion of the client's program; and**
- **Ongoing direct communication between the insurance purchaser and the Canadian broker, as well as involvement of the broker in Insurer discussions**

The CRA does recognize that risk managers speak directly for the client, that those purchasers may themselves not actually be located in Canada, and that more than one broker may participate in discussions. Again, though, the direct instruction of the Canadian broker by the client is essential.

There is a real role for the local broker in mediating with Insurers. Where the client's Insurer-of-choice is licenced both at home and in Canada, coordination between underwriters ensures that coverage is consistent and that overall costs stay in line. At other times, it may be preferable to place separate coverage with specific Canadian Insurers; in that case, the Canadian broker can still dialogue with those arranging coverage elsewhere to verify consistency.

Of course, business reasons may always dictate an unlicensed placement. In those situations, Canadian regulations require that both the client and broker report those placements by specific deadlines. The specific rules, and in some cases additional procedures required, vary widely between provinces, so expert advice is strongly advised. The client must also remit the relevant taxes due; there are substantial penalties for late filing or remittances.

On occasion, coverage is not available from Canadian-licensed sources, for example, if very large limits or particularly specialized coverage is required. In this case, clients may apply to the CRA for an exemption from the excise tax; if approved, the tax is refunded. Canadian broker associations do work with the CRA to facilitate the exemption-request process, streamlining the documentation required and sharing information about current market availability.

Most often, however, it is in the client's best interests to place a program meeting local requirements. Working with a broker experienced in these situations entails a minimum of extra inconvenience or cost to the client. On the contrary, clients then also derive a host of additional benefits that would otherwise be lacking:

- Avoidance of uncertainty and additional costs
- Direct, personal contact with local client
- Facilitate local service eg certificates & lease reviews, etc.
- Language consideration (eg need for French in Quebec)
- On-the-ground familiarity with exposures, local industry standards and ready access to information
- Leverage with local Insurers and knowledge of the immediate insurance market
- Collection and remittance of provincial sales taxes, where applicable

The domestic broker also gains a trusted Canadian partner to help in supporting the domestic client.

In future, it is possible that legislative changes will adjust the strict requirements, and it will be crucial to maintain awareness of government and CRA positions during that process. For the present, however, authorities will continue to rely on the language of the current statutes. Insurance purchasers must partner with reputable and informed advisors to take this into account in insuring their Canadian risks.

About FCA Insurance Brokers:

FCA Insurance Brokers is an independent, privately-owned brokerage based in Toronto, Canada, specializing since 1919 in custom insurance solutions for commercial and corporate clients across Canada. Within the Canadian and international insurance communities, FCA professionals are active in leadership roles, focusing on compliance, regulatory and competitive issues. With its specialized cross-border practice, FCA is well prepared to work with brokers and their clients in other jurisdictions, who need to ensure that their Canadian insurance program is effected with full attention to value, effectiveness and compliance.