Office of the Superintendent of Financial Institutions Canada
Bureau du surintendant des institutions financières Canada

OSFI ANNUAL REPORT 2014-2015

OSFI
BSIF

Canada

Office of the Superintendent of Financial Institutions Canada

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OSFI at a Glance

- OSFI was established in 1987 to contribute to public confidence in the Canadian financial system. It is an independent agency of the Government of Canada and reports to Parliament through the Minister of Finance.
- OSFI provides prudential regulation and supervision to over 400 banks and insurers, and some 1,200 federally registered private pension plans.
- The Office of the Chief Actuary, which is an independent unit within OSFI, provides actuarial valuation and advisory services for the Canada Pension Plan, the Old Age Security program, the Canada Student Loans Program and other public sector pension and benefit plans.
- OSFI recovers its costs, which in 2014-2015 totalled $144.9 million. OSFI is funded mainly through asset-based, premium-based or membership-based assessments on the financial services industry and a user-pay program for selected services. A very small portion of OSFI's revenue is received through an appropriation from the Government of Canada for actuarial valuation and advisory services relating to various public sector pension and benefit plans.
- As of March 31, 2015, OSFI employed 704 people in offices located in Ottawa, Montréal, Toronto and Vancouver.

Superintendent's Message

It has been a privilege to serve my first year as Superintendent of Financial Institutions, and to helm an agency that plays a central role in maintaining the safety and soundness of Canada's financial system for the benefit of all Canadians. My colleagues have been most welcoming and it is a pleasure to lead such a committed and capable team.

In 2014-2015, OSFI undertook a number of initiatives to further strengthen Canada's system of financial regulation and supervision.

With a view to reinforcing prudent mortgage insurance underwriting, in November 2014, OSFI issued the Residential Mortgage Insurance Underwriting Practices and Procedures guideline, following extensive consultation with the industry. The guideline enhances disclosure practices for mortgage insurers and outlines sound risk management principles, including setting prudent requirements for lenders and applying appropriate due diligence to lenders' practices. As mortgages form the major portion of Canadian household debt, this is an important area of OSFI oversight. This is particularly true in the current low-interest rate environment, given the potential impact rising rates would have on household debt levels.

The global financial crisis underlined the importance of the need for financial institutions to have enough quality capital and liquidity to absorb severe losses. In the past year, OSFI issued new or updated guidelines on Leverage Requirements and Liquidity Adequacy Requirements for deposit-taking institutions, Minimum Continuing Capital and Surplus Requirements for life insurers, and the Minimum Capital Test for property and casualty insurers.

Operational risk at financial institutions was another priority area for OSFI in 2014-2015. Work in this area included conducting supervisory reviews on cyber security and outsourcing risks.

We also continued to monitor the global economy, with a special emphasis on assessing the potential impact of various events on the risk profiles of federally regulated financial institutions and pension plans. There remain a number of potential risks to continued global economic recovery, including sovereign debt issues and low growth. Further, the International Monetary Fund (IMF) has noted that protracted low inflation, or even deflation, pose risks in some advanced economies.

OSFI does not work in isolation. Canada's strong regulatory regime is a result of the cooperation and collaboration that exists among our government partners, who are the Bank of Canada, the Department of Finance, Canada Deposit Insurance Corporation, and the Financial Consumer Agency of Canada. This collaboration was highlighted in the 2014 report of the IMF's Financial Sector Assessment Program review of Canada, which spoke favourably of the effectiveness of the oversight of Canada's financial system.

Internally, OSFI continues to enhance both our supervisory capacity and processes. In 2014-2015, we launched a multi-year project that will lead to improved supervisory tools, and we continued the development of a supervision training program to support the needs of supervisory employees.

In my first year as Superintendent, I have observed close at hand the sustained dedication of my OSFI colleagues. Their professionalism, knowledge and integrity continue to contribute to our collective success and allow Canadians to continue to have confidence in Canada's financial system.

Jeremy Rudin

Performance against Priorities 2014-2015

OSFI identified five priorities for 2014-2015 through which to achieve its mandate. This section reports key accomplishments under each of those priorities. OSFI achieved its goals for the reporting year and continues to work on these multi-year priorities. More details are available in subsequent chapters of this report.

PRIORITY A – Anticipating and Responding to Risks Emanating from the Economy and Financial System

Steps Taken

- Issued the final version of the Residential Mortgage Insurance Underwriting Practices and Procedures guideline
- Continued development of a new capital framework for mortgage insurers
- Conducted stress tests for the largest banks and life insurers that included the impact of high consumer debt and other adverse shocks
- Conducted supervisory reviews focused on cyber security self-assessments and outsourcing
- Responded to recommendations from the International Monetary Fund (IMF) Financial Sector Assessment Program (FSAP) update for Canada

PRIORITY B – Enhancing Supervisory Processes

Steps Taken

- Embarked on a multi-year project to improve OSFI supervisory tools and technology, with Phase 1 completed and Phase 2 launched
- Conducted a pilot assessment of risk culture at a federally regulated financial institution (FRFI), with plans to develop and roll out an OSFI approach over time at large complex institutions
- Completed reviews of the internal audit function of a number of FRFIs (banks and insurance companies) in the context of their risk management practices

PRIORITY C – Anticipating and Responding to Risks Emanating from Regulatory Reform

Steps Taken

- Issued new/revised guidelines, advisories or letters, including
    - Liquidity Adequacy Requirements guideline
    - Leverage Requirements guideline
    - Minimum Continuing Capital and Surplus Requirements (MCCSR) guideline
    - Minimum Capital Test (MCT) guideline
    - Derivatives Sound Practices guideline
    - Changes to the Membership of the Board or Senior Management advisory

    - Early Adoption of IFRS 9 Financial Instruments for Domestic Systemically Important Banks advisory

- Issued a policy paper for the Life Insurance Capital Framework Standard Approach, as well as Quantitative Impact Study No. 6 on various aspects of the framework

- Participated actively on various international committees that develop regulatory frameworks for banks and insurers, including
    - Financial Stability Board (FSB)
    - Basel Committee on Banking Supervision (BCBS)
    - International Association of Insurance Supervisors (IAIS)

PRIORITY D – A High-Performing and Effective Workforce

Steps Taken

- Initiated the development of a multi-year Supervision training program to support the needs of Supervision Sector employees

- Ensured change management work streams were built into all IM/IT projects

- Continued enhancements to the corporate planning processes to further integrate Human Resources planning and Enterprise Risk Management processes

- Implemented targeted action plans where necessary to address areas identified for improvement in the 2013-1014 employee survey

PRIORITY E – An Enhanced Corporate Infrastructure

Steps Taken

- Completed the five-year Information Technology Renewal program, including implementation of
    - an integrated Enterprise and Resource Planning module for Finance-related processes (SAP)
    - a Correspondence and Enquiry Management system for external inquiries
    - a Regulatory Returns System (jointly with the Bank of Canada and Canada Deposit Insurance Corporation) for validation and processing of all regulatory return data
    - an upgraded Business Intelligence solution to provide robust insurance industry data for analysis

- Continued to apply the Regulatory Data Governance Framework to approve and prioritize OSFI regulatory data requests

The above five priorities will also guide the achievement of strategic outcomes for 2015-2016. Details can be found on OSFI's website.

Corporate Overview

Role and Mandate

OSFI was established in 1987 by an Act of Parliament: the *Office of the Superintendent of Financial Institutions Act* (OSFI Act). OSFI supervises and regulates all banks in Canada and all federally incorporated or registered trust and loan companies, insurance companies, cooperative credit associations, fraternal benefit societies and private pension plans. Under the OSFI Act, the Superintendent is solely responsible for exercising OSFI's authorities and is required to report to the Minister of Finance from time to time on the administration of the financial institutions legislation.

OSFI's mandate is to:

- Supervise federally regulated financial institutions and private pension plans to determine whether they are in sound financial condition and meeting minimum plan funding requirements respectively, and are complying with their governing law and supervisory requirements;
- Promptly advise institutions and plans in the event there are material deficiencies and take, or require management, boards or plan administrators to take, necessary corrective measures expeditiously;
- Advance and administer a regulatory framework that promotes the adoption of policies and procedures designed to control and manage risk;
- Monitor and evaluate system-wide or sectoral issues that may have a negative impact on institutions.

From its mandate, OSFI has identified two strategic outcomes:

1. A safe and sound Canadian financial system
2. A financially sound and sustainable Canadian public retirement income system

OSFI's legislation acknowledges the need to allow institutions to compete effectively and take reasonable risks. It also recognizes that management, boards of directors and plan administrators are ultimately responsible and that financial institutions and pension plans can fail.

OSFI works with a number of key partners on the Financial Institutions Supervisory Committee (FISC), which the Superintendent chairs, including the Department of Finance, the Bank of Canada, Canada Deposit Insurance Corporation and the Financial Consumer Agency of Canada. Together, these organizations constitute Canada's network of financial regulation and supervision, and provide a system of depositor and policyholder protection.

The Office of the Chief Actuary (OCA), which is an independent unit within OSFI, provides actuarial valuation and advisory services to the Government of Canada in the form of reports tabled in Parliament. While the Chief Actuary reports to the Superintendent, he is solely responsible for the content and actuarial opinions in reports prepared by the OCA. He is also solely responsible for the actuarial advice provided by the OCA to the relevant government departments, including the executive arm of provincial and territorial governments, which are co-stewards of the Canada Pension Plan (CPP).

Financial Resources

OSFI recovers its costs, as stipulated under the OSFI Act. The organization is funded mainly through asset-based, premium-based or membership-based assessments on the financial services industry and a user-pay program for selected services. A very small portion of OSFI's revenue is received through an appropriation from the Government of Canada, primarily for actuarial valuation and advisory services relating to the Canada Pension Plan, the Old Age Security program, the Canada Student Loans Program and various public sector pension and benefit plans.

Human Resources

As at March 31, 2015, OSFI employed 704 people in offices located in Ottawa, Montréal, Toronto and Vancouver.

Accountability

Auditing

OSFI's Audit Committee met five times in 2014-2015. The Committee is comprised of three independent members, one of whom is the Chair, and the Superintendent. The mandate of the Committee

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Human Resources and Administration
Corporate Services Sector

Liz Amorim
Classification Advisor
Human Resources and Administration
Corporate Services Sector

is to provide objective advice and recommendations to the Superintendent regarding the adequacy and proper functioning of OSFI's risk management, control and governance frameworks and processes, including accountability and auditing systems. During 2014-2015, the Audit Committee received information and, as appropriate, provided advice and guidance on key activities including but not limited to: Enterprise Risk Management; Quarterly and Annual Financial Statements; IM/IT Strategy; Performance Measurement Reporting; Internal Control over Financial Reporting; Values and Ethics; Internal Audit reports; and Internal Audit operations.

Surveys and Consultations

OSFI routinely undertakes consultations with the financial institutions it regulates to help assess its performance and effectiveness as a regulator. Copies of the research reports are available on OSFI's website.

- In the fall of 2014, Environics Research Group conducted on OSFI's behalf its biennial Financial Institutions Survey, an online tracking survey of CEOs across all federally regulated financial institutions.

- In the fall of 2014, Harris-Decima acting on OSFI's behalf conducted OSFI's Pension Plans Survey, an online tracking survey of plan administrators and professional advisors of federally regulated private pension plans.

- In the winter of 2014, The Strategic Counsel conducted on OSFI's behalf an in-depth consultation with the property and casualty (P&C) insurance sector. The consultation is part of OSFI's three-year, rotating, sector consultation program. The consultation comprised a series of confidential, one-on-one interviews with a sample of senior executives representing a cross-section of P&C companies regulated by OSFI.

The overall results of these consultations were positive, with participants indicating high levels of satisfaction with OSFI. Some areas for improvement were also identified and, where appropriate, OSFI has developed action plans to address these.

Benefits to Canadians

OSFI's strategic outcomes, supported by our plans and priorities, are intrinsically aligned with broader government priorities, specifically strong economic growth, and income security and employment for Canadians. A properly functioning financial system that inspires a high degree of confidence among consumers and others who deal with financial institutions makes a material contribution to Canada's economic performance.

Mark Zelmer, Deputy Superintendent, Regulation Sector • **Jeremy Rudin,** Superintendent of Financial Institutions • **Gary Walker,** Assistant Superintendent, Corporate Services Sector

Jamey Hubbs was named Assistant Superintendent, Deposit-taking Supervision Sector, in April 2015.

Federally Regulated Financial Institutions

Risk Assessment and Intervention

OSFI supervises federally regulated financial institutions (FRFIs), monitors the financial and economic environment to identify issues that may have a negative impact on these institutions, and intervenes in a timely manner to protect depositors and policyholders from loss. In doing so, OSFI recognizes that management and boards of directors of FRFIs are ultimately responsible and that those institutions can fail.

In 2014-2015, high levels of domestic household indebtedness, exceptionally low interest rates, falling oil prices and ongoing global financial uncertainty continued to be seen as sources of potential systemic vulnerability. OSFI took action to address the possible impact of these challenges and achieve its strategic priorities by communicating its expectations for risk management to FRFIs and conducting significant reviews in several areas, including stress testing, cyber security, risk data aggregation, outsourcing, and internal audit. We continued to develop supporting guidance for OSFI's Supervisory Framework and initiated a review of our supervisory processes and tools.

Review by Sector

Deposit-Taking Institutions

The Canadian banking industry is comprised of six large domestic banks designated as domestic systemically important banks (D-SIBs) and many smaller deposit-taking institutions (DTIs). The six largest banks account for approximately 90% of total assets among Canada's federally regulated DTIs. Their diversified business lines extend beyond traditional deposit-taking and lending activities into trading, investment banking, wealth management and insurance. In addition to their primary domestic focus, these large banks also have operations in many countries across the globe.

The remaining 10% of Canadian banking assets are held by smaller institutions with niche market and business strategies, such as mortgage lending, commercial real estate or credit cards.

Overall, return on equity for the industry was roughly unchanged in 2014 from 2013, remaining around 16%. The main contributing factors were higher revenues, offset by higher non-interest expenses, and a stable credit environment that drove solid profitability. While loan loss provisions for corporate and retail lending (mortgages, auto loans, credit cards) remained low, vulnerabilities continue related to lower oil and gas prices and other economic risks, as well as high household debt levels.

OSFI fully implemented the Basel III capital rules, and banks began reporting the new Common Equity Tier 1 (CET1) capital adequacy ratios in 2013. Canadian bank capital ratios remain above the target level of 7% for CET1; and the six large domestic banks remain above their higher (8%) capital requirements. OSFI implemented a new liquidity adequacy framework – which includes the Basel III Liquidity Coverage Ratio (LCR) requirement – that came into effect in

January 2015. At the same time, the Basel III leverage framework and associated minimum 3% Leverage Ratio (LR) requirement replaced the Assets to Capital Multiple (ACM) leverage constraint. Canadian banks that have reported first quarter results (e.g. D-SIBs, and other banks with October year-ends) show ratios well above the minimum requirements.

Life Insurance

The capital metric used to assess capital adequacy for supervisory purposes is the Minimum Continuing Capital and Surplus Requirement (MCCSR) for federally regulated Canadian life insurance companies, and the Test of Adequacy of Assets and Margin (TAAM) for branches of foreign companies operating in Canada. The requirements for calculating the metrics are updated each year.

In January 2015, OSFI released a policy paper outlining a new standard approach for the life insurance regulatory capital framework. This framework considers recent developments in financial reporting, actuarial methodology, economic capital and financial theory. The framework is intended to provide an improved assessment of solvency risk, and promote improved risk management and business decisions. Industry input is being sought on the policy paper. In addition, quantitative impact studies are being conducted to assess the potential effect of the changes on the life insurance industry. This new regulatory capital framework will be implemented in January 2018.

The aggregate capital ratio for the life insurance industry at year-end 2014 was 239% compared to 242% for 2013. The aggregate level has been well above OSFI's minimum requirements for the last several years as a result of improvement and stability in capital and equity markets, decreasing product guarantees, and product re-pricing. While low long-term interest rates present a continuing strain on profitability, companies have strengthened their balance sheets and persisting low long-term interest rates will not affect solvency.

Return on equity for the industry was 11% and net income was $10.8 billion in 2014, compared to 10% and $8.1 billion respectively in 2013. Approximately 75% of the industry net income is attributable to the three large conglomerates. Net income benefitted from improving equity markets and re-pricing of products to reflect changed market conditions. Challenges remain with persistently low interest rates, which make asset/ liability management more difficult and strain in-force product profitability as many of these products cannot be re-priced due to contractual provisions. There is also the potential for future adverse equity market changes due to instability in the global economy. However, those companies with large exposure to products with market guarantees have adequate capital to withstand a substantial decline in the equity markets.

Property and Casualty Insurance (excluding mortgage insurance)

The financial performance of the property and casualty (P&C) industry in Canada in 2014 improved over that of the previous year, which had been undermined by large insurance claims arising from the Calgary flood and the Toronto rain storm in 2013. Lower claims in 2014 increased underwriting profitability to $732 million from

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$109 million in 2013. Net income for the P&C industry of $4.0 billion increased 60% over the previous year's net income, bolstered by underwriting profits for the industry as well as investment returns at a few select FRFIs.

A key measure of the industry's core profitability is the 'combined ratio', which measures the revenue from premiums relative to the sum of claims plus expenses. A combined ratio under 100% indicates that premium income exceeds claims and expenses, and that an underwriting profit has been earned. In 2014, the combined ratio was 98.7%, an improvement over 2013's break-even combined ratio of 100.2%.

For the P&C industry, investment income before realized gains of $3.2 billion in 2014 was approximately a 25% improvement over 2013, and driven by a few insurers holding their investments at fair value. Most insurers continued to record low investment yields in 2014, reflecting the lower yields available as the portfolio is reinvested and highlighting the importance of core underwriting to achieve and sustain financial results.

The Minimum Capital Test (MCT) is the capital metric for Canadian P&C companies while the Branch Adequacy of Assets Test (BAAT) is used for foreign-owned P&C operations in Canada. Capital ratios for the P&C industry in 2014 improved over 2013, increasing to 269% from a 257% industry-weighted MCT/BAAT ratio – well above OSFI's supervisory target of 150%.

With nearly half of the Canadian P&C insurance industry (by premium volume) being foreign owned (ultimate parents are typically located in the United States or Europe), market conditions in the home jurisdiction can affect Canadian operations; consequently, OSFI continues to monitor parent company conditions.

Domestically, personal auto insurance continued to be the major underwriting challenge, as the auto insurance loss ratio continues to deteriorate. While anticipated impacts of the 2010 Ontario auto insurance reforms have been realized, pressure on Ontario loss ratios is expected to continue with 7% of the targeted 15% reduction slated for August 2015 taking effect in 2015. In Alberta and some Atlantic provinces, auto insurance loss ratios also increased in 2014.

Mortgage Insurance

The private mortgage insurance industry in Canada experienced stable financial results during 2014. The net income of federally regulated private mortgage insurers in Canada rose 7% to $454 million, reflecting higher underwriting income that offset a modest decline in investment returns. The MCT capital ratio also remained largely stable, rising one (1) point to 221%, and above OSFI's supervisory requirement of 150%. Notwithstanding the currently favourable financial results, mortgage insurance remains vulnerable to both consumer debt levels and the potential impact of sustained low oil prices in certain Canadian regions.

Supervisory Tools

Managing Risk Effectively

In 2014-2015, OSFI continued updating internal guidance to support its risk-based Supervisory Framework, which considers an institution's inherent business risks, risk management practices (including corporate governance) and financial condition.

OSFI again held annual risk management seminars in 2014-2015 for the industries it regulates (DTIs, life insurance, and P&C insurance) to reinforce the need for strong risk management and to share lessons learned. The goal is to communicate OSFI's expectations related to key risk management areas based on detailed work OSFI has undertaken during the year, and to share information on issues being discussed internationally by regulators. The seminars also provide participants with the opportunity to ask questions of OSFI's senior supervisory and regulatory teams.

Continuing the practice of organizing Colleges of Supervisors, in 2014-2015 OSFI hosted a college for each of Canada's five largest banks. In line with Financial Stability Board recommendations, the colleges brought together executives from each bank with supervisors from jurisdictions where they do business. OSFI also hosted a supervisory college for a large life insurance company. Crisis management and industry information sessions were again held for the seven largest deposit-taking institutions, in conjunction with Canada Deposit Insurance Corporation.

Composite Risk Ratings

The Composite Risk Rating (CRR) represents OSFI's overall assessment of an institution's safety and soundness. Beginning in 2013-2014, a Branch Risk Rating (BRR) was assigned to Foreign Bank Branches (FBBs) operating in Canada, rather than a CRR, reflecting OSFI's limited access to the information needed to assess the FBB's safety and soundness.

There are four possible risk ratings: ‘low’, ‘moderate’, ‘above average’ and ‘high’. The CRR is reported to most institutions at least once a year (certain inactive or voluntary wind-up institutions may not be rated). The Supervisory Information Regulations for both banks and insurance companies prohibit institutions (or OSFI) from publicly disclosing their rating. As at the end of March 2015, OSFI had assigned CRR ratings of low or moderate to 91% and above average or high to 9% of all CRR-rated institutions. These percentages are unchanged from the previous year.

Intervention Ratings

Financial institutions are also assigned an intervention (stage) rating, as described in OSFI’s guides to intervention for FRFIs, which determines the degree of supervisory attention they receive. Broadly, these ratings are categorized as: normal; early warning (stage 1); risk to financial viability or solvency (stage 2); future financial viability in serious doubt (stage 3); and non-viable/insolvency imminent (stage 4). As at March 31, 2015, there were 23 staged institutions. With a few exceptions, most of the staged institutions were in the early warning (stage 1) category.

Regulation and Guidance

OSFI provides a regulatory framework of guidance and rules that meets or exceeds international minimums for financial institutions. In addition to issuing guidance, OSFI provides input into the development of federal legislation and regulations affecting federally regulated financial institutions (FRFIs) and comments on accounting, auditing and actuarial standards development, which includes determining how to incorporate them into our regulatory framework. OSFI also participates in a number of international and domestic rule-making activities.

Trenton Haggard
Manager
Property and Casualty Insurance Group
Supervision Sector

Shelina Visram
Manager
MFC Team
Supervision Sector

DOMESTIC RULE MAKING

Accounting, Auditing and Actuarial Standards

OSFI is a member of the Canadian Accounting Standards Board's (AcSB) User Advisory Council and an observer on the Insurance Accounting Task Force. With respect to auditing standards, OSFI is a non-voting member of the Auditing and Assurance Standards Oversight Council, which oversees the activities of the Canadian Auditing and Assurance Standards Board (AASB). OSFI also holds a seat on the Canadian Public Accountability Board (CPAB) Council of Governors which carries out an annual high-level assessment of CPAB against its mandate.

In 2014-2015, OSFI issued industry-wide letters promoting relevant domestic and international external audit quality initiatives to assist audit committees, or those charged with governance, in their oversight responsibilities with respect to the external auditor and the statutory audit.

Jennifer Shon
Analyst
Capital Banking
Regulation Sector

Anthony Haddad
Senior Economist
Legislation and Policy Initiatives
Regulation Sector

In addition to a position on domestic audit quality initiatives, OSFI issued an advisory outlining expectations regarding early adoption of IFRS 9 Financial Instruments.

OSFI works closely with the Canadian Institute of Actuaries (CIA) and the Actuarial Standards Board (ASB) to ensure that actuarial standards are appropriate and lead to acceptable practice in areas such as valuation, risk and capital assessment at entities regulated by OSFI. In 2014-2015, we continued to participate on several CIA practice committees and to consult with the CIA on developments related to our work on a new solvency framework for life insurance companies.

OSFI also works with the International Actuarial Association (IAA) and supports the profession in establishing guidance related to initiatives on insurance company valuation for International Financial Reporting Standards (IFRS) and the International Association of Insurance Supervisors (IAIS) Insurance Capital Standard (ICS).

Capital and Liquidity Guidance

Deposit-Taking Institutions

Capital Adequacy Requirements

In October 2014, OSFI released the final version of its Leverage Requirements guideline, which transposed the leverage requirements issued by the Basel Committee on Banking Supervision (BCBS) into guidance appropriate for Canadian banks, federally regulated trust and loan companies and retail associations. Effective January 2015, the guideline replaced the formerly used Assets to Capital Multiple by the leverage ratio requirement.

Liquidity Requirements

In May 2014, OSFI released the final version of its Liquidity Adequacy Requirements guideline, which came into effect as of January 2015. The guideline reflects internationally agreed minimum standards for the measurement of short-term liquidity under a stress scenario that will be applied to all banks, bank holding companies, and trust and loan companies in Canada. In the area of liquidity-related disclosures, OSFI issued a guideline in July 2014.

Life Insurance Companies

OSFI undertook its annual update of the Minimum Continuing Capital and Surplus Requirements (MCCSR) guideline during 2014, with the revised version coming into effect for the 2015 fiscal year. With stakeholder input considered, the guideline was updated to clarify a number of elements. Furthermore, a sixth Quantitative Impact Study (QIS) was issued in November 2014 to gather information related to potential methods for determining the capital requirements for credit, market, insurance and operational risk calculations. Industry submissions were received in early 2015 and the results are being analyzed. Other elements of the new Life Insurance Solvency Framework Standard Approach, such as capital resources and segregated funds, are also under development in collaboration with the industry. The whole framework is scheduled for implementation in 2018.

Property and Casualty Insurance Companies

In September 2014, after extensive industry consultation, OSFI issued the final version of its significantly revised Minimum Capital Test (MCT). The revised guideline is in keeping with OSFI's long-term plan and priorities to ensure the MCT remains risk sensitive and forward-looking.

The property and casualty (P&C) MCT Advisory Committee continued to develop a framework for the use of company-specific models to determine capital requirements for P&C insurance companies.

OSFI is also developing new capital rules for mortgage insurers. These more risk-based capital requirements are expected to be implemented in 2017.

Other Guidance

Changes to the Membership of the Board or Senior Management

In May 2014, OSFI issued its final guidance on Changes to the Membership of the Board or Senior Management, which outlines the process for FRFIs to notify OSFI about potential membership changes to their board or senior management. It further reinforces that decisions on such changes remain with FRFIs themselves, clarifying that OSFI's approval or vetting is not required. In permitting effective regulatory engagement and respecting FRFIs' need to make independent decisions, the advisory strikes the appropriate balance in the Canadian context.

Derivatives Sound Practices

In January 2015, OSFI issued the final version of its revised guideline on Derivatives Sound Practices, The revised guideline reflects the over-the-counter (OTC) derivatives market reforms initiated by G20 leaders, and communicates OSFI's expectations for central clearing of standardized OTC derivatives and reporting of derivatives data to a trade repository. The guideline also mirrors current risk management practices with respect to derivatives activities.

Regulatory Compliance Management

In November 2014, OSFI released the final version of its updated guideline on Regulatory Compliance Management. The guideline, which sets out OSFI's expectations with respect to the management of regulatory compliance risk inherent in FRFIs' business activities, received numerous updates to ensure better alignment with some of OSFI's more recently updated guidance, such as the Corporate Governance guideline and the Supervisory Framework.

Residential Mortgage Insurance Underwriting

As a follow-up to the Residential Mortgage Underwriting Practices and Procedures guideline issued in June 2012, OSFI released the final version of its guideline on Residential Mortgage Insurance Underwriting Practices and Procedures in November 2014. This guideline reinforces prudent mortgage underwriting by introducing expectations for mortgage insurers that complement those applicable to lenders. The date for full implementation of the guideline by mortgage insurers was set for June 30, 2015, with the relevant public disclosures beginning with the quarter ending September 30, 2015.

Anti-Money Laundering (AML) and Anti-Terrorism Financing (ATF)

At the international level, work on strengthening the financial system against money laundering and terrorism financing is led by the Financial Action Task Force (FATF). During 2014-2015, OSFI continued its support of FATF guidance development on money laundering/terrorist financing risks and risk management. In addition, OSFI contributed a financial assessor to the mutual evaluation by the FATF of compliance by Spain with the FATF's 2012 AML/ATF standards. As a member of the Basel Committee on Banking Supervision's AML Experts Group, OSFI participated in updating guidance on AML/ATF risk management.

Nationally, OSFI is one of a number of federal departments and agencies, led by the Department of Finance, which participated in the development of an assessment of inherent money laundering and terrorist financing risks in Canada. In addition, we contributed to preparations for Canada's next mutual evaluation by the FATF, to be conducted in 2015-2016. During 2014-2015, OSFI continued consultations with the Department of Finance on draft AML/ATF legislation and regulations that will impact the financial sector.

During 2014-2015, OSFI continued its AML/ATF supervisory assessment program and regular follow-up work at a wide variety of large and small financial institutions. The assessment program is conducted in partnership with the Financial Transactions and Reports Analysis Centre of Canada (FINTRAC). As financial institutions' AML/ATF programs have become more mature, we have responded with a greater emphasis on monitoring improvements to FRFIs' AML/ATF controls.

Via its website, OSFI continued its role as lead communicator in helping to ensure that the Canadian financial sector is promptly notified of sanctions imposed by the United Nations Security Council (UNSC) and the Government of Canada on terrorists and terrorist organizations, as well as UNSC sanctions against Iran and North Korea.

INTERNATIONAL ACTIVITIES

International organizations play a key role in the development of regulatory frameworks for banks and insurers and OSFI is an active participant in a number of these groups, including the Financial Stability Board, Basel Committee on Banking Supervision, and International Association of Insurance Supervisors.

Financial Stability Board

The Financial Stability Board (FSB) was established in April 2009 to coordinate, at the international level, the work of national financial authorities and international standard setting bodies. It develops and promotes the implementation of effective regulatory, supervisory and other financial sector policies.

Canadian representation on the FSB is shared by the Department of Finance, the Bank of Canada and OSFI. During 2014-2015, OSFI continued its involvement with the FSB through membership on the FSB Plenary, Steering Committee, and Standing Committee on Supervisory and Regulatory Cooperation.

Some of the work in which OSFI and its Canadian partners participated during 2014-2015 included:

- further developing the international standard to enhance the total loss-absorbing capacity of global systemically important banks (G-SIBs) in resolution, with the aim to finalize the standard by the G20 Summit in November 2015;
- actions to strengthen the resilience of market-based finance, including further developing standards around securities financing transactions; and
- work to finalize implementation of the G20 financial sector reforms, including in the areas of resolution regimes and over-the-counter derivatives.

Basel Committee on Banking Supervision

OSFI is an active member of the Basel Committee on Banking Supervision (BCBS), which provides a forum for international rule making and cooperation on banking supervisory matters.

The BCBS provides regular updates on the progress of member countries in implementing Basel standards. OSFI has actively supported the international work done to determine whether internationally active banks are calculating the risk-weighted assets portion of minimum capital ratio standards in a consistent manner.

In 2014-2015, OSFI participated in quantitative impact studies and multiple work streams reporting to the BCBS. These resulted in a first round of proposals to further reduce excessive variability in the calculation of minimum capital requirements, including: capital floors, revised Standardized Approaches to operational and credit risk, and a fundamental review of modeling standards for trading book risks.

OSFI confirmed the prudence of its minimum capital requirements during 2014-2015 by participating in the Regulatory Consistency Assessment Programme (RCAP), which assigned an overall "Compliant" rating for Canada (in contrast to "Largely Compliant" and "Materially Non-Compliant" ratings for some of its peers reviewed during the same period) for its implementation of Basel III capital requirements in Canada. In addition, OSFI's Deputy Superintendent led the RCAP assessment of the European Union (EU) in this regard. The RCAP report on the EU was published in December 2014. OSFI also continued its leadership role in benchmarking studies to gauge consistency across jurisdictions for the treatment of risk-weighted assets in the determination of capital ratios of global banks. This work is being conducted with the goal of achieving more consistent implementation of international risk-based capital standards.

International Accounting and Auditing Standards

Since all FRFIs in Canada are required to follow International Financial Reporting Standards (IFRS) and International Standards on Auditing (ISA), OSFI interprets and assesses international rules that may apply to Canadian financial institutions. OSFI works with the International Accounting Standards Board (IASB) and International Auditing and Assurance Standards Board (IAASB) through active participation and leadership in the Accounting Experts Group of the BCBS and the Accounting and Auditing Working Group of the International Association of Insurance Supervisors (IAIS). In 2014-2015, OSFI worked through the BCBS and IAIS to provide its positions on:

- IAASB Proposed Strategy for 2015-2019 and Proposed Work Program for 2015-2016
- IAASB Exposure Draft: Proposed ISA 720 (Revised) The Auditor's Responsibilities Relating to Other Information
- IAASB Exposure Draft: Proposed Changes to the International Standards of Auditing (ISAs) - Addressing Disclosures in the Audit of Financial Statements
- IASB Exposure Draft: Disclosure Initiative - Proposed amendments to IAS 1
- IASB Discussion Paper: Accounting for Dynamic Risk Management: A Portfolio Revaluation Approach to Macro Hedging

In addition, OSFI actively participated in the BCBS initiative to revise BCBS guidance on Sound Credit Risk Assessment and Valuation for Loans to address the new IASB accounting standard IFRS 9 dealing with expected credit losses (ECL). The consultation paper *Guidance on accounting for expected credit losses* was published for comment. It sets out supervisory requirements on sound credit risk practices associated with the implementation and ongoing application of ECL accounting frameworks in a robust, high quality and consistent manner. This guidance is expected to be finalized in 2016 in order for internationally active banks to apply the guidance for implementation of IFRS 9 in 2018.

Active participation in the development of these standards promotes a set of high-quality global standards and enhances our understanding of key IFRSs and ISAs that impact FRFIs. Significant changes to accounting standards require early involvement and close consultation and communication with standard setters, other regulators, and both international and domestic firms. OSFI collaborates closely with all stakeholders as key accounting and auditing standards are developed. For example, during 2014-2015, OSFI worked closely with the Actuarial Standards Board and the International Actuarial Association on setting standards, particularly in relation to IFRS 4 Insurance Contracts.

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International Association of Insurance Supervisors

OSFI participates in the work of the International Association of Insurance Supervisors (IAIS), which represents the insurance regulators and supervisors of approximately 140 countries. IAIS objectives are to contribute to the improved supervision of the insurance industry for the protection of policyholders worldwide, to promote the development of well-regulated insurance markets and to contribute to global financial stability.

OSFI is a member of the IAIS Executive, Technical, Financial Stability, and Audit and Risk committees, Supervisory Forum, and several working groups. In October 2013, the IAIS announced plans to develop a risk-based global Insurance Capital Standard (ICS). Through various committees, OSFI is engaged in the development of the ICS, which is targeted for completion by 2016, with full implementation to begin in 2019. To that effect, the IAIS issued the *Risk-based Global Insurance Capital Standard* public consultation document in December 2014. In the interim, the IAIS completed a basic capital requirement in October 2014 for implementation by global systemically important insurers (G-SIIs) in 2017. Through its continued involvement in the Higher Loss Absorbency Drafting Group and the Field Testing Task Force, OSFI is playing a key role in the development of these very important projects.

As a member of the IAIS Financial Stability Committee, OSFI is participating in the refinement of the methodology to assess which, if any, reinsurance companies may be global systemically important insurance institutions and what kind of supervisory measures would apply to those identified as such. This IAIS initiative will extend through 2015.

Through membership on the Accounting and Auditing Working Group, OSFI continues to monitor key developments and contribute to international policy work on issues of main concern to OSFI, such as the IASB's key insurance project IFRS 4 Insurance Contracts.

Approvals and Precedents

The *Bank Act, Trust and Loan Companies Act*, *Insurance Companies Act*, and *Cooperative Credit Associations Act* require federally regulated financial institutions (FRFIs) to seek regulatory approval from the

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Laura Nicholl
Senior Supervisor
BMO Team
Supervision Sector

Superintendent of Financial Institutions or the Minister of Finance (after receiving the recommendation of the Superintendent) prior to engaging in certain transactions or business undertakings.

Regulatory approvals are also required by persons wishing to incorporate a FRFI, and by foreign banks or foreign insurance companies wishing to establish a presence or to make certain investments in Canada. OSFI administers a regulatory approval process that is prudentially effective, responsive and transparent. OSFI's Approvals division is responsible for making recommendations to the Superintendent and to the Minister regarding those matters requiring regulatory approval.

In 2014-2015, OSFI processed 223 applications of which 200 were approved. Individual applications often contain multiple approval requests. The 200 approved applications involved a total of 371 approvals, 286 of which were granted by the Superintendent and 85 by the Minister. This represents an increase relative to last year, when 199 applications were processed. Most applications for 2014-2015 related to property and casualty (P&C) insurers (47%) and banks (41%). *(See figure 1)*

In 2014-2015, OSFI processed 223 applications of which 200 were approved and 23 were withdrawn.

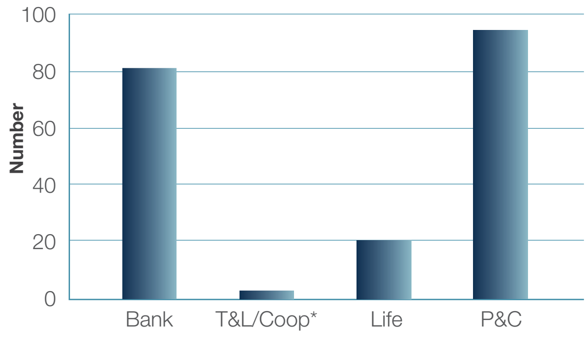
The most common applications received from deposit-taking institutions related to purchases or redemptions of shares or debentures, substantial investments, and transfers of assets in excess of 10%. Applications received from insurance companies related mainly to reinsurance with related unregistered reinsurers, amending orders to commence and carry on business or insuring in Canada of risks, and purchases or redemptions of shares or debentures.

During 2014-2015, letters patent were granted incorporating Esurance Insurance Company of Canada as a Canadian P&C insurer. In addition, orders authorizing the establishment of a foreign insurance branch in Canada were issued to Arch Reinsurance Company, XL Specialty Insurance Company, Technology Insurance Company, and Hannover Re (Ireland) Limited.

Upon request, OSFI also provides advance capital confirmations on the eligibility of proposed capital instruments. A total of 43 such opinions and validations were provided in 2014-2015, compared to seven the previous year.

FIGURE 1

Approved Applications by Industry 2014-2015



*Trust and Loan/Cooperative Associations

In 2014-2015, OSFI processed 223 applications of which 200 were approved and 23 were withdrawn.

OSFI has performance standards establishing time frames for processing applications for regulatory approval and for other services, all of which were surpassed during 2014-2015. More information on service performance standards can be found on OSFI's website.

Guidance and Education

In keeping with the objective of enhancing the transparency of OSFI's legislative approval process and promoting a better understanding of our interpretation of the federal financial institution statutes, OSFI develops and publishes legislative guidance including advisories, rulings, and transaction instructions. In 2014-2015, OSFI made revisions to the following guidance documents:

- Guide for Incorporating Banks and Federally Regulated Trust and Loan Companies
- Advisory on the Legislative Framework for Foreign Banks
- Advisories on Substantial Investments
- Transaction Instructions on Related Party Asset Transactions as Part of a Restructuring
- Transaction Instructions on Related Party Asset Transactions with a Financial Institution

Federally Regulated Private Pension Plans

OSFI supervises federally regulated private pension plans and intervenes in a timely manner to protect members and beneficiaries of such pension plans from loss, while recognizing that plan administrators are ultimately responsible and that funding difficulties can result in a loss of benefits.

Approximately 6% of private pension plans in Canada are federally regulated (Statistics Canada data as at January 2013). As at March 31, 2015, 1,226 private pension plans were registered under the *Pension Benefits Standards Act, 1985*, covering over 1,076,000 active members and other beneficiaries in federally regulated areas of employment, such as banking, inter-provincial transportation and telecommunications. Between April 1, 2014 and March 31, 2015, federally regulated private pension plan assets increased by slightly more than 10%, to a value of approximately $189 billion (*see figure 2*).

Private Pension Environment

Following a year that brought a significant overall improvement in the health of federally regulated private pension plans, 2014 marked the return to a more challenging economic environment. Though equity markets for 2014 as a whole were generally strong, the overall solvency position of defined benefit pension plans deteriorated. This was due primarily to further declines in long-term interest rates which, after having risen somewhat in the latter part of 2013, resumed their decline to historic lows in 2014 and into 2015. However, the impact of this deterioration in solvency positions on required solvency funding payments is expected to be moderated for most federally regulated defined benefit pension plans, as federal solvency funding requirements are based on a pension plan's average solvency position over the past three years. For federally regulated defined benefit pension plans as a whole, the three-year average solvency ratio for the period ending December 2014 is slightly higher than it was for the period ending December 2013.

The sustained low interest rate environment, ongoing market volatility and improvements in longevity are leading plan sponsors and administrators to consider new ways to manage pension funding risks. At the same time, new pension plan designs are being explored, as evidenced by the Government of Canada's consultation paper issued in April 2014 on Target Benefit Plans, as well as similar legislation being adopted or proposed in other Canadian jurisdictions.

In 2014, OSFI registered the first federal Pooled Registered Pension Plans (PRPPs) for PRPP administrators who had received federal licenses in 2013-2014. The growth of this new type of plan will depend to a large degree on the implementation of provincial legislation that will support the operation of PRPPs across different Canadian jurisdictions. A number of provincial governments are expected to implement PRPP legislation in 2015-2016.

FIGURE 2
Federally Regulated Private Pension Plans by Type (last 4 years)[1]

	2012	2013	2014	2015[2]
Total Plans	**1,354**	**1,234**	**1,234**	**1,226**
Defined Benefit	358	347	335	323
Combination	94	100	111	112
Defined Contribution	902	787	788	791
Total Active Membership	**646,000**	**639,000**	**639,000**	**631,000**
Defined Benefit	378,000	358,000	353,000	342,000
Combination	144,000	154,000	162,000	161,000
Defined Contribution	124,000	127,000	124,000	128,000
Total Other Beneficiaries[3]	**-**	**420,000**	**430,000**	**445,000**
Defined Benefit	-	265,000	268,000	272,000
Combination	-	142,000	147,000	156,000
Defined Contribution	-	13,000	15,000	17,000
Total Assets	**$142 billion**	**$155 billion**	**$171 billion**	**$189 billion**
Defined Benefit	$102 billion	$104 billion	$112 billion	$123 billion
Combination	$35 billion	$46 billion	$54 billion	$60 billion
Defined Contribution	$5 billion	$5 billion	$5 billion	$6 billion

[1]As at March 31st
[2]Does not include the five PRPPs registered in 2014
[3]Data is available only as of 2013

As at March 31, 2015, there were 1,226 private pension plans registered under the *Pension Benefits Standards Act, 1985*, covering over 1,076,000 active members and other beneficiaries. (The drop from 1,354 plans in 2012 to 1,234 plans in 2013 was largely due to a Supreme Court of Canada decision that affected the jurisdiction of 110 First Nations pension plans.

Risk Assessment, Supervision and Intervention

In 2014-2015, OSFI encouraged plan administrators to consider reviewing their strategies to manage risks in their pension plans, particularly given the improved financial position at the end of 2013. OSFI also continued to emphasize the importance of stress testing to administrators of federally regulated private pension plans. In general, OSFI has observed that plan administrators and employers are paying closer attention to their pension plans' underlying risks, and to how these risks can be managed.

In October 2014, OSFI posted updated versions of the Risk Assessment Framework for Federally Regulated Private Pension Plans and the accompanying Guidance Notes. These documents, which support OSFI's supervisory methodology for pension plans, were developed as a resource tool to assist in making consistent risk assessments.

OSFI's Risk Assessment System for Pensions (RASP) analyses information from pension plan filings and other sources and generates key risk indicators for each federally regulated private pension plan registered with OSFI, thereby enabling early identification of issues. In 2014-2015, OSFI finalized an in-depth review of the key risk indicators it built into RASP in 2012 and has since identified a number of changes that will be implemented during 2015-2016. OSFI also re-evaluated its process to support the assessments of a pension plan's overall risk profile and will be implementing changes in 2015-2016.

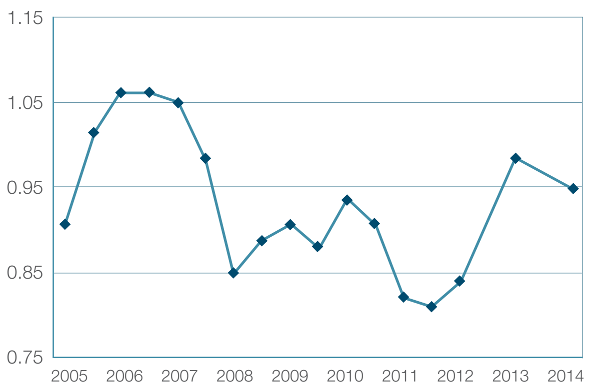
During 2014-2015, OSFI reviewed its supervisory processes with respect to plans with defined contribution provisions and concluded that more comprehensive information is needed to identify any gaps. A detailed study is planned for 2015-2016.

Solvency Testing

OSFI estimates solvency ratios (ratio of assets over liabilities on a plan termination basis) on an annual basis for the defined benefit pension plans it regulates. This test provides OSFI with important information that enables earlier intervention in higher-risk pension plans. At December 31, 2014, the estimated solvency ratio (ESR) for all plans was 0.94, down from 0.98 at year-end 2013 *(see figure 3)*. ESRs calculated by OSFI at year-end 2014 showed that approximately 79% of all defined benefit pension plans supervised by OSFI were underfunded (up from 61% in 2013), meaning their estimated liabilities exceeded assets, on a plan termination basis.

FIGURE 3

Defined Benefit Plans' Estimated Solvency Ratio (ESR) Distribution (past 9 years)



The ESR decreased from 0.98 to 0.94 since year-end 2013.

Examinations

As part of its risk-based supervisory approach, OSFI conducts examinations of selected federally regulated private pension plans. The examinations may be limited to a desk review of additional information that would not be part of the normal regulatory filings. Examinations may also be conducted on the plan administrator's premises (on-site examinations) during which, in addition to the more thorough review of the plan administrator's processes, OSFI interviews those involved in the administration of the pension plan. The objective of an examination is to gather additional information and better assess the plan's quality of risk management. During 2014-2015, OSFI performed 11 examinations and findings continued to focus on governance, asset management and communication to members.

Watch List

Pension plans facing higher risk – due to their financial condition, plan management or other reasons – are placed on a watch list and actively monitored. The number of watch list plans at March 31, 2015 decreased to 60 from 92 at March 31, 2014. Of the 60 plans, 42 were defined benefit plans and 18 were defined contribution plans. During 2014-2015, 48 plans were removed from the watch list while 16 new plans were added.

Intervention

OSFI strives to protect members' benefits through cooperation with plan administrators and employers before exercising its powers to enforce legislative requirements. In 2014-2015, OSFI interventions with respect to high-risk pension plans included issuing two directions of compliance requiring the employers to remit outstanding contributions.

Rules and Guidance

Pension Benefits Standards Regulations, 1985

Amendments to the *Pension Benefits Standards Regulations, 1985* (the Regulations) were published by the federal government for comment in September 2014, and finalized in March 2015. A number of amendments, such as those requiring that additional information be provided to plan members in annual statements, will come into effect at a later date to allow plan administrators time to make the necessary changes. Through its website and regular *InfoPensions* newsletter, OSFI provided up-to-date guidance on the status of changes to federal pension legislation and will issue revised guidance in 2015-2016.

Pension Industry Outreach

In April 2014, OSFI hosted a web conference or "webinar" that included topics on supervisory findings and expectations, actuarial concerns, and expectations with respect to regulatory approvals. The webinar format enables OSFI to reach a greater number of stakeholders across the country in a manner that is cost effective both for OSFI and those attending.

In November 2014, OSFI conducted a survey of plan administrators and professional advisors of federally regulated private pension plans, through an independent research firm, to obtain their assessment of OSFI's effectiveness as a supervisor and regulator of private pension plans. These consultations are a part of our ongoing commitment to be responsive to stakeholder input and to seek suggestions for improvement. All survey results are published on OSFI's website.

Guidance

In keeping with the objectives of promoting prudent practices and a transparent regulatory framework, OSFI regularly provides guidance to plan administrators on legislative requirements and OSFI's expectations.

Reflecting the growing interest in strategies to manage the risks facing defined benefit pension plans, OSFI issued a policy advisory titled Longevity Insurance and Longevity Swaps in June 2014, following consultation with pension stakeholders in 2013. The advisory provides guidance to administrators of federally regulated defined benefit pension plans who are considering this type of contract as a means of hedging longevity risk.

In 2014, OSFI issued revised instructions on how to complete *Form 1 – Attestation Regarding Withdrawal Based on Financial Hardship* for applicants who wish to unlock funds held in a federally regulated locked-in

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FIGURE 4

Asset Breakdown* of Pension Plans Regulated by OSFI

($ millions)	2013		2014	
Cash	**$1,266**	**0.7%**	**$986**	**0.5%**
Debt Securities				
Short Term Notes, Other Term Deposits	5,676	3.3%	4,619	2.4%
Government Bonds	36,681	21.4%	47,548	25.2%
Corporate Bonds	12,606	7.4%	13,714	7.3%
Mutual Funds - Bonds, Cash Equivalent & Mortgage	11,883	6.9%	15,046	7.9%
Mortgage Loans	780	0.5%	864	0.5%
General Fund of an Insurer	195	0.1%	194	0.1%
Total Debt Securities	**67,821**	**39.6%**	**81,985**	**43.4%**
Equity				
Shares in Investment, Real Estate or Resource Corporation	4,275	2.5%	4,163	2.2%
Common and Preferred Shares	52,710	30.8%	54,174	28.7%
Stock Mutual Funds	19,825	11.5%	20,469	10.8%
Real Estate Mutual Funds	1,504	0.9%	1,958	1.1%
Real Estate	2,922	1.7%	2,697	1.4%
Total Equity	**81,236**	**47.4%**	**83,461**	**44.2%**
Diversified and Other Investments				
Balanced Mutual Funds	5,938	3.5%	5,152	2.7%
Segregated Funds	2,825	1.7%	3,311	1.8%
Hedge Funds	4,879	2.9%	5,986	3.2%
Private Equity	1,272	0.7%	1,887	1.0%
Infrastructure	2,059	1.2%	2,552	1.3%
Miscellaneous Investments	6,528	3.8%	9,287	4.9%
Total Diversified and Other Investments	**23,501**	**13.8%**	**28,175**	**14.9%**
Other Accounts Receivables (net of liabilities)	**(2,575)**	**-1.5%**	**(5,682)**	**-3.0%**
TOTAL NET ASSETS	**171,249**	**100.00%**	**188,925**	**100.0%**

* Represents asset distribution as reported in the financial statements of pension plans during respective years.

Approximately 44% of federally regulated private pension plan assets are invested in equities, 43% in debt instruments and 13% in other assets. Equities produced strong returns in 2014, compensating for the negative results on debt instruments. Investment returns for federally regulated private pension plans were 13% in 2014 compared to 12% in 2013.

savings plan due to financial hardship. The instructions were revised in response to questions received on the previous version.

In February 2015, OSFI conducted a targeted, online consultation with a small number of pension industry professionals who regularly request interpretations relating to the Regulations. The overall results of the consultation were positive and have helped OSFI to identify areas for improvement, including formalizing service delivery standards for responding to enquiries.

InfoPensions

OSFI published its bi-annual newsletter *InfoPensions* in May and November 2014. The newsletter includes announcements and reminders on issues relevant to administrators of federally regulated private pension plans, pension advisors, and other stakeholders. It also includes descriptions of how OSFI applies selected provisions of the pension legislation and OSFI guidance. OSFI regularly consults with its stakeholders to ensure that we are communicating effectively and continues to look for ways to ensure that *InfoPensions* is highly readable, accessible and relevant.

Approvals

Federally regulated private pension plans are required to seek approval from the Superintendent for several types of transactions, including plan registrations and terminations, asset transfers between registered defined benefit pension plans, refunds of surplus, and reductions of accrued benefits. During 2014-2015, the number of pension transactions submitted to the Superintendent for approval returned to historical norms, following a year when requests for approval were unusually high. OSFI processed 63 applications for approval and received 56 new requests in 2014-2015, compared to 104 processed applications and 89 new requests in 2013-2014. Thirty new plans were registered by OSFI in 2014-2015 (14 defined benefit plans and 16 defined contribution plans), while 18 plan termination reports were approved (7 defined benefit plans and 11 defined contribution plans).

In addition to the approvals noted above, OSFI is responsible for licensing administrators and registering plans under the *Pooled Registered Pension Plans Act*. In 2014-2015, OSFI registered five PRPPs, one for each federal PRPP administrator licensed by OSFI in 2013-2014. No new PRPP administrators were licensed by OSFI in 2014-2015.

Office of the Chief Actuary

Jean-Claude Ménard
Chief Actuary

The Office of the Chief Actuary (OCA) contributes to a financially sound and sustainable Canadian public retirement income system through the provision of expert actuarial valuation and advice to the Government of Canada and to provincial governments that are Canada Pension Plan (CPP) stakeholders.

The OCA provides statutory actuarial valuation and advisory services for the CPP, Old Age Security program, the Canada Student Loans Program, Employment Insurance program, and pension and benefits plans covering the federal Public Service, the Canadian Forces, the Royal Canadian Mounted Police (RCMP), federally appointed judges, and Members of Parliament.

The OCA was established within OSFI as an independent unit. The Chief Actuary reports to the Superintendent; however, the accountability framework of the OCA makes it clear that the Chief Actuary is solely responsible for content and actuarial opinions in reports prepared by the OCA.

Tabling of the 12th Actuarial Report on the Old Age Security Program

The OCA is required by law to produce an actuarial report on the Old Age Security (OAS) program every three years or whenever an amendment is made that affects the cost of benefits. The triennial 12th Actuarial Report on the OAS Program as at 31 December 2012 was tabled on August 20, 2014. This actuarial report provides information on future expenditures until 2060. The report facilitates a better understanding of the status of the OAS program and the factors that influence its costs, thereby contributing to an informed public discussion of issues related to it.

The OAS program, financed through Government of Canada general tax revenues, is one of the cornerstones of Canada's retirement income system. Benefits include the basic OAS pension, the Guaranteed Income Supplement (GIS) and the Allowance. The basic pension is a monthly benefit available to most Canadians who meet age and residence requirements. The age of eligibility for OAS benefits is currently 65 but is scheduled to increase gradually to 67 by January 2029. The GIS and the Allowance are monthly benefits paid to residents of Canada who receive a basic, full or partial OAS pension and have little or no other income.

In 2014, about 5.5 million Canadians received OAS benefits, with a total value of approximately $44 billion or 2.2% of Canada's Gross Domestic Product (GDP). The report's key findings show that, over the long term, the ratio of total OAS expenditures to GDP is projected to reach a high of 2.8% by 2033 and then decrease slowly to a level of 2.4% by 2050.

External Peer Review of the 26th CPP Actuarial Report

The OCA is continually working to strengthen its technical expertise, as well as internal and external communications. External peer reviews of CPP actuarial reports and their ensuing recommendations have helped the OCA achieve these objectives and ensure that the OCA continues to provide a valuable service with tangible benefits to Canadians.

The OCA released, in May 2014, the findings of an external peer panel commissioned to review the 26th Actuarial Report on the Canada Pension Plan. Key findings were reported in the 2013-2014 OSFI Annual Report and the complete review is available in the Office of the Chief Actuary section of the OSFI website.

The peer review resulted in eight recommendations dealing with various aspects of the report including data, methodology, communication of results, and other actuarial issues. The OCA has either taken or plans to take action on these recommendations. In particular, the OCA will continue to broaden its sources of information before setting assumptions. The work performed by the Chief Actuary as Chairman of the International Social Security Association (ISSA) Commission on Statistical, Actuarial and Financial Studies, as well as the OCA inter-disciplinary seminar planned for September 2015, are aimed at gathering opinions from national and international experts. The OCA will also continue to obtain expert advice from various fields such as demographics, economics, statistics and investments.

To further increase the transparency and independence of the peer review process, an external party was responsible for the oversight of the review. The United Kingdom's Government Actuary's Department (GAD) selected the peer review panel members and released an opinion in May 2014 on the work performed by the external panel. The GAD opinion noted that the work carried out for the review and the review report adequately addresses the issues set out in the terms of reference and that the three reviewers were able to reach agreement on all of the opinions and recommendations set out in the review report. (The GAD opinion is also available on the OSFI website.)

Public Sector Insurance and Pension Plans

In 2014-2015, the OCA completed four actuarial reports with respect to public sector insurance and pension plans, which were submitted to the President of the Treasury Board for tabling before Parliament. The Actuarial Report on the Pension Plan for the Members of Parliament as at March 31, 2013 and the Actuarial Report on the Regular Force Death Benefit Account as at March 31, 2013 were tabled on October 31, 2014, and the Actuarial Reports on the Pension Plans for the Canadian Forces – Regular Force and Reserve Force as at March 31, 2013 were both tabled on November 21, 2014. These reports provide actuarial information to decision makers, Parliamentarians and the public, thereby increasing transparency and confidence in Canada's retirement income system.

Actuarial Report on the Employment Insurance Premium Rate

In 2014-2015, the OCA presented to the Canada Employment Insurance Commission the 2015 Actuarial Report on the Employment Insurance Premium Rate that was tabled before Parliament on September 24, 2014. This report provides the forecast break-even premium rate for the upcoming year and a detailed analysis in support of this forecast.

Special Events, Presentations and Special Studies

Increasing longevity affects the sustainability of pension plans. The impact of this trend, coupled with high uncertainty with respect to the evolution of future mortality rates, makes the development of appropriate mortality assumptions of paramount importance. As stated by Chief Actuary Jean-Claude Ménard during his appearance at the House of Commons Standing Committee on Public Accounts in May 2014, the expected future mortality improvements are embedded in actuarial valuations of the pension plans prepared by the OCA. If the future improvements in mortality were not taken into account, the total actuarial liability of the three largest public sector pension plans (public service, Canadian Forces and RCMP) as at 31 March 2013 would be reduced by $7.7 billion or 3.4%.

In 2014-2015, the OCA published two mortality studies that address mortality assumptions. Actuarial study No. 12 *Mortality Projections for Social Security Programs in Canada* explored trends in Canadian population mortality and discussed mortality assumptions developed for the latest CPP and OAS Actuarial Reports. The findings of this study were presented to various national and international audiences, including by Chief Actuary Jean-Claude Ménard at the Society of Actuaries' Annual Meeting. Actuarial study No. 14 *Pension Plan for the Public Service of Canada Mortality Study* was produced in response to the development by the Canadian Institute of Actuaries of mortality tables based on the experience of Canadian pensioners. The OCA study found that life expectancies of federal public servants are similar to those of members of private sector pension plans.

For a complete list of studies, meetings, presentations and speeches, see the Office of the Chief Actuary section of OSFI's website.

Corporate Services

Communicating Effectively

During 2014-2015, OSFI communicated its plans and activities to a wide range of stakeholders via its website and other means. As in previous years, OSFI received many requests to address external conferences and events. The Superintendent and senior OSFI officials delivered presentations across Canada and internationally. The Superintendent appeared before the Senate Standing Committee on Banking, Trade and Commerce, and the Chief Actuary appeared before the House of Commons Standing Committee on Public Accounts.

Coinciding with Jeremy Rudin's first public address as Superintendent, in September 2014, OSFI began using Twitter to broadcast content to a larger audience. OSFI tweets from two accounts: @OSFICanada (English) and @BSIFCanada (French).

OSFI's external newsletter, *The Pillar*, was published four times in 2014-2015. It updates stakeholders on the latest guidelines, notices, public statements, and other pertinent information.

Throughout 2014-2015, OSFI communicated with interested Canadians, including members of the general public, industry, regulators, legislators and the news media, as follows:

- Served 1,744,643 visitors to OSFI's website
- Responded to 9,861 public enquiries, 185 enquiries from Members of Parliament and 175 enquiries from representatives of the news media
- Delivered over 63 presentations to industry and regulatory forums, including 12 key speeches that were posted to OSFI's website
- Processed 43 access to information requests and 24 consultations within permitted statutory timelines, as per the *Access to Information Act*.

Renewing Technology and Systems

2014-15 marked the successful completion of a five-year Information Technology Renewal program. By the end of the fiscal year, the last three projects concluded as planned and the new systems are providing OSFI with updated business data management capability. OSFI now uses the federal government's shared SAP platform for its financial and contracting processes; a modern HR Management System enables self-serve transactions; and a Correspondence and Enquiry Management system manages inquiries received from Parliament, federally regulated financial institutions, pension plan members, media and the general public. System upgrades delivered over the preceding four years include: on-line filing for regulatory data; business intelligence analytics tools; a new website; a risk assessment system for the Pension Plans Division; and modernized networking and technology tools.

The overall result is significantly fewer applications and rationalized data, and a strong emerging focus on enterprise information management across the Office.

Managing Human Resources

To achieve its strategic outcomes, OSFI's priority is to have a high-performing and effective workforce.

In 2014-2015, ongoing risks posed by the current environment, both at the level of the economy and within the financial sector, as well as internal factors, continued to have an impact on how we do our work. To mitigate these risks, a number of priorities were identified through the Human Resources (HR) planning process and the following actions were taken to address gaps:

- Supported the reorganization of the Supervision Sector, which led to the creation of new sectors for Deposit-taking Institutions, Insurance Institutions and the Supervision Support Group, with staffing expected to be completed early in 2015-2016

- Provided support and oversight to contain costs and growth in the organization, and helped managers identify and reallocate resources to address organizational priorities

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Human Resources Advisor
Human Resources and Administration
Corporate Services Sector

Chris Cooper
Administrative Officer
Administration
Corporate Services Sector

- Continued to update HR policies and guidelines to provide appropriate guidance to managers and employees and to support their consistent application across the organization
- Focused on employee engagement by ensuring that managers worked with employees to implement action plans to address issues raised in the bi-annual employee survey done in 2013-2014
- Provided learning and development opportunities for staff across the organization based on individual learning plans in support of business plans
- Continued to support managers in handling complex performance, disability and sick leave cases on a timely basis

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Financial Review and Highlights

OSFI recovers its costs from several revenue sources. OSFI is funded mainly through asset-based, premium-based or membership-based assessments on the financial institutions and private pension plans that it regulates and supervises, and a user-pay program for legislative approvals and other selected services.

The amount charged to individual institutions for OSFI's main activities of risk assessment and intervention (supervision), approvals and precedents, and regulation and guidance is determined in several ways, according to formulas set out in regulations. In general, the system is designed to allocate costs based on the approximate amount of time spent supervising and regulating each industry. Costs are then assessed to individual institutions within an industry based on the applicable formula, with a minimum assessment for smaller institutions.

Staged institutions are assessed a surcharge on their base assessment, approximating the extra supervision resources required. As a result, well-managed, lower-risk institutions bear a smaller share of OSFI's costs.

OSFI also receives revenues for cost-recovered services. These include revenues from provinces for which OSFI provides supervision of their institutions on contract, federal Crown corporations such as the Canada Mortgage and Housing Corporation (CMHC) which OSFI supervises under the *National Housing Act*, and revenues from other federal organizations to which OSFI provides administrative services.

OSFI collects Administrative Monetary Penalties from financial institutions when they contravene a provision of a financial institutions Act and are charged in accordance with the *Administrative Monetary Penalties (OSFI) Regulations*. These penalties are collected and remitted to the Consolidated Revenue Fund. By regulation, OSFI cannot use these funds to reduce the amount that it assesses the industry in respect of its operating costs.

The Office of the Chief Actuary (OCA) is funded by fees charged for actuarial valuation and advisory services relating to the Canada Pension Plan, the Old Age Security program, the Canada Student Loans Program and various public sector pension and insurance plans, and by a parliamentary appropriation.

Overall, OSFI fully recovered all its costs for the fiscal year 2014-2015.

OSFI's total costs were $144.9 million, a $2.9 million, or 2.1%, increase from the previous year. Human resources costs, OSFI's largest expense, rose by $0.3 million, or 0.3%. The increase in basic salaries was offset by less usage of contracted personnel services combined with a decrease in the prescribed employee benefit plan contribution rate. Information management/technology costs increased by $2.0 million, or 14.1%, largely driven by amortization expense related to new system implementations during the year and in the latter half of the preceding one. Facilities costs increased by $1.1M, or 11.6%, as a result of additional leased space to accommodate the growth in staff complement of recent years. All other costs decreased by $0.5M as a result of efforts to contain discretionary spending.

OSFI's average number of full-time equivalent employees in 2014-2015 was 687, a 3.2% increase from the previous year as a result of the full year impact of employees added during 2013-2014. In the year under review, OSFI set a limit on head count and ended the year with an actual head count of 704, a 1.0% increase from its head count of 697 as at March 31, 2014.

Federally Regulated Financial Institutions

Revenues

Total revenues from federally regulated financial institutions were $130.8 million, an increase of $3.8 million, or 3.0%, from the previous year. Base assessments on financial institutions, which are recorded at an amount necessary to balance revenue and expenses after all other sources of revenue are taken into account, increased by $3.3 million, or 2.8%, from the previous year.

Revenues from cost recovered services increased by $0.4 million, or 8.4%, from the previous year as a result of services provided to two additional federal Crown corporations.

Costs

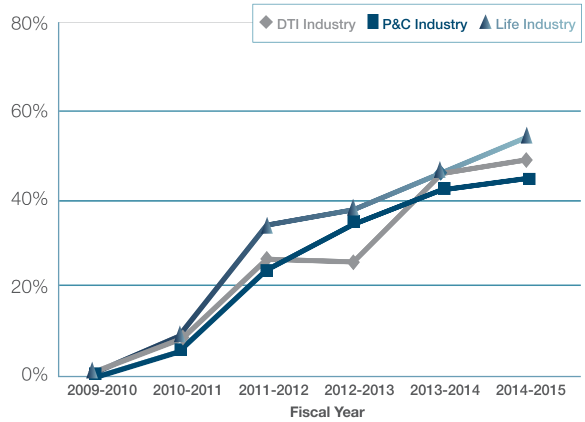
Total costs were $130.8 million, an increase of $3.8 million, or 3.0%, from the previous year. The increase is primarily due to two factors: facilities costs increased by $1.1M and information management/technology costs increased of $2.1 million, for the reasons mentioned above.

Base Assessments by Industry

Base assessments are differentiated to reflect the share of OSFI's costs allocated to each industry group (base assessments are the costs allocated to an industry, less user fees and charges and cost-recovered services revenues). The chart below compares the cumulative growth of base assessments by industry group over the past five years, using 2009-2010 as the base year.

The increase in base assessments on the deposit-taking institutions (DTI) industry during 2010-2011 and 2011-2012 was driven by growth in our complement of

Base Assessments by Industry
Cumulative Growth Rates from Fiscal Year 2010



specialized skills in research, credit risk and capital to enhance OSFI's ability to guide and supervise federally regulated financial institutions in managing risks. While base assessments stabilized in 2012-2013, they increased in 2013-2014 as a result of work related to domestic systemically important banks (D-SIBs). The rate of growth in base assessments eased in 2014-2015, in line with that of OSFI's total expenses.

The increase in assessments on the property and casualty (P&C) insurance industry in 2010-2011 through 2013-2014 reflects OSFI's continued efforts to enhance its specialization in the P&C industry, support more sophisticated risk-sensitive capital rules and fulfill international commitments. During 2014-2015, OSFI finalized and issued its revised Minimum Capital Test (MCT) and continued development work on a framework for the use of company-specific models to determine capital requirements for P&C insurance companies and new capital rules for mortgage insurers.

The increase in assessments on the life insurance industry in 2010-2011 through 2013-2014 reflects the addition of staff with specific expertise in life insurance, OSFI's efforts in developing a new framework for the standardized Minimum Continuing Capital and Surplus Requirements (MCCSR) approach, and its continuing focus on reviewing and revising the framework used to determine the capital requirements for segregated fund guarantee products. In 2014-2015, OSFI continued its efforts on the MCCSR guideline and continued to work on the development of a new Life Insurance Solvency Framework Standard Approach that is scheduled for implementation in 2018.

In addition to these industry-specific cost drivers, other generic factors caused increases in base assessments on all industries: OSFI's development and implementation of an Information Management/ Information Technology (IM/IT) strategy and renewal program from 2010-2011 to 2014-2015 contributed to overall growth in expenditures and assessments; and, slight decreases during 2010-2011 and 2011-2012 in the number of staged institutions across all industries, and hence in surcharge assessments. This in turn had the effect of increasing base assessments. In 2012-2013, there was a further decrease in the number of staged institutions; however, surcharge assessments increased slightly as a result of changes to the mix of staged institutions. In both 2013-2014 and 2014-2015, surcharge assessments decreased slightly which, in turn, slightly increased base assessments.

Federally Regulated Private Pension Plans

Assessments

OSFI's costs for regulating and supervising private pension plans are recovered from an annual assessment charged to plans, based on the number of plan beneficiaries. Plans are assessed a fee upon applying for registration under the *Pension Benefits Standards Act, 1985* (PBSA) and annually on the due date of their annual information return.

The assessment rate is established based on OSFI's estimate of current year costs to supervise these plans, adjusted for any excess or shortfall of assessments in the preceding years. The estimate is then divided by the anticipated assessable membership to arrive at a base fee rate. The rate established for 2014-2015 was $10.00 per assessable beneficiary, unchanged from the previous year. Total fees assessed during the fiscal year were $6.7 million, down from $6.8 million in 2013-2014.

The excess or shortfall of assessments in any particular year is amortized over five years in accordance with the assessment formula set out in regulations. Prior to 2009-2010, rates had been set to recover an accumulated shortfall and the annual costs of administering the PBSA. A small surplus position was re-established in 2008-2009 and was buoyed by lower than planned expenses in each of the two subsequent years. Since 2012-2013, rates have been set to draw the surplus down. The rate established and published in the Canada Gazette for 2015-2016 is set at $10.00 per assessable beneficiary, unchanged from 2014-2015.

Costs

The cost of administering the PBSA for 2014-2015 was $6.7 million, a decrease of $0.4 million, or 6.2%, from the previous year due to lower human resources costs as a result of vacancies within the division.

Actuarial Valuation and Advisory Services

The OCA is funded by fees charged for actuarial valuation and advisory services and by an annual parliamentary appropriation. Total costs were $7.3 million, a decrease of $0.3 million or 4.2% from the previous year due to some vacancy savings and the completion of a triennial review of the Canada Pension Plan in 2013-2014.

Fees Assessed and Costs for Fiscal Years 2009-2010 to 2014-2015

($000, except Basic Fee Rate)

FY	2009-2010	2010-2011	2011-2012	2012-2013	2013-2014	2014-2015
Fees Assessed	8,578	7,866	7,949	6,477	6,842	6,725
Costs	6,529	6,555	6,701	6,905	7,196	6,666
Basic Fee Rate* per assessable member	24.00	22.00	22.00	10.00	10.00	10.00

* The minimum and maximum annual assessment per plan is derived by multiplying the annual assessment by 50 and 20,000 respectively. With an annual assessment of $10.00 per member, the minimum annual assessment is $500 and the maximum is $200,000.

Changes in Accounting Standards

Transition to Public Sector Accounting Standards (PSAS)

In December 2014, the Public Sector Accounting Board (PSAB) issued amendments to Public Sector Accounting Standards (PSAS). These amendments introduced the concept of a new public sector entity – referred to as a government component – and provided guidance on the basis of accounting to be used by such entities. OSFI is considered a government component and is required to adopt PSAS effective the 2017-2018 fiscal year.

OSFI has chosen to approach the conversion in five phases: (1) Diagnostic Assessment; (2) Design and Planning; (3) Assessment, Design and Development; (4) Implementation; and, (5) Post Implementation Review. OSFI began the diagnostic assessment phase during 2014-2015.

The design and planning phase will begin in summer 2015. This will include a transition plan and a timetable for assessing the impact of the change in accounting standards on systems, internal controls over financial reporting and business activities.

OSFI continues to monitor standards development as issued by PSAB. Such developments could affect the timing, nature or disclosure of the adoption of PSAS.

The transition to PSAS is a significant undertaking. As the design and planning phase has not yet begun, OSFI is unable to quantify the impact of PSAS on its financial statements. The following table outlines the elements of OSFI's conversion to PSAS and presents an assessment of progress towards achieving these objectives. As the project progresses or further changes in regulation conditions occur, changes to the transition plan may be required.

OSFI PSAS Conversion Approach: Assessment as at March 31, 2015

Project Phase	Milestone	Status
Diagnostic Assessment		
• Identify differences in IFRS/PSAS accounting policies	External advisor's report presented to OSFI's Executive and and Audit Committees	To be completed in June 2015
Design and Planning		
• Launch project, establish project governance • Develop training and communications plan	Project governance and policy choices are in place	To be completed in 2015-2016
Assessment, Design and Development		
• Identify solutions to PSAS and evaluate • Develop final solutions to PSAS	Solutions approved by OSFI's Executive and Audit Committees	To be completed in 2015-2016
Implementation		
• Rollout PSAS solutions • Test and remediate	Financial systems and processes are able to capture and report PSAS information	To be completed in 2016-2017
Post Implementation Review		
• Debrief management and assess implementation • Ongoing PSAS update and related changes management	Ongoing process post implementation	To be started in 2017-2018

Appendix

Disclosure of Information

Under the OSFI Act, the Superintendent is required to report to Parliament each year on the disclosure of information by financial institutions and the progress made in enhancing the disclosure of information in the financial services industry.

OSFI promotes effective disclosure by: publishing selected financial information on OSFI's external website (and through Beyond 20/20 Inc. for federally regulated insurance companies only – see OSFI's website under Financial Institutions/Financial Data); providing guidance to federally regulated financial institutions (FRFIs) on their disclosures; and, participating in international supervisory groups with similar objectives.

Public Disclosures Associated with Building a More Stable Future

Public disclosures of risk management practices and risk exposures made by FRFIs have become a significant focus to achieving transparency, financial stability and restoring market confidence since the global financial crisis. Over the past few years, publications released by international organizations, such as the Financial Stability Board (FSB), the European Banking Authority, and the Basel Committee on Banking Supervision (BCBS) have stressed the need for enhanced risk disclosures. OSFI believes that strong disclosures and market discipline are key elements for effective corporate governance and sound risk management practices within an institution.

During 2014-2015, OSFI focused on issuing guidance for several disclosure projects which included:

- April 2014 – revisions to Public Disclosure Requirements related to Basel III Pillar 3 composition of capital, to accommodate Credit Valuation Adjustment (CVA) phase-in
- July 2014 – issuance of the final Guideline D-11: Public Disclosure Requirements for Domestic Systemically Important Banks on Liquidity Coverage Ratio
- September 2014 – issuance of the final Guideline D-12: Public Disclosure Requirements related to Basel III Leverage Ratio

OSFI has also participated as a member of the Working Group on Disclosures subgroup of the BCBS on recent Pillar 3 disclosures initiatives and will be working on the domestic implementation of the BCBS Revised Pillar 3 Disclosure Requirements standard issued in January 2015.

Financial Stability Board Guidance

In October 2012, the Enhanced Disclosure Task Force (EDTF), established by the FSB, issued 32 recommendations to improve risk disclosures. Since then, OSFI has worked closely with Canada's six major banks (designated as domestic systemically important banks) to implement the 32 EDTF recommendations and performed quarterly reviews of the six major banks' public disclosures to monitor the progress of implementation. The six major banks, as highlighted by the EDTF in its 2014 progress report, made substantial improvements to risk disclosures and achieved virtually full compliance with the 32 EDTF recommendations by 2014.

OSFI expects the six major banks to adopt future disclosure recommendations in the banking arena that are endorsed by international standard setters and the FSB, as well as evolving domestic and international bank risk disclosure best practices.

OSFI is committed to continuing to improve public disclosures in order to promote safety and soundness in the way institutions conduct business, and contribute to public confidence in the Canadian financial system. OSFI will continue to support disclosure initiatives through its membership in international associations and through reviewing our domestic disclosure requirements and practices.