



Office of the Superintendent of
Financial Institutions Canada

Bureau du surintendant des
institutions financières Canada

Office of the Superintendent of Financial Institutions

Internal Audit Report on Supervision Sector – Life Insurance Group - Conglomerates

November 2013



OSFI
BSIF

Canada

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1. Background

Introduction

Internal Audit (*IA*) conducts assurance work to determine whether the Office of the Superintendent of Financial Institutions Canada's (*OSFI's*) risk management, control, and governance processes, as designed and represented by management, are adequate and functioning in a manner to ensure risks are appropriately identified and managed, and to ensure compliance with such requirements as policies, plans, procedures and applicable laws and regulations.

The audit of Life Insurance Group – Conglomerates was approved by the OSFI Audit Committee and the Superintendent for inclusion in the OSFI's 2013 to 2014 Internal Audit Plan.

This report presents the results of that review based on audit work completed at the end of September 2013.

This report was presented to the OSFI Audit Committee on November 21, 2013 and approved by the Superintendent on November 29, 2013. The Deputy Superintendent, Supervision Sector, and Life Insurance Group – Conglomerates Senior Management, who have provided their management comments within this report, have also reviewed it.

Context

Life Insurance Group – Conglomerates (*LIG-C*) is the division within OSFI's Supervision Sector responsible for the supervision of the large and complex conglomerate federally regulated life insurance institutions.

LIG-C supervises and monitors the safety and soundness of the life insurers by focusing on elements such as governance, risk management practices and controls, capital adequacy, proper accounting of assets and liabilities, and liquidity. The division's supervisory activities also include verifying and enforcing insurers' compliance with the rules established by legislation and OSFI's regulatory framework.

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1. Background, Continued

Context
(continued)

In June 2012, Internal Audit completed an Internal Audit of Life Insurance Group – Conglomerates. In that audit, IA examined whether OSFI's supervisory methodology (Methodology) was appropriately applied in assessing the safety and soundness of the life insurance conglomerate institutions.

That audit noted that LIG-C supervisory teams demonstrated a sound understanding of the business activities of the institutions. While supervisory teams understood the principles of risk-based supervision, the quality control reviews required improvement to ensure OSFI's Methodology was consistently applied and that the logic and flow of the documentation clearly showed how the supervisory teams' conclusions were reached and the ratings assigned. Furthermore, management oversight needed to be strengthened to ensure that the quality control reviews were conducted at each step in the supervisory process and achieved their intended purpose.

LIG-C management agreed and committed to address IA's findings by March 2014. While IA was not scheduled to follow up on these findings until such time, management requested that IA provide an interim assessment of management's progress to date to gain comfort that LIG-C is advancing in the right direction, given the long time horizon to complete its action plans.

2. Audit Objective, Scope and Approach

Audit Objective The objective of this audit report was to provide reasonable assurance that LIG-C's management action plans to audit recommendations from the June 2012 Internal Audit of LIG-C are progressing as planned, and completed actions to date are directionally appropriate to support LIG-C to put in place appropriate processing, reviews, approvals, and monitoring controls to mitigate identified risks. Specifically, IA assessed whether management's actions reported as completed as at June 2013 support the ongoing progression of other planned and in-progress management actions.

Audit Scope IA reviewed key management actions to IA's three recommendations reported as "Completed" to the Audit Committee on June 20, 2013. Specifically, IA conducted limited reviews of recent¹ supervisory documents for evidence that the completed actions are contributing to ongoing betterment of LIG-C's application of the supervisory methodology.

Audit Approach The audit was conducted in accordance with the Institute of Internal Auditors' International Standards for the Professional Practice of Internal Auditing, consistent with the Treasury Board Policy on Internal Audit.

The approach to conducting the audit included:

- Examination of documents, such as training material, supervisory documents, and quality control results, etc. and
 - Discussions with LIG-C personnel and other stakeholders (e.g. Supervisory Practices Division), as needed.
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¹ From June 2012 to June 2013

3. Conclusion

Conclusion Life Insurance Group-Conglomerates' (*LIG-C*) management action plans are progressing as planned and are directionally appropriate to address IA's recommendations from the *June 2012 Internal Audit of Life Insurance Group-Conglomerates*. Its actions reported as completed to the Audit Committee in June 2013 support the ongoing progression of other planned and in-progress management actions.

Key management actions undertaken to date are:

1. Targeted training to the supervisors, which included holding multiple sessions for different areas of the Supervisory Framework, and the use of existing files as training examples to apply the Framework,
2. Quality assurance reviews performed by the Quality Assurance Advisor, Supervisory Practices Division, and
3. Quality control processes performed by LIG-C management, which included management reviews of supervisory work by the LIG Director, Operations, and quality review and sign-off on supervisory documents by the Managing Director, LIG-C and Senior Director, LIG.

The quality assurance reviews and LIG-C management reviews were effective in identifying issues and providing feedback to the supervisors. However, due to the timing of the feedback and the natural life cycle of the supervisory documents, lessons learned will need to be reinforced through the completion of the remaining actions. Our limited review of recent supervisory documents indicates that LIG-C is improving its application of the Supervisory Framework.

In my professional judgment as Chief Audit Executive, sufficient and appropriate audit procedures have been conducted and evidence gathered to support the accuracy of the opinion provided and contained in this report. The opinion is based on a comparison of the conditions, as they existed at the time, against pre-established audit criteria that were agreed on with management. The opinion is applicable only to the entity examined. The audit was conducted in conformance with the internal audit standards of the Government of Canada, as supported by the results of the Quality Assurance and Improvement Program.

We wish to recognize the excellent rapport and exchange of views with all involved in the audit. The depth of the review and focusing on what matters would not have been possible without the support received throughout the audit.

Chief Audit Executive, IA

Date

4. Management Response

Overview This report has been reviewed by the Senior Director, Life Insurance Group and Managing Director, Life Insurance Group-Conglomerates, and the Deputy Superintendent, Supervision Sector, who acknowledge its recommendation that LIG-C continue to complete remaining actions in management's action plans.

Responses / Comments We thank the audit team for providing an interim assessment of the progress to date on the implementation of our action plans to address the findings noted in the *June 2012 Internal Audit of Life Insurance Group – Conglomerates* report.

We are pleased that IA has concluded that our action plans are progressing in a manner directionally appropriate to address their recommendations. We recognize that, although we have made substantial progress in applying the Supervisory Framework, we need to continue to reinforce key messages and see them consistently applied in all supervisory documents. To this end we will continue with our original plan of management review, LIG mini audits and training. However, we will adjust the relative focus to emphasize the mini audits as the preferred means, at this time, to achieve more hands on coaching and feedback to RM team members.

Competing priorities, increased workload and resource issues have impacted the progress on our action plan to date. Although we anticipate we will have substantially completed our action plan by the original completion date of March 2014 we believe it will require additional time to satisfy ourselves that the lessons learned have been sufficiently ingrained and become routinized in the supervisory process within LIG-C. In light of this we are proposing a completion date of September 2014.
