Report on

Office of the Superintendent of Financial Institutions

Supervision Sector
Operational Planning Process Review

April 2010

Canada

OSFI - Supervision Sector: Operational Planning Process

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1. Background

Introduction

The Supervision Sector has reorganized along industry lines, effective October 1, 2009, after the commencement of our review. This change in organization structure did not impact our review as our scope entailed an assessment of the 2009/10 plan year. A&CS does not anticipate that changes arising from the new Supervision Sector structure will fundamentally alter the current design of the Supervision Operational Planning framework and we expect our assessment to remain applicable to the new structure.

For the 2009/10 plan year the Supervision Sector included the Financial Conglomerates Group (FCG), the Life Conglomerates Group (LCG), the Financial Institutions Group (FIG), the Specialist Support Group (SSG), the Supervisory Practices Group and the Supervision Support Office (SSO). Responsibility for the overall coordination of Supervision's operational planning process and monitoring of achievement of planning objectives resides with the Supervision Support Office Group which reports to the Assistant Superintendent, Supervision.

Objectives and Approach to Planning

The purpose of operational planning is to align the Supervision Sector's operational activities with OSFI's legislative mandate and strategic outcomes and plan and budget for effective resource allocation, balancing objectives and priorities with business capacities.

Supervision's annual operational planning process is part of a broader corporate planning process and is guided by the outcomes of OSFI Executive strategic planning discussions and corporate planning timelines. In the Supervision Sector operational planning takes place at several levels:
- Institution –specific level
- Division or Responsibility Centre Level
- Group Level (FIG, FCG, LCG, SSG)
- Sector Level (Supervision).

This necessitates the maintenance of appropriate mechanisms to foster and facilitate communication and coordination among these various levels.

2. Review Objective, Scope and Approach

Providing Assurance to the

In order to manage its work in a complex and rapidly changing environment, OSFI develops and puts in place specialized policies, guidance and processes.

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Superintendent

In general, these are called frameworks. These frameworks provide assurance to the Superintendent that the nature and scope of work required to carry out Supervision activities is well defined and that consistency and quality of the work is maintained.

Such frameworks are essential to the Superintendent and the Audit Committee in being able to fulfill their responsibilities under the Treasury Board Policy for Internal Audit regarding OSFI's governance, risk and control processes. Under the policy, Audit & Consulting Services is to conduct assurance reviews and audits of OSFI's operations reporting on the adequacy of OSFI's frameworks and their application in carrying out OSFI's activities. This Supervision Operational Planning Process Review is such an assurance report.

Review Objective

The objective of this review was to provide an independent assessment and comment on the design of the Supervision Operational Planning framework which includes a review of the:

- **Process framework** – the core operational planning process for the achievement of OSFI's supervisory mandate and strategic objectives. Generally this can be considered a review of policies, procedures and practices.
- **Management Oversight framework** - the oversight activities and controls built around the core process that help ensure the Supervision Operational Planning activity is appropriately conducted and meets its objectives. This would generally entail an assessment of activity objectives, operating environment, risk management, information and communication and monitoring and management reporting.

Review Scope

The review covered the Supervision Operational Planning process for the period 2009/10. It did not include Financial Planning, Strategic Planning or HR Planning.

Operational planning in the Supervision Sector is conducted at various levels and there are some differences at the group and divisional levels in how the resource estimates are developed and incorporated into the sector level planning process. Consequently, the scope for this review was limited to a focus on the sector level operational planning process with a high level analysis of linkages with the group/division level planning process for all groups other than FIG. With respect to FIG this engagement included a more detailed review of the operational planning process within the group including a "walkthrough" of sample institution specific plans to facilitate our understanding of the process within the FIG divisions.

Additionally, this review focused on how the various business tools are used in the supervision operational planning process but did not include an

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assessment of the tools themselves.

Evaluation Approach

The design of the process and management oversight framework was assessed against evaluation criteria described in Appendix A – Supervision Operational Planning Framework Evaluation Criteria. These criteria are based on internationally recognized *Enterprise Risk Management – Integrated Framework* recommended by the *Committee of Sponsoring Organizations of the Treadway Commission (COSO)* as adapted to OSFI environment. In applying these evaluation criteria, A&CS looked for the existence of the criteria element and related components.

We formed our view of the Supervision Operational Planning Framework through review of documentation; a "walkthrough" of institution specific plans for a sample of FIG institutions and interviews with appropriate staff and management as required.

Our overall conclusions and recommendations are included in Section 3 and Section 4 of this report.

Consistent with the Treasury Board Policy on Internal Audit the review was conducted in accordance with the Institute of Internal Auditors' International Standards for the Professional Practice of Internal Auditing.

3. Review Conclusion

Review Conclusion

Our review conclusion based on an assessment of the Supervision Operational Planning framework is that the framework is well developed and generally sound in design in terms of both the Process Framework (core process and associated policies, procedures and practices) and Management Oversight Framework (Objective Setting, Operating Environment, Risk Management, Information and Communication and Monitoring and Reporting). No significant concerns were noted. As outlined in this report, some enhancements are recommended to further formalize and strengthen the current framework.

A&CS would like to thank all participants for their cooperation and contribution to this engagement.

_____   _____
Senior Director, A&CS   Date

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4.   Observations and Recommendations

Overview

Although we do not have any significant concerns with the design of the Supervision Operational Planning framework it is our view that this framework can be further formalized and strengthened in the following areas:

- Planning Process Descriptions
- Operational Planning Tools
    - Supervisory Planning Application (SPA)
    - Resource Allocation Model (RAM)

Each of these is discussed below.

Planning Process Descriptions

The Supervision operational planning activity has evolved considerably over the last few years and continues to evolve in response to the changing business needs of the Supervision Sector. As part of this evolution over the past year there has been a concerted effort made to further formalize the framework through documentation of planning expectations, practices and procedures. At the sector level a process description document *Supervision Business Planning Process Description (July 2009)* has been developed. At the group level process descriptions have been prepared for FCG and FIG but A&CS did not find similar process descriptions for the Specialist Support Group (SSG) or the individual divisions within SSG to document the planning steps and reflect how planning is conducted within each individual division and how it is linked to the sector level planning process.

We also found that the existing process description documents appear to still be "Draft" and although we were advised that they were shared with the Supervision Steering Committee and other Supervision senior management and as such may be seen to represent implicit management approval the documents do not provide evidence of approval.

In our view, an approved process description, appropriate for the business, is an important control mechanism at both the sector and divisional level. It establishes and communicates management expectations regarding the process to be followed for the achievement of the operational planning activity objectives. Maintaining divisional process descriptions in addition to the sector level documentation provides a transparent linkage between the division and sector process to allow for a periodic, independent review at the sector level of whether the planning steps as documented at a divisional level are consistent with sector management expectations in contributing to the overall efficiency and effectiveness of the operational planning activity. The efficiency and effectiveness of the sector level process is dependent on the extent to which the sector level expectations have been cascaded down to and

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incorporated into the divisional planning activity and the maintenance of formal divisional process descriptions will, in our view, facilitate such an assessment.

Recommendation:

- **The *Supervision Business Planning Process Description* should be updated to incorporate changes to the operational planning process resulting from the reorganization of the Supervision Sector. Divisional planning process description documents should be developed as appropriate and existing process descriptions updated to reflect the impact of changes to the sector level process.**
- **All planning process description documents should be approved at the appropriate level; date stamped and disseminated to Supervision staff as appropriate to promote consistency of understanding and application of process.**
- **A formal process should be established for the periodic review, update, approval and communication of all process descriptions.**

Operational Planning Tools

The Supervision operational planning process is supported by a number of tools including the Supervision Planning Application (SPA) and the Resource Allocation Model (RAM) which is housed within SPA. The purpose of SPA is to support OSFI's risk-based planning process and to act as a centralized database for all Supervision planning data. RAM was developed within Supervision to operationalize the OSFI Risk Tolerance Framework so that it could be applied as a guide/benchmark in making consistent risk-based planning/resource decisions in FIG. It is used to plan supervisory work, estimate required resources and foster risk-based dialogue and decision-making among teams and with management.

Both these tools were developed and implemented a few years ago and although they were satisfactory, cost effective alternatives at the time, they are acknowledged by Supervision management to have limitations in their ability to support the current Supervision operational planning process. In our view the Supervision operational planning process has evolved significantly in response to changing business needs resulting from a more volatile economic environment but these tools have not been updated to keep pace with the changing process largely due to resource and cost considerations and competing priorities. It is important that the key tools supporting the Supervision operational planning process continue to remain appropriate and relevant as the process evolves and that there is a formal mechanism in place for the periodic assessment of these tools to ensure their continued relevance.

The limitations in both SPA and RAM are resulting in the use of many "workarounds" and the requirement for implementation of additional controls to manage these workarounds. In our view the efficiency and effectiveness of

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the operational planning process is negatively impacted when additional process steps need to be performed to compensate for the inadequacies of the tool as appears to be happening with the use of RAM and SPA in their current forms.

A&CS recognizes that although Supervision management is well aware of the limitations of SPA and the related process inefficiencies there are cost considerations that need to be factored into any decisions regarding replacement alternatives. In the interim Supervision is managing the shortcomings of the application through workarounds and proposed changes to SPA that are required to fix some of the design issues. It is expected that most of these changes will be available for the 2011/12 plan year but even with these changes, which are not expected to add significant functionality, A&CS is of the view that a longer term solution will need to be pursued if the Supervision operational planning process is to be appropriately supported.

Despite the acknowledged limitations of the RAM it continues to be used as a tool to support the operational planning process as management believes that the real significance of tools like RAM lies in their ability to trigger the right kind of dialogue and thought process and this adds value to the planning decision. A&CS notes that Supervision senior management is well aware that in order for it to be a more meaningful tool the RAM should be updated and in furtherance of this it is likely that RAM will be reassessed in the upcoming year in the context of the Supervision Sector reorganization and lessons learned from the recent global financial crisis. In our view, since RAM is housed within SPA, decisions regarding changes to RAM will of necessity need to be coordinated with the decisions pertaining to SPA.

Recommendation

- **The long term viability of the continued use of SPA as the key planning tool in Supervision should be assessed; alternatives considered and a strategy developed to address the on going operational planning needs of the Supervision Sector.**

- **The cost/benefit of the use of RAM for the development of high level estimates as part of the top down planning process should be assessed and if continued use is warranted the model should be updated to minimize required adjustments so that it appropriately supports the operational planning process.**

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Management Response

Overview   This report has been reviewed by the Supervision Sector, which acknowledges its observations and recommendations. The recommendations will support Supervision with its work to continuously improve the efficiency and effectiveness of its planning processes. We appreciate the effort taken by A&CS to assist us in this regard.

Planning Process & Description

The Supervision Sector Business Planning Process document, which provides a full description of the planning process in Supervision, will be updated to incorporate the recent organizational changes in Supervision.

Planning process description documents that describe the unique aspects of planning have been developed for some of Supervision's divisions. Similar documents will be developed as appropriate for other divisions.

A formal process will be established for the periodic review and updating as appropriate of planning process description documents.

Planning process description documents will be formally approved, date stamped, and communicated to staff using established communication processes.

Operational Planning Tools

Supervision Planning Application(SPA)

Supervision will continue to monitor, evaluate and update our planning tools to ensure that they continue to support an effective planning process. While the Supervision Planning Application (SPA) does not address all of our needs, it is a major improvement over the planning tools that were used in Supervision a few years ago. The upgrades that are scheduled for implementation in June 2010 will ensure the medium term viability of the application as a longer-term solution is considered as part of OSFI's Information Technology Renewal Program.

The assessment and renewal of the planning application will be managed according to OSFI's IM/IT Portfolio Management Framework. Supervision will work with Client Portfolio Management (CPM) to complete an assessment of our operational planning requirements and options to address them. The assessment will need to consider the outcome of the Application Modernization Review, which will include a renewal roadmap for a variety of applications including SPA. This information will than help guide the Business Council when prioritizing and budgeting for these requirements within the context of the Information Technology Renewal Program. We will also continue to work with IM/IT to develop a strategy to identify and implement a planning application platform that meets the various needs of OSFI, taking into consideration the IM/IT Strategic Plan.

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Operational
Planning Tools
continued

Resource Allocation Model (RAM)

The Resource Allocation Model (RAM) used in Supervision provides a useful guide for the resources that should be required to perform particular types of reviews in typical institutions. The RAM factor is then adjusted to take into consideration the many differences that exist among institutions. However, the Resource Allocation Model, has not been reviewed for several years and as such we will undertake a review to ensure that the model continues to support our current supervisory practices and our general views on risk profiles of different types of businesses.

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Appendix A: Supervision Operational Planning Framework Evaluation Criteria

Supervision Operational Planning Framework Evaluation Criteria	
Element	**Components**

1. Process and Control Activities	▪ The planning process is clearly defined with decision and control points in place that are aligned to identified inherent risks, and includes:
	  ▪ Decision-making guidance and policies where necessary;
	  ▪ Appropriate level of analysis, application of judgment and documentation supporting the process;
	  ▪ Clearly defined calendar, deliverables and control points;
	  ▪ Mechanisms for the coordination and management of planning complexity;
	  ▪ Engagement of stakeholders in discussions on risks and input into planning process;
	  ▪ Authorities, escalation and approval/sign–off requirements.
	  ▪ Reporting requirements within and outside of the Supervision Sector.
	
	▪ Quality assurance processes have been built into the planning process framework to facilitate:
	  o Monitoring adherence to the planning process
	  o Dealing on a timely and effective basis with matters of non- compliance
	  o Escalating matters of non-compliance where necessary

2. Operating Environment	▪ Responsibilities, authorities, and the reporting structure are defined. ▪ Staff competencies, including required formal and informal training necessary to maintain knowledge levels, are defined.

3. Objective Setting	▪ Objectives for the business planning activity are
	  - defined,
	  - align with and support OSFI objectives,
	  - include established performance standards and
	  - are understood.
	▪ Risk tolerances have been established through the OSFI ERM process.

4. Risk Management	▪ Potential inherent risks or events that may impact the achievement of objectives have been :
	  ▪ Identified;
	  ▪ Assessed in accordance with OSFI's ERM policy; and
	  ▪ Mitigated where control gaps exist.
	
	▪ Senior management has communicated its views on the risks of the planning process.

5. Information and Communication	▪ Information systems appropriately support the planning process through the provision of timely and accurate information;
	▪ A corporate memory is built and maintained through the capture of information pertaining to planning decisions made;
	▪ The policies, practices and procedures for dealing with the planning process are appropriately communicated.
	▪ Staff and management involved in the planning process understand how their work relates to the work of other stakeholders in the process.
	▪ Open and timely channels of communication exist among staff and managers to:
	  o Ensure appropriate input and consistency of decision making
	  o Foster the development and appropriate application of professional judgment and
	  o Ensure expectations are communicated.

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Supervision Operational Planning Framework Evaluation Criteria	
Element	**Components**

6. Monitoring and Management Reporting	▪ Ongoing quality assurance activities exist to monitor and report on:
	  o Adherence to the planning practices, processes and performance standards;
	  o Planning activities to ensure adequacy of resources to support the business planning activity;
	  o Areas for process improvement; and
	  o Overall effectiveness in achieving planning process objectives.
	
	▪ Appropriate management reporting tools and practices are in place to monitor progress against the plan, identify risks to the plan and allow timely adjustments to be made. This includes reporting at the sector and OSFI level.