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

Key Principles for the Future Direction of Canadian Regulatory Capital Framework

IAIS – ASSAL Training Seminar

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OSFI BSIF

Canada

New Canadian Capital Framework

- **Target Date 2014**
- **Internal Models**
- **Canadian Version of Solvency II**
- **We Believe that Principles are Universal**
- **Include Lessons Learned from the Financial Crisis**

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Encourage Good Risk Management

- **Reward companies that manage risks properly**
- **Models should be used internally to manage risks**
- **Cherry picking not allowed**

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Encourage Capital Planning
Avoid Pro-cyclicality

- **Encourage buffers during times of profitable growth**
- **Capital requirements should not exacerbate the effect of the business cycle**
- **Create sufficient capital for the industry**

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Consider All Risks

- **Risk Categories**
  - Insurance
  - Market
  - Credit
  - Liquidity
  - Operational
- **Should reflect risk mitigants, reinsurance, diversification and concentration**
- **No diversification between categories without conclusive evidence**

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Measure Assets and Liabilities on a Consistent Basis

- **Off balance sheet items must be included**

Be Practical, Yet Technically Sound

- **A standard approach for every risk**
- **Internal models are permitted**
- **Standardized assumptions where they are not dependent on company specific assumptions**
- **Immaterial risks could be based on a standardized approach**

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Reflect Risks on a Going Concern Basis but Reflect Winding-up Costs

- **Risks should be considered on a going concern basis**
- **Future new business and renewals have to be considered**
- **Capital must be sufficient to cover winding-up costs**
  - Terminal liabilities

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Use Measures that are Compatible Across Risks and Products

- **Possible measures**
  - VAR
  - CTE
- **A common time horizon should be used by all institutions**
- **Companies capital targets should exceed regulatory requirements**
  - Economic cycles
  - Desired ratings
  - Risk management philosophy

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Use a Total Asset Requirement

- **Capital and reserve margins should be considered on an integrated basis**
- **Any decrease in reserve margins must be offset by an increase in capital and vice versa**

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Ensure that Capital is Prudent

- **While the Total Asset Approach is used there must be a minimum capital requirement**
- **Leverage ratios and other relevant measures complement a risk based capital test**

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Consider International Principles and Practices

- **The insurance market is global**
- **Must comply with IAIS Standards and Principles**

Allow Comparisons of Similar Risks Across Financial Institutions

- **Banks and Life and P & C Insurance companies should hold comparable levels of capital for similar products**
- **Capital framework should recognize differences in the nature of business**

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Transparent, Validated and Based on Credible Data

- **Users should have ability to analyze models**
- **Minimum standards for data and inputs to models are necessary**
- **Data is subject to audit**
- **Professional Standards (e.g. Actuarial) should be considered**
  - There may be a need for additional standards

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Use Reliable Processes with Assumptions Sustainable in Times of Stress

- **Rules for using models should be clear**
- **A review process should be implemented**
- **The results should be replicable**
- **Material changes will be subject to approval**

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Be Part of Intervention Levels for Supervisory Action

- **Minimum and target capital levels should be established**
- **These levels will define possible supervisory interventions**
- **The capital level for intervention should be sufficiently high to allow supervisory action at an early stage**

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Questions

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