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

Supervisory Framework Renewal

Briefing

Fall 2023

OSFI | BSIF

Canada

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Agenda

1. Why we are updating the Framework
2. A closer look at the new Framework
3. Impact on regulated financial institutions and pension plans
4. Key milestones and timeline

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1 **Why we are updating the Framework**

2 A closer look at the new Framework

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4 Key milestones and timeline

History of OSFI's Supervisory Framework

First Introduced
1999

Limited Updates
2010

Comprehensive Updates
2024

The risk environment is changing rapidly, and we are modernizing our Supervisory Framework to ensure it remains fit for purpose

Our approach

The Supervisory Framework guides our supervision of federally regulated financial institutions (FRFIs) and federally regulated pension plans (FRPPs). We undertook the following initiatives to help inform the design of the new Framework.

Benchmarking peer review

- Five international peer regulators provided observations, recommendations, and considerations
- Bilateral conversations with three other regulatory authorities

Supervisory roundtables

- Supervisory roundtable discussions in early 2022 on technical risk areas (e.g., culture, climate, data and technology)
- Nine foreign regulatory agencies participated in discussions with OSFI

Internal focus groups

- Focus groups organized in early 2022 included a representative mix of OSFI supervision staff
- Feedback from the focus groups have contributed to the conceptual design of the new Framework

Supervisory Framework vision

While our Supervisory Framework is changing, supervisory judgement will remain a core part of OSFI's principles-based approach.

Capturing the impact of systemic and macro-centric risks on the risk profile of rated financial institutions and pension plans

Enabling early corrective action through greater differentiation in risk ratings, particularly within Stage 0 (normal activities)

Building in flexibility in the Framework to accommodate new risks, the interplay between financial and non-financial risks, and non-traditional business models

Leveraging data and advanced analytics to support a more risk-intelligent approach to supervision and the application of judgment

Streamlining and simplifying our supervisory processes to focus effort and empower staff to make more timely decisions

Framework scope and notable changes

Scope	
Who it affects	Federally regulated financial institutions and pension plans
Flexibility	We will update the Framework when needed so that it reflects the risk environment and new capabilities
Intervention Rating effects	No direct impact on intervention ratings
New mandate implications	No immediate impact; some updates possible in medium-term
Tools	Enhance our supervisory management system to achieve better data quality and effective reporting

Notable changes

1. Expanded 8-point rating scale with greater disclosure about risk drivers
2. Linkage to OSFI's risk appetite through new tier ratings reflecting size, complexity, and potential for contagion
3. Introduction of new risk categories including business risk and operational resilience
4. Integration of climate risk considerations
5. Creating additional capacity for risk-based supervisory work

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Three key elements of the new Framework

Entity Level Assessment

Tiering

The tier rating reflects size and complexity, with consideration of potential contagion in the event of failure

Tiering impacts supervisory intensity

Overall Risk Rating (ORR)

The **risk of failure** (level of overall risk to the financial viability) of a financial institution or security of member benefits for a pension plan

Expanded 8-point scale provides more information about risk position

Outcome focused

Disclosure of ratings and their drivers to financial institutions as well as recommendations

Providing more information to help you address supervisory concerns

Supervisory intensity will be driven by impact of failure (tier rating) and risk of failure (ORR)

Tiering

The tier rating reflects size and complexity, with consideration of potential contagion in the event of failure.

Purpose: to create a consistent risk-based approach to supervision in alignment with OSFI's risk appetite

- Institutions are categorized (typically, annually) into tiers based on their size and complexity and consider factors such as interconnectedness and substitutability for banks and insurers.
- Number of applicable risk categories assessed and rated varies by entity tier, with higher tiers requiring more assessment.
- For any given tier, more detailed assessments are carried out as the risk profile increases.
- Tier rating will be communicated to the institutions.

Differences between tiering and SMSB category ratings are presented in the appendix.

Contagion Risk

Tier 1 & 2 — **High and Medium-High**

Failure would materially impact stakeholders and/or financial stability.

Tier 3 — **Medium**

Failure may result in moderate systemic consequences.

Tier 4 — **Medium-Low**

Failure would result in little to no systemic consequences.

Tier 5 — **Low**

Failure would have no systemic impact.

Related institution: Default tier for consolidated institutions

Rating assigned to underlying institutions belonging to a group, where the largest operating institution would be assigned a tier from 1-5 based on tier methodology.

Overall Risk Rating (ORR)

Purpose: An updated and expanded 8-point scale risk rating system with four categories assessing the level of overall risk to the financial viability (risk of failure) of a financial institution or pension plan

Context

1 All categories drive an outcome

All of the four risk categories have the ability to drive the ORR outcome (there are no fixed weights) and all speak to the risk to viability of the institution.

2 What we will disclose*

The ORR is OSFI's assessment of the safety and soundness of the financial institution. Supervisory ratings are not disclosed to pension plans.

To support outcome focused engagement with financial institutions, in addition to disclosure of the ORR, we will disclose the four risk categories that contribute to the ORR for tier 1-4 institutions.

4 Risk categories contributing to the ORR

Overall Risk Rating

- Business Risk
- Financial Resilience
- Operational Resilience
- Risk Governance

* Supervisory ratings are not disclosed publicly and remain prescribed supervisory information

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ORR Scorecard

How it works: An ORR Scorecard will replace the current risk matrix to record our risk assessments of a financial institution or pension plan and provide a consistent approach to rating risks. Our assessments culminate in the ORR.

Disclosed to institutions

NOT disclosed to institution INTERNAL ASSESSMENT ONLY

Tier		ORR Scorecard												
All	ORR	**Overall Risk Rating**												
1-4	Category	Business Risk	Financial Resilience				Operational Resilience			Risk Governance				
1-3	Sub-Category		Financial Risk Profile		Capital	Liquidity	Technology	Cyber	Operations	Governance	Business and Central Functions	Risk & Compliance Oversight	Internal Audit	
1 & 2	Detailed Rating		Insurance		Capital Adequacy	Liquidity Adequacy								
			Credit		Capital Management	Liquidity Management								
			Insurers Only	*Banks Only*										
			Investments	Market (Trading)		Funding Risk								
			Asset/Liability Management	Market (Non-Trading)										
All	Transverse Risk	Climate Risk												

> The number of categories rated depends on the tier and industry

Key features of the ORR Scorecard

Dynamic adjustment

The risk categories that need to be rated depend on the industry and tier of the entity

Rate identified risk

The ratings scale is focused on identified risks and the potential impact on viability

Focus

Rating is focused at the whole level of the financial institution or pension plan– not significant activity

A holistic approach to mitigating risks

Ratings of financial resilience and operational resilience combine risk level and risk management

No fixed weights

Each risk category has the ability to drive the ORR – one issue can influence many categories

Risk responsiveness

Category ratings reflect the level of risk to overall viability related to that category and, as a result, the ORR cannot be better than the weakest category rating

Transverse risk

The scorecard highlights the importance of climate risk that is taken into consideration across the entire scorecard

Supervisory intensity

Supervisory intensity will be driven by risk of failure (ORR) and impact of failure (tier rating)

Rating Scale

How it works: Expanded 8-point rating scale maps to existing Intervention Ratings and provides greater granularity for stage zero entities.

Rating of 1 does not imply perfection

Ratings of 5-8 include assessment of risk level and velocity

ORR Rating Scale		Stage
1	**Minimal** No significant issues identified	0
2	**Low** Issues are unlikely to impact financial performance or critical operations	
3	**Moderate** Issues could impact financial performance or critical operations unless addressed	
4	**Watchlist** Issues expected to impact financial performance or critical operations unless addressed promptly	
5	**Early warning** Issues could impact viability, but this is not expected within two years	1
6	**Material** Issues could impact viability within one to two years	2
7	**Serious** Issues raise serious doubts about viability within one year	3
8	**Non-viability imminent** Non-viability is imminent	4

The changes to the Framework do not have a direct impact on Intervention Ratings

Outcome-focused supervision

Purpose: Increased level of transparency and disclosure to help financial institutions and pension plans prioritize matters requiring attention.

Disclose ORR and the four risk categories to tier 1-4 institutions

Share urgent findings as well as recommendations with institutions

Agility of the new Supervisory Framework

1. Risk ratings can be updated dynamically

2. Once an issue(s) is identified and documented, it is assessed to determine potential impact on viability

3. New risk rating determined based on the weakest rating in any category. Driven by actions OSFI is looking for the financial institution or pension plan to change

4. As a financial institution or pension plan grows, there is greater supervisory intensity

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What it means for you

What is changing

New ORR rating

Institutions will receive an ORR instead of a CRR; assessed on an 8-point rating scale.

Increased transparency and disclosure in supervisory letters

In addition to the ORR, four risk category ratings will be disclosed for tier 1-4 institutions.

Introduction of "urgent findings"

Urgent findings and recommendations will be included in supervisory letters.

What is staying the same

Intervention Stage Ratings

The Intervention Stage Ratings will continue on the existing scale. These stage ratings provide an 'anchor' to our intervention activities as other elements of the Framework change.

Supervisory letters

Institutions will continue to receive annual and interim supervisory letters.

Prescribed Supervisory Information

The rating and recommendations shared by OSFI will still be protected information.

Assessment process

Information requests and interaction with OSFI's Lead Supervisors will remain unchanged to support OSFI risk assessments.

Commitment to transparency

Our objective is to provide more information about our assessments to help address any supervisory concerns. We expect this will lead to a richer dialogue and better assessments.

We welcome your feedback – please let us know what else we can do to achieve this objective.

The Framework provides a structure for our risk assessment. As such, we do not conduct public consultation about changes to the Framework.

We are communicating with stakeholders to explain why and how the Framework is changing, and how it will impact you.

Continuous improvement including post-implementation review and holistic reviews at least once every five years.

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Key milestones and timeline

Sep/ Nov 2023 — Info sessions with largest institutions

Nov 2023 — Industry webinar

Feb 2024 — Publication of new Framework content on OSFI's website

April 2024 — New Framework effective

You will hear more about the timeline and upcoming milestones from your Lead Supervisor.

Questions

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- Questions with the most votes will be prioritized for responses

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- If you have questions later, please reach out to your OSFI Lead Supervisor
- Maria Moutafis (Senior Director of Supervision Methods, Standards and Controls) can also be contacted at SFR-RCS@osfi-bsif.gc.ca