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summary of directors' duties under OSFI guidance

The following chart sets out the duties, obligations, and expected practices of the boards of directors of insurance companies under recent Office of the Superintendent of Financial Institutions ("**OSFI**") Guidelines. Guidelines published in the year 2000 and onwards have been summarized, along with the Derivatives Best Practices (1995) and Earthquake Exposure Sound Practices & Annexes (1998). The summary information with respect to OSFI's Corporate Governance Guideline relates to the final 2003 version and not to the August 2012 draft version because it has not yet been finalized.

OSFI directs its Guidelines towards federally regulated entities ("**FREs**"), including Banks, Foreign Bank Branches and Representative Offices, Trust and Loan Companies, Cooperatives, Life Insurance Companies & Fraternals, and Property & Casualty Insurance Companies. This guide only summarizes the Guidelines applicable to Life Insurance Companies & Fraternals ("**L&F**"), and Property & Casualty Insurance Companies ("**P&C**") where responsibilities are imposed on the board of directors. The entity to which each Guideline is directed (i.e. L&F, P&C, or both) has been indicated.

OSFI Guideline	Guideline Objective	Board of Directors' Responsibilities

Corporate Governance Guideline
 	
January 2003, L&F; P&C
	• sets out OSFI's expectations regarding corporate governance, internal control procedures, oversight mechanisms, and risk management policies
	• FREs are expected to keep up to date with applicable best practices from other institutions, such as securities commissions, stock exchanges, government regulators, and international bodies
	• OSFI conducts on-site examinations and monitors the performance of regulated institutions to assess safety, soundness, regulatory compliance, and quality control
	    ◦ the examination is risk-focused and the quality of oversight and control provided by the board of directors is paramount
	    ◦ examinations consider the governance process against the composition of the board, its roles and responsibilities, the operations of board committees, board practices, and self-assessment programs
		• general board oversight responsibilities include:
		    ◦ reviewing and approving the FRE's organizational structure and controls
		    ◦ reviewing and approving organizational and procedural controls, and ensuring they operate effectively
		    ◦ ensuring that senior management is qualified, competent and appropriately compensated
		    ◦ reviewing and approving broad business strategies and policies for major initiatives and activities
		    ◦ monitoring performance against business objectives
		    ◦ obtaining regular assurance that the institution is operating within an appropriate control framework
		    ◦ ensuring adequate succession planning has taken place for critical management positions
		• effective boards are also expected to:
		    ◦ ensure policies and procedures are understood and followed
		    ◦ understand the regulatory environment within which the board operates, and be open to sharing information with regulators
		    ◦ be informed of regulator examination results and require appropriate follow-up on deficiencies identified by the regulators

	Risk Management
	• risk management refers to understanding the quality of assets and the nature of associated liabilities
	• every FRE should have integrated risk management and risk exposure policies that are tailored to the particular institution
		• risk management duties of the board include:
		    ◦ understanding the types of risks to which the FRE may be exposed and the techniques to control those risks
		    ◦ requiring timely and accurate reporting from management on significant risks and controlling procedures
		    ◦ reviewing and approving the overall risk philosophy and risk tolerance of the institution, along with the institution's risk reporting, monitoring, and management policies
		    ◦ being aware of material changes to the institution's business strategies or risk tolerance
		    ◦ ensuring capital management strategies are in place
		    ◦ assuring itself that the risk management activities of the institution have sufficient independence and are periodically reviewed
		    ◦ including a review of requisite/related changes in risk management and controls in its reviews of changes in strategies or new business initiatives

OSFI Guideline	Guideline Objective	Board of Directors' Responsibilities

	Internal Controls
	• internal control mechanisms support the achievement of the intuition's objectives, contribute to effective risk management, and facilitate compliance with laws and regulations
	• senior management is responsible for developing and implementing internal control mechanisms, which must then be reviewed and approved by the board
		• internal control duties of the board include a review of:
		  ◦ management reports on operations and financial conditions;
		  ◦ reports and opinions of legal counsel, independent auditors, internal auditors, and regulators; and
		  ◦ Dynamic Capital Adequacy Test results and policy liability reports from the appointed actuary
		• the board must also:
		  ◦ evaluate and approve internal control procedures developed by management,
		  ◦ review and discuss reports from independent oversight providers,
		  ◦ understand the regulatory environment within which the board operates, and be informed of OSFI examination results, and
		  ◦ ensure there is appropriate follow-up on recommendations and deficiencies identified by regulators

	Independent Oversight • independent oversight functions (such as internal auditors, appointed actuaries, risk management teams, and external auditors) help the board validate whether internal controls are working and whether the institutions' operations and results are reliably reported • may be undertaken through a board committee such as an audit committee or risk management committee	• ensure independent oversight groups are free from influence, and have adequate resources/authority to provide objective assessments • regularly review and understand the work of these groups, discuss their reports, and follow up on any concerns • recommend an external auditor to shareholders • regularly review internal control functions and activities of external auditors, and approve any major changes to their mandates • regularly review the nature of the function being carried out and the effectiveness and independence of those fulfilling these functions

	Audit Committees
	• FREs are required by legislation to establish an audit committee of non-employee directors, a majority of whom are not affiliated with the institution
	• audit committee members should also be independent board members
	• audit committees review annual statements, evaluate and approve internal control procedures, and review reports from independent oversight providers
		• the board audit committee should:
		  ◦ make recommendations concerning the external auditor's appointment, assess the skills and appropriateness of the auditor's accounting practices, obtain assurances regarding the auditor's independence, and establish criteria for any non-audit services
		  ◦ assure itself that the external audit plan is appropriate, risk-based, addresses major areas of concern, and is reviewed with appropriate frequency
		  ◦ hold regular meetings with the external auditor and appointed actuary, and discuss their correspondence, reports, results, and financial statements (annual and quarterly) with senior management
		  ◦ satisfy itself the financial statements fairly present the financial position of the FRE
		  ◦ regularly review the auditor's performance

OSFI Guideline	Guideline Objective	Board of Directors' Responsibilities

	Subsidiaries
	• parent companies should determine what board structures for subsidiaries allow effective oversight
	• parent companies should pay special attention to the performance and activities of subsidiary boards if:
	  ◦ the subsidiary's activities are significantly different, or the subsidiary operates in a different jurisdiction with different governance expectations
	  ◦ there is the potential for conflicts of interest between parent and subsidiary stakeholders
	  ◦ if actions of the subsidiary may give rise to substantial regulatory or legal risks.
		• be aware of material risks that may originate in subsidiaries
		• exercise adequate control over subsidiaries' activities
		• the corporate governance responsibilities of boards of FREs are the same as those of regulated parent FRE boards
		• the corporate governance responsibilities of regulated holding company boards are the same as those of regulated financial institutions, except that a regulated holding company is not required to have a conduct review committee or to establish procedures to deal with complaints

Guideline A-2 **Capital Regime for Regulated Insurance Holding Companies and Non-Operating Life Companies** July 2005, L&F	• sets out OSFI's expectations that holding companies and operating companies will maintain adequate capital for unexpected losses, and manage their capital in a manner that aligns with their group risk profile and control environment	• general oversight • approve capital management policies • monitor capital levels • ensure appropriate capital management plans are in place at the holding company level • ensure capital plans and targets for each FRE in the group are consistent with their risk profiles
Guideline A-4 **Internal Target Capital Ratio for Insurance Companies** June 2011, L&F; P&C	• describes the regulatory capital ratios considered in the assessment of insurers' capital adequacy • sets out OSFI's expectations regarding Internal Target capital ratios and capital management policies • the Internal Target is the level of capital, based on the company's own risk and capital adequacy assessment process, that is necessary to cover the risks specified in the capital tests as well as all other risks of the insurer • insurers are expected to operate at a level of capital above the Internal Target	• review and approve capital management policy annually or more frequently as conditions warrant, as board has ultimate responsibility for insurer's overall risk management program • establish the Internal Target • oversee management's implementation of the process for determining Internal Target ◦ the process for determining the Internal Target should identify, measure and appropriately consider all material risks • conduct reviews and approvals of appropriateness of Internal Target • receive a report documenting the analysis supporting the determination of an Internal Target, and ensure report is updated annually
Guideline B-2 **Large Exposure Limits** August 2003, L&F	• addresses the issue of large credit risk exposure of life insurance companies and fraternal benefit societies • all companies and foreign branches must set out in writing their internal policies on large exposures, including exposures to individual customers, financial institutions, industries and countries	• approve written policies on large exposures, internal exposure limits, exposures to individual customers, financial institutions, industries and countries • receive reports on exposures against policy limits • monitor exclusions from the definition of exposure

OSFI Guideline	Guideline Objective	Board of Directors' Responsibilities

Guideline B-7
Derivatives Best Practices
 	
May 1995, L&F; P&C
	• outlines what OSFI expects management and the board of directors to consider when including derivative products as part of its investment and financing profile	• approve and periodically review all significant policies pertaining to the institution's use of derivatives
		• when approving policies, consider:
		  ◦ the board's level of risk tolerance and the level and probability of loss from derivatives activity
		  ◦ the capital resources of the institution and its business strategy
		  ◦ the level of expertise of its senior management and trading staff
		• have a good understanding of the institution's risk management process, the derivative products in use and the risk exposure arising from those products
		• ensure senior management has a good understanding of the above
		• approve internal global policy limits on the combined market risk of all financial instruments, which should be consistent with the board's view of the maximum amount of the institution's capital that should be put at risk on an ongoing basis
		  ◦ the global policy limit for market risk should also relate to the measures of risk used internally and be accordingly allocated to individual business units

Guideline B-9
Earthquake Exposure Sound Practices & Annexes
 	
May 1998, L&F; P&C
	• sets out sound practices for the management and measurement of earthquake exposures
	• all companies with earthquake exposure in either British Columbia or Québec must have documented written policies and procedures outlining how they manage earthquake insurance risk; all other companies are encouraged to comply
		• annually review and approve the policies and procedures developed by senior management
		• ensure reviews are documented
		• ensure management adheres to earthquake exposure management policies and procedures
		  ◦ these policies and procedures should quantify the company's willingness to take on earthquake insurance risk and outline how the company's financial resources cover its calculated gross Probable Maximum Loss
		  ◦ exposure management policies should also address data quality and integrity plans

Guideline B-10 **Outsourcing of Business Activities, Functions and Processes** March 2009, L&F; P&C	• sets out OSFI's expectations for FREs that outsource, or contemplate outsourcing, one or more of their business activities to a service provider • as the board retains overall accountability for all outsourcing arrangements, OSFI expects FREs to ensure their boards, chief agents or principal officers receive sufficient information to discharge their duties under this guideline	• ensure that the FRE has appropriate risk management policies and practices in place that are reviewed regularly • periodically approve or reaffirm the policies that apply to outsourcing arrangements (e.g., risk philosophy, materiality criteria, risk management program and approval limits) • review a list of all the entity's material outsourcing arrangements and other relevant reports outlining the success of the outsourcing arrangement and the effectiveness of the risk management program

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OSFI Guideline	Guideline Objective	Board of Directors' Responsibilities

Guideline B-11
Pledging
 	
May 2003, L&F; P&C
	• assists FREs with establishing policies on the creation of security interests in their property and the acquisition of beneficial interests in property that is subject to security interests
	• OSFI expects FREs to establish and implement pledging policies that set out the framework within which pledging can occur in relation to various business activities
		• approve pledging policies
		• review pledging policies at least annually and approve significant changes
		  ◦ when approving pledging policies, take into account factors such as the institution's size, the nature and complexity of its operations, its overall risk philosophy, and its ability to monitor and control transactions that require pledging
		• the pledging policy should include:
		  ◦ an outline of the FRE's objectives when pledging, having regard to the FRE's risk and risk management policy
		  ◦ a description of the business reasons for the activities or transactions that require pledging and appropriate limits
		  ◦ limits on an individual officer's ability to execute agreements or approve transactions that require pledging
		  ◦ measures aimed at monitoring the value and aggregate value of assets pledged in various activities or transactions
		  ◦ the basis, frequency, and format of reporting and monitoring of pledging (although reviews of policies and adherence must be undertaken annually)
		  ◦ appropriate practices and procedures to ensure that the policies are respected

Guideline C-1 **Impairment - Sound Credit Risk Assessment and Valuation of Financial Instruments at Amortized Cost** July 2010, L&F; P&C	• supplements IAS 39, of the International Accounting Standards Board's (IASB) International Financial Reporting Standards, and applies to financial instruments classified at amortized cost under IAS 39 • OSFI may review the adequacy of the allowance for impairment of financial instruments held at amortized cost, and evaluate the FRE's internal review function, its monitoring systems, and whether portfolio credit quality information is regularly provided to the board • the institution's procedures for establishing allowances on individually impaired amortized cost financial instruments must be prudent and appropriate in relation to total credit risk exposure in the portfolio	• overseeing and monitoring the credit risk assessment and impairment processes • ensuring appropriate risk assessment processes and internal controls are in place • receiving information about the credit quality of a portfolio and any related allowances
Guideline B-8 **Deterring & Detecting Money Laundering** December 2008, L&F;	• focuses on risk-based deterrence and detection programs to fight terrorist financing and reduce the susceptibility of FREs to being used to launder funds • FREs must designate Chief Anti-Money Laundering Officers ("**CAMLO**"s) who will supervise and design the FRE's Anti-Money Laundering and Anti-Terrorism Financing ("**AML/ATF**") program	• oversight accountability for approving policies and procedures and regularly monitoring the effectiveness of AML/ATF programs • receive regular reports from CAMLO, the auditor, and other senior officers involved with the AML/ATF program • have an adequate level of understanding about AML/ATF matters

OSFI Guideline	Guideline Objective	Board of Directors' Responsibilities
Guideline E-13 **Legislative Compliance Management (LCM)** March 2003, L&F; P&C	• conveys OSFI's expectations regarding controls through which they manage regulatory risk inherent to their worldwide activities • regulatory risk refers to the risk of non-compliance with the FRE's governing federal legislation (e.g. the *Insurance Companies Act*), its regulations and regulatory directives, and other legislation and regulations applicable worldwide	• receive reports on compliance oversight, regulatory risk management effectiveness, internal audits, and other independent reviews • approve the FRE's LCM framework, and ensure it is implemented and maintained • establish thresholds for the type, content and frequency of reports it expects from internal and independent reviewers • receive regular reports on material LCM program weaknesses, exposures, non-compliance, and remedial action plans at least annually from management's Chief Compliance Officer
Guideline E-15 **Appointed Actuary: Legal requirements, Qualifications and External Review** November 2006, L&F; P&C	• describes the role of the Appointed Actuary ("**AA**") in federally regulated insurance companies • sets out OSFIs expectations for external review of the AA	• receive a copy of the AA's report on any matters that may have material adverse effects on the financial condition of the company • it is good practice for the board audit committee to play a role in the selection of the AA reviewer • the board audit committee should review the external reviewer's written report
Guideline B-3 **Sound Reinsurance Practices and Procedures** December 2010, L&F; P&C	• sets out OSFI's expectations for effective reinsurance practices and procedures, which should form an important part of an insurer's reinsurance risk management policy	• responsibility for oversight of a sound and comprehensive reinsurance risk management policy • board should review and approve the reinsurance risk management policy as a part of its annual review of the enterprise-wide risk management plan • receive annual attestation from management confirming that the risk management practices and procedures meet the standards of the Guideline and that the insurer's reinsurance arrangements effect a risk transfer and are accounted for appropriately.
Guideline E-16 **Participating Account Management and Disclosure to Participating Policyholders and Adjustable Policyholders** November 2011, L&F	• sets out OSFI's expectations regarding the implementation of the requirements found in the *Insurance Companies Act* and *Policyholders Disclosure Regulations* on the subject of participating and adjustable life insurance policies • Permission must be obtained from OSFI to change the basis of the operation of closed participating blocks	• establish criteria for changes to adjustable products • file with the Superintendent a copy of a resolution approving the method of allocation of investment income and expenses to a participating policy account within 30 days of making the resolution • approve allocation methodologies by a resolution • receive annual written reports from the AA on the fairness of the establishment or amending of policies for determining dividends of participating accounts to participating policyholders, and on the management and continuing fairness of each of the participating accounts • consider the AA's reports before establishing or amending a policy for determining dividends or managing participating accounts • ensure the dividend policy includes the principal factors that might cause it to review the policy • formally propose any changes to the basis of the operation of closed participating blocks, and notify OSFI of such changes

OSFI Guideline	Guideline Objective	Board of Directors' Responsibilities
Guideline E-17 **Background Checks on Directors and Senior Management of FREs** February 2008, L&F; P&C	• sets out prudent practices and standards to be considered by all FREs in developing their own policies regarding assessments of directors, principal officers, chief agents, and senior managers (**"Responsible Persons"**) • the primary responsibility for ensuring FREs are soundly managed and directed rests with the board of directors and senior management	• approve a FRE's written policies regarding assessments of the suitability and integrity of its Responsible Persons, as well as any amendments • approve the list of Responsible Persons subject to assessment • if no other process in place, determine whether a Responsible Person is suitable or possesses sufficient integrity to continue in that position • if the Responsible Person is not suitable, then the board must either remove the person or ensure adequate measures are taken to manage the risk of misconduct or mismanagement
Guideline E-18 **Stress Testing** December 2009, L&F; P&C	• sets out OSFI's expectations with respect to stress testing used in making business strategy, risk management, and capital management decisions	• be aware of key findings from stress tests, as board has the ultimate responsibility for the FRE's overall stress testing program • ensure that senior management has a suitable enterprise-wide stress test program in place, and that policies have been adopted requiring stress testing as a management tool

table of summarized of guidelines

All Guidelines are available online from the Office of the Superintendent of Financial Institutions at:
http://www.osfi-bsif.gc.ca/osfi/index_e.aspx?DetailID=527

Guideline	Title	Date	Applicable FREs
	Corporate Governance Guideline	January 2003	L&F; P&C
A-2	Capital Regime for Regulated Insurance Holding Companies and Non-Operating Life Companies	July 2005	L&F
A-4	Internal Target Capital Ratio for Insurance Companies	June 2011	L&F; P&C
B-2	Large Exposure Limits	August 2003	L&F
B-7	Derivatives Best Practices	May 1995	L&F; P&C
B-9	Earthquake Exposure Sound Practices & Annexes	May 1998	L&F; P&C
B-10	Outsourcing of Business Activities, Functions and Processes	March 2009	L&F; P&C
B-11	Pledging	May 2003	L&F; P&C
C-1	Impairment - Sound Credit Risk Assessment and Valuation of Financial Instruments at Amortized Cost	July 2010	L&F; P&C
D-1A	Life Insurance Companies & Fraternals and Property & Casualty Insurance Companies with fiscal years commencing on or after January 1, 2011	July 2010	L&F; P&C
D-1B	Life Insurance Companies & Fraternals and Property & Casualty Insurance Companies with fiscal years commencing before January 1, 2011	February 2009	L&F; P&C
B-3	Sound Reinsurance Practices and Procedures	December 2010	L&F; P&C
B-8	Deterring & Detecting Money Laundering	December 2008	L&F
E-13	Legislative Compliance Management (LCM)	March 2003	L&F; P&C
E-15	Appointed Actuary: Legal requirements, Qualifications and External Review	November 2006	L&F; P&C
E-16	Participating Account Management and Disclosure to Participating Policyholders and Adjustable Policyholders	November 2011	L&F; P&C
E-17	Background Checks on Directors and Senior Management of FREs	February 2008	L&F; P&C
E-18	Stress Testing	December 2009	L&F; P&C