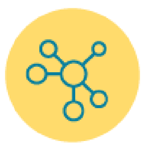
Approach



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Risk Based Supervisory Framework for Ontario-incorporated Insurance Companies and Reciprocals

Purpose

The **Risk Based Supervisory Framework for Ontario-incorporated Insurance Companies and Reciprocals ("RBSF-I")** sets out FSRA's approach for supervision and assessment of Ontario's provincially incorporated insurance companies and reciprocals ("Insurers"). Its primary focus is to determine the impacts of current and potential future events, both internal and external, on the risk profile of each Insurer, and drive FSRA's allocation of supervisory resources.

This Approach Guidance ("Guidance") articulates FSRA's supervisory approach for all Insurers, as well as the practices and processes for determining an Insurer's Overall Risk Rating ("ORR"), Intervention Level ("IL"), and level of FSRA's supervisory activity under the *Insurance Act* (the "*Act*"), supporting Regulations, and FSRA Rules and Guidance.

This Guidance does not prescribe compliance obligations for Insurers. Rather, it describes the processes and practices that FSRA will follow when establishing supervisory plans and exercising supervisory action or discretion powers under the *Act*[1].

The level and extent of supervision under the RBSF-I will depend on the size, complexity, and risk profile of the Insurer, and the potential consequences of an Insurer's failure including systemic impact.

Scope

This Guidance affects the following entities regulated by FSRA under the *Act*:

- Ontario-incorporated Insurance companies
- Reciprocals based in Ontario

As part of its supervisory reviews and assessments, FSRA will apply this framework to subsidiaries, joint ventures, or any other entities connected to the Insurer through financial or management resources, or whose conduct may affect policyholders (i.e., consolidated group supervision).

This Guidance complements the information provided in and should be read in conjunction with other FSRA guidance and supporting publications available on FSRA's website, "Guidance - Life and Health Insurance and Property and Casualty, and General Insurance".

Rationale and background

FSRA uses an integrated (prudential and market conduct) RBSF-I to identify imprudent or unsafe business practices and misconduct impacting policyholders of Insurers and intervene on a timely basis. FSRA uses the RBSF-I to guide its supervisory activities to comprehensively assess the risk profile and determine the overall risk rating of each Insurer.

The RBSF-I is designed to assist FSRA in meeting its statutory objects and obligations under the *Financial Services Regulatory Authority of Ontario Act*, 2016 (the *FSRA Act*)[2]. The RBSF-I will support FSRA's efforts to:

- contribute to public confidence in the insurance sector
- promote high standards of business conduct in the insurance sector
- protect the rights and interests of policyholders
- foster strong, sustainable, competitive, and innovative financial services sectors
- promote and otherwise contribute to the stability of the insurance sector with due regard to the need to allow Insurers to compete effectively while taking reasonable risks

The ORR of an Insurer will also help FSRA consider whether an Insurer should be subject to increased level of supervisory engagement. It will also determine the supervisory actions that typically occur at each of the intervention levels, which may include recovery and resolution activities.

Approach – Processes and practices

FSRA has developed this Guidance to provide clarity in respect of FSRA's supervisory practices and approach to supervision through the articulation of the key principles and features of the RBSF-I. This Guidance also articulates how FSRA assesses the most important prudential and conduct risks posed by Insurers to supervisory outcomes and the extent to which Insurers can manage and mitigate these risks.

The RBSF-I is principles-based and aligned with national and international supervisory practices. The RBSF-I increases the effectiveness of supervision by enabling supervisory outcomes to be met while increasing efficiency through improved processes and resource allocation. It involves allocating resources to the areas of greatest risk; for example, not all activities within an Insurer may need to be assessed for each review or at the same intensity.

Guiding principles and supervisory standards

The foundation of FSRA's RBSF-I is centered around the Risk definition, Principles, and Supervisory standards described below.

Risk definition

The Risk definition provides clarity for the meaning of "risk" wherever it is used in the RBSF-I and is applied consistently in the risk assessments of all Insurers.

Risk in FSRA's RBSF-I is assessed from prudential and market conduct perspectives respectively by considering both possibility of loss to policyholders and possibility that the conduct, acts, or omissions of an Insurer harm or deliver poor/unfair outcomes for its policyholders and consumers.

Principles

The RBSF-I Principles focus on achieving outcomes from supervisory work and are aligned with FSRA's supervisory principles.[3]

Outcomes-focused

Supervisory work is performed to achieve successful supervisory outcomes rather than completing a standard cycle or process.

Risk-based

Supervisory work focuses on material risks of business activities that could pose threats to achieving the key supervisory outcome of policyholder protection.

Dynamic, proactive, and adaptable

Supervisory work is continuous, dynamic, and timely to ensure changes in the business, sector, and environment are identified early and reflected in FSRA's actions and priorities.

Comprehensive

Supervisory work results in a consolidated assessment of the business of an Insurer. This holistic approach includes assessment of all material interests of the Insurer such as subsidiaries, joint ventures, and other material investments and activities.

Supervisory standards

The Supervisory standards describe key aspects of how FSRA supervisors conduct work using the RBSF-I. They form the standards of practice of FSRA supervisors.

Forward-looking

To the extent possible assessments are forward-looking and consider the velocity, persistence, and amount of change of the risks. This enables early identification of issues, timely intervention, and higher likelihood of achieving desired outcomes.

Sound judgment

Supervisors exercise sound judgment, supported by rationale, in assessing the Insurer.

Evidence-based

Supervisors combine sufficient quantitative and qualitative evidence to support observations, recommendations, and requirements.

Efficient and effective

Supervisory work and assessments are planned and completed in an efficient and effective way. This includes use of FSRA's regulatory actions, data collection, filing requirements, guidance documents, enforcement tools, and service standards.

Use of work of others

FSRA uses, where appropriate, the work of others (e.g., External Audit, Internal Audit, the Appointed Actuary, and an Insurer's other Oversight Functions and other regulators) to augment its supervisory work and minimize duplication of effort.

Relationship management

FSRA designates a relationship manager ("RM") as the lead supervisor for each Insurer. The RM is the main point of contact for the Insurer and engages in ongoing dialogue with the Insurer's management and Board. The RM is responsible for leading the maintenance of an up-to-date risk profile of the Insurer and is supported by other staff within FSRA. The RM is responsible for providing FSRA's feedback to the Insurer, leading discussions about the assessment results, and monitoring the Insurer's remediation or action plans to ensure supervisory concerns, expectations, and requirements are addressed in a timely manner.

Proportionality

The level and extent of supervision will depend on the size, complexity, and risk profile of an Insurer, and the potential consequences of an Insurer's failure. Where there are identified risks or areas of concern the degree of FSRA's intervention will be commensurate with the Insurer's risk profile. Insurers that are well managed relative to their risks will require less oversight.

Risk-based supervision for Ontario-incorporated Insurance Companies and Reciprocals overview

This section of the guidance articulates the essential elements of risk-based supervision, facilitated by FSRA's RBSF-I.

A. FSRA's Assessment process

The following elements of FSRA's RBSF-I enable a common approach to assessments across Insurers and over time. The Overall Risk Rating is determined through the assessment of inherent risks, quality of controls and oversight, and financial and non-financial resilience with assessment ratings recorded in the Risk Matrix (refer to Appendix A: Risk Matrix). The various elements of the RBSF-I are described below.

For each of the elements in the Risk Matrix, FSRA will apply a rating based on a five-level scale where the criteria are tailored to each of the elements assessed.

1. Significant activities and importance

An Insurer's significant activities ("activities") are identified at the start of the assessment process. A significant activity can be a line of business, business unit, or enterprise-wide process that is fundamental to an Insurer's business model and its ability to meet its overall business objectives. The identification and assessment of significant activities and their relative importance or materiality require the use of supervisory judgment which is informed by knowledge of an Insurer's external environment, sector, and business profile. To understand the business profile of an Insurer, supervisors use various sources including organization charts, strategic business plans, capital allocations, internal audit reports, and internal/external reporting.

2. Inherent risk

Inherent risk is assessed for each significant activity of an Insurer without regard to size of the activity or the size of the Insurer. Inherent risk is intrinsic to a significant activity and arises from exposure to, and uncertainty from, potential future events. Inherent risk is evaluated before any mitigation and by considering the probability of an adverse impact to an Insurer's[4] capital or earnings, and ultimately its policyholders. When determining the probability of an adverse impact arising from market conduct risk, FSRA will consider the probability that the conduct, acts, or

omissions of an Insurer harm or result in poor/unfair outcomes for its policyholders and consumers.

FSRA uses the following seven categories to assess inherent risk:

- Financial inherent risks
    - credit
    - market
    - insurance
- Non-financial inherent risks
    - operational (including legal)
    - compliance
    - strategic
    - market conduct

The above inherent risk categories cover other risk sub-categories. For example, reputational risk is viewed as a consequence of each of the seven inherent risk categories; therefore, it is contemplated in each of the inherent risk categories and legal risk is considered under operational risk.

Based on the inherent risks identified for a significant activity and the level of these inherent risks, supervisors will assess the extent to which commensurate level of controls and oversight are needed to adequately mitigate the inherent risks.

Refer to Appendix D for details regarding market conduct risk assessments.

3. Quality of Controls and Oversight ("QCO")

The assessment of QCO for each significant activity considers both the appropriateness of their characteristics and the effectiveness of their performance, in the context of the size, complexity,

and risk profile of an Insurer. Characteristics of a function refer to how it is designed to carry out its role. Performance of a function refers to its effectiveness in carrying out its role and responsibilities. The performance assessment is more important than the characteristics assessment. Consequently, the performance assessment will carry more weight when determining the rating of the function.

Controls

Operational management of an Insurer for any significant activity is responsible for the controls used to manage that activity's inherent risks on a day-to-day basis. Operational management ensures that an Insurer's line staff clearly understand the risks that the activity faces and must manage, and that policies, processes, and staff are sufficient and effective in managing these risks. When assessing operational management, FSRA's primary concern is whether operational management can identify the potential for material loss or misconduct that may arise by taking on that activity and has in place adequate controls to mitigate the inherent risks that may materialize and cause loss or misconduct (see Appendix D). In general, the extent to which FSRA needs to review the effectiveness of operational management of a significant activity depends on the effectiveness of an Insurer's Oversight Functions. If an Insurer has sufficient and effective Oversight Functions, FSRA may not need to also assess the effectiveness of operational management.

Oversight functions

An Insurer's Oversight Functions are responsible for providing independent, enterprise-wide oversight to operational management for each significant activity.

FSRA's assessment includes the following six Oversight Functions:

- Actuarial
- Compliance
- Risk Management
- Internal Audit
- Senior Management

- Board

The presence and nature of these functions vary based on the size, complexity, and risk profile of an Insurer and the inherent risks in its significant activities. Where an Insurer lacks a critical Oversight Function and has engaged external expertise to perform that function, FSRA expects an Insurer to maintain accountability for that function (i.e., Insurers can outsource the function's responsibility but not the accountability and ownership of risks).

Where an Insurer lacks some of the other Oversight Functions, they are not sufficiently independent, or they do not have enterprise-wide responsibility, in applying proportionality, FSRA expects other functions (for example Senior Management) to provide the independent oversight.

Oversight Functions should have sufficient stature, authority, and independence from operational management, with unfettered access and a functional reporting line to the Board or the appropriate Board committee.

Controls and oversight assessments, including corporate governance assessments, are based on an evaluation of an Insurer's current practices for controls and oversight related to the Insurer's significant activities.

Enterprise-wide oversight ratings

Enterprise-wide oversight assessments are FSRA's determination of the Oversight Functions' effectiveness across all activities to provide an enterprise-wide view. It considers each function's characteristics and performance, and FSRA's expected outcomes, in executing the oversight responsibilities.

The assessment focuses on how well the Oversight Function oversees an Insurer and considers any weaknesses in the function's characteristics that may not have affected its performance yet but may do so in the future. Hence, these ratings act as early warning indicators of potential future performance issues with the Oversight Functions within the activities.

4. Residual risk

Residual risk is defined as inherent risks mitigated by the quality of controls and oversight functions. For each significant activity the level of residual risk is determined by considering all relevant and rated inherent risks and QCO ratings. For each significant activity FSRA will assess

the QCO and the degree to which it is commensurate with the level of inherent risks so that the residual risk is considered prudent.

5. Prudential Summary Residual Risk (“PSRR”), Market Conduct Summary Residual Risk (MCSRR), Summary Residual Risk (“SRR”)

The PSRR (from the prudential perspective) and MCSRR (from the market conduct perspective) measure the prudential and market conduct risk profiles of an Insurer based on inherent risks taken on by engaging in significant activities, mitigated by controls and oversight functions, but before the assessment of capital, liquidity, and resilience.

The PSRR is the aggregation of the ratings for the prudential residual risks of all significant activities weighed according to their importance. The MCSRR is determined in a similar way to the PSRR but from a market conduct perspective.

The SRR is determined after considering both the PSRR and the MCSRR.

6. Capital (including Earnings), Liquidity, and Resilience

This section should be read and interpreted in conjunction with the information published in other relevant FSRA guidance, rules and supporting publications.

Capital (including Earnings)

Capital is a source of financial support to protect against unexpected losses and is a key contributor to the safety and soundness of the Insurer. Capital management is the ongoing process of raising and maintaining capital at levels sufficient to support planned operations. For more complex Insurers, capital management also involves allocation of capital to recognize the level of risk in various activities.

FSRA assesses the capital adequacy of an Insurer on both a current (at time of assessment) and forward-looking time frame (e.g., how expected earnings would affect capital).

This approach enables a longer and wider view of an Insurer’s capital adequacy and recognizes the key role that retained earnings plays in maintaining and building the capital base of Insurers. FSRA uses quantitative and qualitative measures in the assessment of an Insurer’s capital adequacy and capital management program.

Liquidity

Liquidity is the ability of an Insurer to obtain sufficient cash or its equivalents in a timely manner at a reasonable price to meet its commitments as they fall due. Managing and maintaining adequate levels of liquidity are critical for the overall safety and soundness of an Insurer. An Insurer must ensure that there is enough liquidity for orderly funding, operational expenses, and other obligations, and provide a prudent cushion for unforeseen liquidity needs. An Insurer's obligations, and the funding sources used to meet them, depend significantly on its business mix, balance sheet structure, and the cash flow profiles of its on and off-balance sheet obligations.

Liquidity risk management is necessary given that a liquidity shortfall of an Insurer can have potential sector-wide repercussions. FSRA uses quantitative and qualitative measures in the assessment of an Insurer's liquidity adequacy and liquidity management programs.

Resilience

Resilience is the ability of an Insurer to respond to adversity, absorb shocks, and adapt to changes especially during a period of stress or crisis. It is the ability of an Insurer to continue to:

- deliver on its objectives
- remain sustainable and prosper
- make positive adjustments under challenging conditions
- emerge strengthened and more resourceful

The Board and Senior Management of an Insurer have a fiduciary duty which includes the obligation to plan for adverse scenarios and to ensure that an Insurer is crisis prepared. This aligns with FSRA's goal of protecting policyholders and contributing to the stability of the sector in Ontario.

Significant stress or failure of one Insurer could accelerate stress at others and lead to other failures in the sector. Risk of contagion could further manifest in the broader financial services system in Ontario due to loss of confidence of policyholders.

A resilient Insurer should be able to:

- monitor the current environment
- anticipate future threats and opportunities
- respond effectively to any type of event
- learn from past failures and successes

Overall resilience of an Insurer is assessed holistically through both financial and non-financial factors and considers both “business as usual” and “stress event” conditions. Financial resilience factors include capital and liquidity; non-financial factors are generally governance and operational-based and focus on crisis preparedness. Some key indicators of resilience are the strength of an Insurer’s Own Risk & Solvency Assessment (“ORSA”), the Recovery Plan, the Business Continuity Plan, and the Disaster Recovery Plan

7. Overall Risk Rating (ORR)

The ORR is an assessment of the Insurer’s overall risk profile, after considering the impact of Capital (including Earnings), Liquidity, and Resilience on its SRR. It reflects FSRA’s assessment of the safety and soundness of an Insurer. The ratings from the Capital, Liquidity, and Resilience assessments are used to determine modification needed to the SRR, if any, to arrive at the ORR.

The five risk ratings for the ORR are: “Low”, “Low-Moderate”, “Moderate”, “Moderate-High” and “High” (descriptions of each of the five ORR risk ratings are detailed in Appendix B).

B. Supervisory process

FSRA uses a defined process to guide its insurance-specific supervisory framework that includes the following:

1. Developing a supervisory strategy and planning supervisory work

A supervisory strategy (“strategy”) for each Insurer is prepared annually. The strategy identifies the supervisory work necessary to keep the Insurer’s risk profile current. The intensity of supervisory work depends on the size, complexity, and risk profile of an Insurer. The strategy outlines the supervisory work planned for the next three years, with more detailed description of

work for the upcoming year. The strategy is the basis for a more detailed annual plan, which indicates the expected work and resource allocations for the upcoming year.

FSRA's planning also includes a process to compare the work effort across Insurers. This is to ensure that assessments of risk for individual Insurers are subject to a broader standard, and to assign supervisory resources effectively to higher-risk Insurers and significant activities.

2. Executing supervisory work

Supervisory work includes, but is not limited to, the following:

- monitoring
- targeted assessment
- comprehensive assessment

Monitoring refers to the regular review of information about an Insurer, its industry, and external environment to keep abreast of changes that are occurring or planned in an Insurer, and to identify emerging risks and issues. Issues include both Insurer-specific and sector-wide concerns.

Insurer-specific monitoring includes the analysis of an Insurer's financial results, typically considering its performance by business line and vis-à-vis its peers and any significant internal developments. The other reviews and assessments refer to more extensive supervisory work than monitoring and may involve on-site work depending on the specific requirements identified in the planning process.

In addition to the core supervisory work of monitoring, and assessments, FSRA undertakes thematic, comparative, and benchmarking reviews to identify standards, best industry practices, and sector-wide patterns.

FSRA periodically requires Insurers to perform specific stress tests that FSRA uses to assess the potential impact of changes in the operating environment on individual Insurers or industries. Environmental scanning and stress testing have increased in importance as changes in the external environment are a main driver of rapid changes in Insurer risk profiles. FSRA may also request the insurer's internal auditor, or at an Insurer's expense, its external auditor, or other

external resource (e.g., consulting firm or appointed actuary) to investigate and report on a matter to FSRA.

3. Updating assessments

Through monitoring if new information indicates a material change in an Insurer's risk profile, the assessment and ratings will be revisited and changed to reflect the current state of the Insurer. When there are shifts in the risk assessment of an Insurer, FSRA responds by adjusting work priorities set out in the supervisory strategy and annual supervisory plan as necessary to ensure that important emerging matters take precedence over items of lesser risk. Such flexibility is vital to FSRA's successful implementation of risk-based supervision and its ability to meet its legislated mandate.

Assessments for all Insurers are subject to FSRA's rigorous quality assurance process to ensure ratings are proportionate, accurate, and consistent.

4. Reporting and communication to Insurers

In addition to ongoing discussions with Insurer management through the RM, FSRA communicates to Insurers through Supervisory Letters. Supervisory Letters summarize FSRA's recommendations and requirements as necessary based on the supervisory work (both prudential and market conduct) that was completed since issuing the last Supervisory Letter and discloses or affirms the Insurer's ORR.

During the year FSRA may also issue an Interim Supervisory Letter to an Insurer to provide change in the ORR and/or timely feedback on issues arising from a specific body of supervisory work, especially if a recent review was performed.

With both types of letters FSRA will discuss the recommendations and requirements with an Insurer before issuing the letter. FSRA considers communication and the provision of feedback to an Insurer an important part of its supervisory process.

5. Intervention level

The ORR of an Insurer is used in determining the level of intervention FSRA will take to address identified prudential or market conduct issues. FSRA's Intervention Guide (**"**The Guide**"**) addresses situations where FSRA has concerns with an Insurer's corporate governance,

oversight, conduct, viability, or solvency. The Guide (Appendix C of this Guidance) aims to communicate at which level an action/intervention would typically occur. The Guide also provides a mapping of the typical combinations of ORR and Intervention Level.

6. Level of supervisory engagement

After determining the intervention level proportionality is applied to the ORR of an Insurer to determine the level of supervisory engagement (i.e., amount of FSRA resources and attention placed on an Insurer). FSRA will have a higher level of supervisory engagement with larger and/or more complex Insurers whose misconduct or failure could materially impact the sector.

FSRA will also have a higher level of supervisory engagement with Insurers that have higher risk profiles.

The misconduct or failure of a large or complex Insurer could give rise to contagion and undermine public confidence in the insurance sector. Therefor FSRA's risk tolerance is low for these Insurers that display an elevated risk profile. Hence, FSRA will allocate more resources and supervisory attention to those Insurers to reduce the likelihood of their misconduct and/or failure, including in extreme cases, exercising its authority under section 62 of the *Act* to take possession and control of the assets of an Insurer and conducts its business, taking such steps as are required towards its rehabilitation.

Effective date and future review

This Guidance will be effective as of April 3, 2023 and will be reviewed on or before April 2028.

About this guidance

This Guidance is consistent with FSRA's Guidance Framework.

As Approach Guidance it describes FSRA's internal principles, processes, and practices for supervisory action and application of Chief Executive Officer discretion. Approach Guidance may refer to compliance obligations but does not in and of itself create a compliance obligation. Visit FSRA's Guidance Framework to learn more.

Appendix A: Risk matrix

The Risk Matrix (as shown below) is used to record all the assessment ratings described above. The purpose of the Risk Matrix is to facilitate a holistic assessment of an Insurer. This assessment culminates in an Overall Risk Rating ("ORR"), which represents the overall risk profile of an Insurer.

FSRA RBSF-I RISK MATRIX – Insurers

Significant Activities	Inherent Risks							Quality of Controls and Oversight							Residual Risk		
	Credit	Market	Insurance	Operational	Compliance	Strategic	Market Conduct	Operational Management	Actuarial	Compliance	Risk Management	Internal Audit	Senior Management	Board	MC	Prudential	Importance
									Enterprise-Wide Oversight Ratings					MCSRR	PSRR	
														SRR		

IR, Residual Risk, MCSRR, PSRR, SRR and ORR ratings:
Low, Low-Moderate, Moderate, Moderate-High, High

QCO, Capital, Liquidity, Resilience ratings:
Strong, Adequate, Needs Improvement, Inadequate, Weak

Importance ratings:
Low, Medium, High

Capital & Earnings	
Liquidity	
Resilience	
Overall Risk Rating	ORR
Intervention Level (IL)	IL

Appendix B: ORR level descriptions

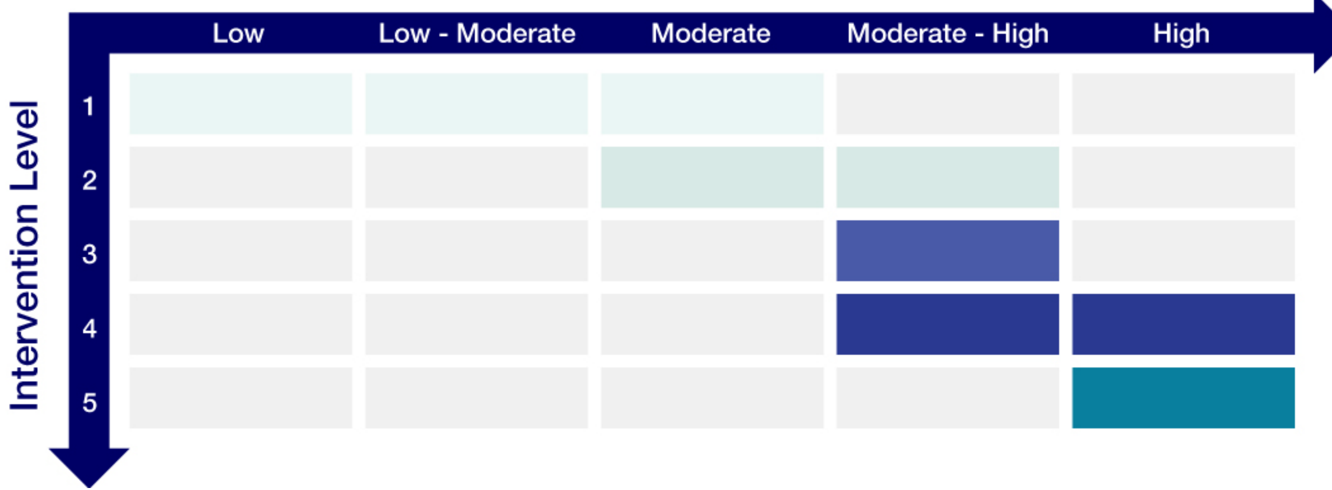
ORR Rating	Description
Low	This rating indicates a highly safe, sound, well-managed, and well- governed Insurer. The combination of its summary residual risk and its capital, liquidity, and resilience makes the Insurer resilient to most adverse business and economic conditions, which will not materially affect its risk profile. The Insurer has consistently performed well and most key indicators are better than sector averages.
Low-Moderate	This rating indicates a safe, sound, well-managed, and well- governed Insurer. The combination of its summary residual risk and its capital, liquidity, and resilience makes the Insurer resilient to many adverse business and economic conditions, which will not materially affect its risk profile. The Insurer has generally performed well and many key indicators are better than sector averages.
Moderate	This rating indicates a generally safe, sound, well-managed, and well-governed Insurer. The combination of its summary residual risk and its capital, liquidity, and resilience makes the Insurer resilient to some adverse business and economic conditions which will not materially affect its risk profile. The Insurer's performance is satisfactory and key indicators are generally comparable to sector averages.
Moderate-High	The Insurer has safety and soundness concerns. It has issues that trigger early warning indicators of potential misconduct or financial non-viability if not addressed. One or more of the following conditions are present:

ORR Rating	Description
	• The combination of its summary residual risk and its capital, liquidity, and resilience makes the insurer vulnerable to some adverse business and economic conditions. • Its performance is unsatisfactory or deteriorating, with some key indicators below sector averages. • The Insurer has issues or weaknesses with its controls and oversight that although not serious enough to present an immediate threat to financial viability or solvency could deteriorate into serious problems if not addressed promptly.
High	The Insurer has serious safety and soundness concerns. One or more of the following conditions are present: • The combination of its summary residual risk and its capital, liquidity, and resilience makes the insurer vulnerable to most adverse business and economic conditions, posing a serious threat to its viability or solvency unless effective corrective action is implemented promptly. • Its performance is poor and most key indicators are worse than sector averages

Appendix C: Intervention guide

Intervention level

The ORR of an Insurer is used to determine the level of intervention or remediation FSRA will take to address any prudential or market conduct issues identified. FSRA has also developed this Guide to address situations where FSRA has concerns with an Insurer's vulnerabilities, practices that could lead to misconduct, or when viability or solvency are of concern. The Guide gives summary descriptions of Insurer risk profiles for each intervention level and indicates supervisory actions that typically occur at each level. The intervention process is not fixed as circumstances may vary from case to case. It is not a rigid regime under which every situation is necessarily addressed with a predetermined set of actions. The Guide aims to communicate at which level an action would typically occur, and the actions described at one level may also be used in subsequent levels; in some situations, certain actions may also take place at earlier levels than set out in the guide. If warranted, an Insurer's intervention level can be increased or decreased by more than one level at one time. Risk profiles as summarized by the ORR and typical supervisory actions for each corresponding intervention level are described below.



Intervention Level

- Level 1
- Level 2
- Level 3
- Level 4
- Level 5

Intervention Type

- Enhanced Monitoring
- Watchlist
- Recovery
- Resolution

Level 1 – Normal

The Insurer has a sound financial position, adequate market conduct practices, and sufficient controls, oversight, and governance for its size, complexity, and risk profile. Its practices do not indicate any significant problems or material deficiencies. Early Warning System (“EWS”) ratios are not indicating material issues or flags. The Insurer is not likely to fail or pose any undue loss or harm to policyholders and consumers in foreseeable circumstances.

Level 1 supervisory actions include but are not limited to:

- monitoring of select information on a monthly, quarterly, and/or annual basis
- performing other supervisory activities including assessments and reviews
- providing the Insurer with a supervisory letter annually and interim supervisory letter as warranted

Level 2 – Early warning

The Insurer categorized at this level is not expected to fail or engage in practices that pose any immediate loss or harm to policyholders and consumers; however, there are aspects of its risk profile that may create vulnerabilities under adverse circumstances, or its future trend may create vulnerabilities in the mid-term, and as such requires more extensive oversight by FSRA. Some EWS ratios have moved outside of the normal range. At level 2, the Insurer is expected to implement an improvement plan to rectify or address identified concerns and commit to reducing its level rating. FSRA expects the Insurer to return to level 1 (normal) within the timeframes established by an appropriate improvement plan.

In addition to activities in the preceding level, Level 2 supervisory actions may include but are not limited to:

- placing an Insurer on the watchlist
- higher frequency of assessments and reviews
- requiring special assessments performed by external experts
- requesting more frequent and detailed collection and analysis of data
- performing follow up and assessment of remediation/action plan
- communicating concerns to the Insurer’s Board, senior management, and internal and external auditors
- requesting stress testing, revised business plan, and/or risk appetite statement
- establishing or issuing expectations under a voluntary compliance agreement

Level 3 – Risk to financial viability or solvency

Improvements are needed as an Insurer's business operations or circumstances potentially put policyholders at risk. EWS ratios and indicators may be significantly outside normal range. At this level, these improvements will be mandated by FSRA. The Insurer is unlikely to fail in the short-term but supervisory intervention is necessary to help avert any failure. At level 3, the Insurer must address identified problems or implement improvements to quickly reduce its level rating. The Board and Senior Management must demonstrate a commitment to improvement by establishing urgent timelines. FSRA expects the Insurer to reduce its level rating within the determined timeframe.

In addition to activities in preceding levels, Level 3 supervisory actions may include but are not limited to:

- requiring recovery or restructuring plans
- implementing the recovery or restructuring plan
- requiring the Insurer to revise its business plans
- expecting an Insurer to increase liquidity and/or capital levels
- requiring the Insurer to consider merger opportunities under FSRA's oversight
- entering into a voluntary compliance agreement
- placing conditions or prohibitions on business authorization

Level 4 – Future financial viability or solvency in serious doubt

The Insurer has severe safety and stability concerns and is experiencing problems that are expected to pose loss to policyholders unless corrective measures are promptly undertaken. EWS ratios and indicators may be critically outside normal range. The Insurer has failed to remedy the issues identified in previous intervention levels and its situation is worsening. At level 4 the Insurer will be directed to immediately resolve issues or implement mandated improvements. Immediate actions will be taken to reduce the Insurer's overall risk profile and intervention level.

In addition to activities in preceding levels, Level 4 supervisory actions may include but are not limited to:

- FSRA taking possession and control of the assets of an Insurer pursuant to s. 62 of the *Act* after the CEO makes a report under s. 58 of the *Act*
- implementing the recovery or resolution plan
- winding down or merging with another Insurer
- divesting non-core businesses
- sale of assets
- requesting financial assistance from the Property and Casualty Insurance Compensation Corporation ("PACICC") or the Fire Mutual Guarantee Fund ("FMFG")

Level 5 – Nonviability or insolvency imminent or has occurred

The Insurer is experiencing severe financial difficulties and has deteriorated to such an extent that there is a high level of certainty that the Insurer has insufficient resources (for example capital) to adequately protect policyholders.

In addition to activities in preceding levels, Level 5 supervisory actions may include but are not limited to:

- suspending or canceling the Insurer's licence
- winding-up the Insurer under the *Corporations Act* or other applicable insolvency and bankruptcy regimes
- implementing the Insurer's resolution plan
- notifying PACICC or the FMFG of the insolvency
- claims payout and premium refunds, where applicable, by PACICC or the FMGF.

Appendix D: Market conduct assessments

As an integrated regulator, both market conduct and prudential risks are essential components of FSRA's supervisory framework. Market conduct risk refers to the probability that the conduct, acts, or omissions of an Insurer or its staff harm or deliver poor/unfair outcomes for consumers. Provincially incorporated Insurers and reciprocals are subject to a risk-based approach to market conduct supervision carried out by FSRA.

Market conduct risk is assessed by evaluating the controls Insurers have in place to ensure compliance with the *Act* and its regulations, and with FSRA rules and guidance. Ensuring the fair treatment of customers ("FTC") is the guiding principle in market conduct assessments. Regulatory expectations for FTC are set out in FSRA's Guidance, *Fair Treatment of Customers in Insurance*, and may include assessing Insurer controls as they relate to:

- corporate governance
- agent training and outsourcing arrangements
- incentives and remuneration
- product marketing and advertising
- point-of-sale information
- claims handling
- complaint handling and dispute settlement

Insurer conduct assessments can be initiated pursuant to alleged patterns or practices reported, risk-based assessments, or proactive monitoring to identify non-compliant business practices. FSRA utilizes data such as the Annual Statement on Market Conduct, annual attestations, thematic reviews, and complaint trends, to inform its assessment of Insurer conduct risk and to select of Insurers for supervision activities. FSRA also monitors media trends, incorporates government priorities, and engages with stakeholders to identify and verify the greatest consumer protection risks in the sector.

Note: In addition to market conduct supervision, Insurers providing auto coverage are subject to FSRA's auto assessment regime, which ensures that insurance companies' proposed rates are fair and not excessive.

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[1] Both the CEO of FSRA and FSRA may exercise discretion under the *Act*. However, for the purposes of this Guidance, reference will be made to FSRA, instead of the CEO, as the CEO may delegate his authority to FSRA, as permitted by the *Act*.

[2] See ss. 3(1), 3(2) and 3(4) of the *FSRA Act*.

[3] FSRA uses the following principles as the foundation for its approach to using guidance: Accountable (Internal and External), Effective, Efficient, Adaptable, Collaborative and Transparent. The definitions of these principles can be found on the FSRA Guidance Framework webpage.

[4] Note that supervisors assess the insurer's inherent risk in the context of the industry experience and the "impact" is to the generic institution ("an institution") and not the specific insurer that is being assessed. In contrast, later when arriving at the Summary Residual Risk we refer to the impact to the specific insurer being assessed.