



Canadian Life
and Health Insurance
Association Inc.

Association canadienne
des compagnies d'assurances
de personnes inc.

January 31, 2014

Submitted to FSB via email

Financial Stability Board

Re: FSB Public Consultation Document – Guidance on Supervisory Interaction with Financial Institutions on Risk Culture (“Draft Guidance”)

The Canadian Life and Health Insurance Association Inc. ("CLHIA") is a voluntary trade association whose member companies account for 99 percent of Canada's life and health insurance business. Our industry provides a wide range of financial security products such as life insurance, annuities and supplementary health insurance to about 26 million Canadians.

The CLHIA welcomes the opportunity to provide input to the FSB on the Draft Guidance.

Executive Summary

We support the FSB's initiative to formalize the process to assess risk culture at financial institutions, particularly SIFIs. In formalizing this process, it should be recognized that: risk culture is company and jurisdictional specific; assessing the effectiveness of risk culture involves a high degree of judgment and subjectivity; the application of the principle of proportionality is key to achieving effectiveness; and management and supervision of risk culture practices continue to evolve and improve. Therefore, we believe that supervisory expectations for the assessment of risk culture should be as principles based as possible to recognize the diversity, subjectivity, proportionality of application, and evolution of specific practices. Accordingly we appreciate the FSBs decision to release its paper in the form of Guidance and recommend that the Guidance avoid undue prescriptiveness.

Introduction

The CLHIA supports the following principles outlined in this paragraph of the Draft Guidance:

- The approach should be pre-emptive, rather than reactive, outcomes-based supervision.
- Supervision encompasses ensuring not only compliance with the rules but also with the spirit and ensuring there are appropriate behaviors and judgments.
- The Guidance does not define a “good” or “bad” culture.
- The appropriateness of the four categories of indicators.
- Recognition that differences in risk culture might be driven in part by differences in corporate and also national cultures.

We are of the opinion, as a result of our views outlined in the remainder of this submission, that the Guidance should address, in the Introductory section, the premise that there is not a necessarily highly causal effect of intensity on effectiveness, and that for assessments of risk culture, the principle objective should be to seek effectiveness.

Judgment and Subjectivity

The assessment of the effectiveness of risk culture by both management and the supervisor is inherently very subjective. Therefore it may be difficult to ensure the Guidance is applied on a consistent basis across the industry. Culture is manifested through employees. The assessment of their “risk integrity” involves judgment more than against objective metrics. The best example of effective risk culture at the top of an organization may be different than at other levels in the organization. Therefore, while we are supportive of the Guidance being applied at an individual institution level we would strongly caution against applying it in horizontal or cross sector reviews.

Proportionality

While the Guidance has been developed specifically for SIFI’s we believe it is likely that this Guidance will quickly be applied to many financial institutions. As such we believe it is important for the Guidance to emphasize the principle of proportionality. The intensity of the assessment of risk culture must reflect the nature, scale and complexity of the types of risks assumed, the size of organization, the organization’s legal structure and the complexity of the organization’s operations. The assessment of effectiveness of risk culture is by its very nature intangible and therefore consistently providing evidence for it is challenging and may force financial institutions to take actions that would burden the natural flow of business and risk control.

Guidance Prescriptiveness

Practices for assessing risk culture are evolving, vary among jurisdictions and types of institutions, and are very specific to a particular company. Hence the Guidance should avoid granularity and prescriptiveness as much as possible. Even recognizing the “guidance” status of the document, institutions and their supervisors may feel compelled to error on the side of ensuring “compliance”. This could result in unnecessary burdens to create and maintain processes and documentation to “prove compliance” without commensurate benefit of improvements in risk culture.

General Supervisory Guidance

The Draft Guidance states: “The challenge for supervisors is to strike the right balance between taking a more intensive, proactive approach and not unduly influencing strategic decisions of financial institution’s management”. The CLHIA views this as a vital pre-requisite to achieving effectiveness. It should be emphasized earlier on in the document (in the Introduction section), including, for example: clarifying supervisory assessments should not have the effect of influencing the culture towards undue risk avoidance; the Guidance’s objective is to strive to increase the effectiveness of risk culture without an exhaustive “checklist” of prescriptive requirements and expectations; processes of “mechanisms to assess” and the “gathering of evidence” should be viewed as risk management tools as opposed to merely compliance exercises.

Specific Comments

We are concerned, as currently drafted, about the assessment of risk culture including identifying the root cause of *why* there are supervisory findings and believe further clarification on what this entails is required. We are supportive of supervisors recognizing the role risk culture plays in the sound management of institutions and believe where weaknesses in risk culture are evident they should be raised. However, requiring supervisors to determine *why* there is a finding in most, or all instances, could lead to a counter-productive, even adversarial relationship between supervisors and management on a highly subjective, judgment driven topic.

Regarding the “Tone from the top” indicator, we have two comments on the sub-indicators. The Draft Guidance only addresses actions related to *failures* in risk culture. We believe the review of risk culture *successes* will also provide valuable insights into strengthening risk culture as it will assist in highlighting both good and bad judgments and behaviors. Secondly, many of the sub-indicators refer to both the Board and Senior Management together. This implies more of a hands on role for the Board instead of stewardship. The Board should concentrate more on establishing the tone, leaving senior management to operationalize it.

The CLHIA trusts our comments provide the FSB with valuable insights to assist it with finalizing the Guidance.

We would be pleased to provide any further insights to the FSB.

Sincerely

A handwritten signature in black ink, appearing to read 'S. Easson', written in a cursive style.

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