



SUCCEEDING IN A CHANGING ENVIRONMENT

OSFI ANNUAL REPORT

2001-2002



Office of the Superintendent  
of Financial Institutions

Bureau du surintendant  
des institutions financières

Canada



## OSFI'S MISSION

We are the primary regulator of federal financial institutions and pension plans. Our mission is to safeguard policyholders, depositors and pension plan members from undue loss by advancing and administering a regulatory framework that contributes to public confidence in a competitive financial system. We also provide actuarial services and advice to the Government of Canada.

We are committed to being a professional, high-quality and cost-effective organization.

Letter of Conveyance	02
Superintendent's Message	03
Role and Responsibilities	06
Mandate and Objectives	07
New Regulatory Environment	10
Impact of September 11 <sup>th</sup>	11
International Environment	13
Enhancing the Supervisory Framework	15
Recent Corporate Failures	17
Office of the Chief Actuary	18
Priorities Going Forward	20
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Financial Statements	21
Appendix 1 – Complaints and Enquiries	36
Appendix 2 – Disclosure of Information	39
Consumer Information	41

## TABLE OF CONTENTS

□ Letter of Conveyance

The Honourable John Manley, P.C., M.P.  
Deputy Prime Minister and Minister of Finance  
Ottawa, Canada K1A 0A6

Dear Minister:

Pursuant to section 40 of the *Office of the Superintendent of Financial Institutions Act*, I am pleased to submit to you and the Secretary of State (International Financial Institutions) the Annual Report of the Office of the Superintendent of Financial Institutions for the period April 1, 2001, to March 31, 2002.

Yours sincerely,



Nicholas Le Pan  
Superintendent

Ottawa, October 1, 2002  
c.c.: The Honourable Maurizio Bevilacqua

## □ Superintendent's Message

The theme of OSFI's 2001-2002 annual report is "Succeeding in a Changing Environment".

Over the past year, we have faced the September 11<sup>th</sup> tragedy. We have seen billions of dollars in value disappear in the telecom sector and in equity markets more generally. Credit quality issues have emerged in several industries and North America has experienced an economic slowdown. A number of other serious events, such as financial statement surprises at major industrial corporations and financial crises in certain emerging market economies, have also contributed to increased uncertainty in world markets. Profitability in parts of the financial services industry or certain business lines has suffered as a consequence.

We at OSFI are often asked whether we are worried given such stresses. OSFI is paid to be aware of risks in the system and be prepared to address them, but not to overreact.

One of OSFI's responsibilities is to remember the lessons of the past and to remind institutions of the risks that may lie ahead. The system is more resilient today in part because of measures taken by OSFI over the past several years to encourage institutions to strengthen their capital and provisioning levels. During the year under review and the year prior, OSFI significantly enhanced the breadth and depth of its assessment of credit quality and credit risk management processes. As well, efforts on the part of institutions and regulators to update contingency plans in anticipation of Y2K served us well in the aftermath of September 11<sup>th</sup>.

Credit quality deterioration overall has been much less than in the early 1990s and capital levels at most federally regulated financial institutions remain well above OSFI's target levels. As of writing, the economic recovery in Canada is proceeding, although the recovery is less robust in the United States. While individual financial institutions have experienced losses, generally these have been manageable.



Canadians rightly have a high degree of confidence in their financial system. The overall strength of the industry and the quality of governance and risk management in place at financial institutions supports that confidence. So does our sound and effective regulatory system. High-quality regulation benefits financial institutions and all Canadians.

Over the next few years, OSFI will be judged on: how well we anticipate and deal with problems that arise; how appropriately our various regulatory and supervisory frameworks are structured and implemented; and the professionalism we demonstrate in all our endeavours.

OSFI has a mandate from Parliament for early intervention when material issues arise that might compromise the safety and soundness of individual institutions. We will continue to actively pursue this mandate. Encouraging institutions to act quickly and decisively when a problem is identified in its early stages improves the chances of success and helps to maintain confidence in the financial system in Canada.

At the same time, OSFI's role is not to impede responsible business endeavours. Risks must be taken and innovation encouraged if the industry is to grow and prosper. Good management and profitability are always the first line of defense for institutions when coping with adverse developments. A well-managed, profitable institution is usually a sound one; an institution suffering chronic losses is not.

There will be times when OSFI has to intervene to protect depositors and policyholders, but it is not our role to provide a failure-proof system. That kind of guarantee does not exist in a competitive marketplace and would not be desirable even if it did. Our governing legislation anticipates the possibility of business failures and gives OSFI the means to respond.

### **A strong regulatory system in Canada opens doors globally.**

How we set and put into effect our rules and supervisory framework can be an aid or an unwarranted impediment to institutions' success. In carrying out our mandate, OSFI must balance safety and soundness with the need for intelligent risk taking in a competitive financial sector. New rules are not always an appropriate reaction to events in the market place. On the other hand, financial institutions need to operate under an effective regulatory and supervisory system because it facilitates their access to capital and raises their status as counter parties. A strong regulatory system in Canada opens doors globally.

Canada is a relatively small player in world capital markets and cannot afford an inefficient regulatory system. By focussing on issues of greatest importance, OSFI can succeed in reducing the costs of supervision for well-managed firms. In recent years, we have introduced more flexible regulation and have made use of the work done by institutions themselves to manage and control risks. It is a direction in which OSFI will continue to move, provided we can continue to rely on effective governance and risk management processes that are supported by

effective checks and balances from those such as auditors and actuaries. Although recent events have led to some doubts about the effectiveness of checks and balances, OSFI has taken action, as outlined elsewhere in this report, to increase the likelihood of these mechanisms being effective.

Paying attention to the costs incurred by financial institutions in complying with regulation is at least as important as keeping our own direct costs under control. By changing the way we supervise institutions – a path we embarked on three years ago – we are putting our focus on

**As external events affect financial institutions, OSFI can advise, prod and regulate, but we do not manage them.**

areas of greatest risk. Another major effort in that regard was gearing up for implementing the federal government's new financial services legislation. Getting our framework right – whether it's our supervisory framework, capital framework or regulatory/legislative framework – is important. OSFI will continue to regularly assess how we are doing in this regard.

As external events affect financial institutions, OSFI can advise, prod and regulate, but we do not manage them. The ultimate responsibility for running safe and sound institutions rests with the boards of directors and management of the institutions. We will continue to promote effective corporate governance and robust risk management in financial institutions as well as effective external checks and balances that are key to a sound regulatory system.

Succeeding in a changing environment requires that OSFI have staff with a vast range of experience and a strong commitment to the achievement of our mandate. We are fortunate to have such resources. The high quality of Canada's system of prudential regulation and supervision is widely recognized by other countries. We benefit from strong relations with other governmental and regulatory organizations in Canada and with regulators in other countries. OSFI is an active participant in international forums to strengthen and harmonize prudential regulation of banks and insurance companies, as well as to help emerging market economies implement higher standards.

During the course of the past year, John R. V. Palmer retired as Superintendent. We owe him considerable thanks for directing the major accomplishments of OSFI over his seven-year term. We will continue to build on those successes.

Yours sincerely,



Nicholas Le Pan  
Superintendent

## □ Role and Responsibilities

**OSFI was established in 1987 by an Act of Parliament—the *Office of the Superintendent of Financial Institutions Act*.** OSFI supervises and regulates all banks in Canada, and all federally incorporated or registered trust and loan companies, insurance companies, cooperative credit associations, fraternal benefit societies and pension plans.

OSFI also provides actuarial advice to the Government of Canada and conducts reviews of certain provincially chartered financial institutions by virtue of federal-provincial arrangements or through agency agreements with the Canada Deposit Insurance Corporation (CDIC).

OSFI derives powers from and is responsible for administering the following legislation:

- *Bank Act*;
- *Trust and Loan Companies Act*;
- *Cooperative Credit Associations Act*;
- *Insurance Companies Act*;
- *Pension Benefits Standards Act, 1985*.

These Acts set out the rules for the structure and operation of federally regulated financial institutions and the standards for pension plans. The various Acts address the unique aspects of the sectors each governs, but are designed to be consistent with each other.

OSFI is comprised of the Supervision, Regulation, Specialist Support and Corporate Services Sectors, as well as the Office of the Chief Actuary, employing some 450 people in offices located in Ottawa, Montréal, Toronto and Vancouver.

OSFI is funded mainly through asset-based, premium-based or membership-based assessments on the financial services industry and a modified user-pay program for selected services. A small portion of OSFI's revenue is derived from the Government of Canada, primarily for actuarial services relating to the Canada Pension Plan, the Old Age Security Plan, the Canada Student Loan Program and various public-sector pension and benefit plans.



## □ Mandate and Objectives

**To accomplish its mission of safeguarding policyholders,** depositors and pension plan members from undue loss, OSFI advances and administers a regulatory framework that provides for the early identification and resolution of compliance or operational issues that could threaten the safety and soundness of financial institutions or affect public confidence in the financial

**...OSFI advances and administers a regulatory framework that provides for the early identification and resolution of compliance or operational issues that could threaten the safety and soundness of financial institutions...**

system. At the same time, OSFI recognizes the regulatory system must not unduly impede institutions from competing effectively. OSFI's employees are committed to delivering professional, high-quality and cost-effective performance.

OSFI has two objectives that are critical to achieving its mission:

**Safeguarding from Undue Loss** – We identify institution-specific risks and trends and intervene in a timely manner so as to minimize losses to policyholders, depositors and pension plan members.

**Public Confidence** – We contribute to public confidence by enhancing the safety and soundness of the Canadian financial system in a competitive environment. We evaluate system-wide risks and promote the adoption of sound business and financial practices

## □ Financial Institutions and Pension Plans Regulated by OSFI

	Number <sup>1</sup>	Assets <sup>2,3</sup> (Millions)
<b>Banks</b>		
Domestic	14	\$1,597,357
Foreign bank subsidiaries	33	\$77,508
Foreign bank branches	17	\$27,614
<b>Trust and Loan Companies</b>		
Bank-owned	36	\$187,853
Other	29	\$8,321
<b>Cooperative Credit Associations</b>	7	\$11,966
<b>Life Insurance Companies</b>		
Canadian-owned	44	\$318,117
Foreign branches	64	\$26,093
<b>Fraternal Benefit Societies</b>		
Canadian-owned	13	\$7,145
Foreign Branches	12	\$1,035
<b>Property and Casualty Insurance Companies</b>		
Canadian-incorporated	94	\$43,215
Foreign branches	104	\$18,679
<b>Pension Plans</b>	1,189	\$90,436

<sup>1</sup> Number of regulated companies as at 31 March 2002. Includes institutions in the process of liquidation or termination and institutions limited to servicing existing business. A list of institutions regulated by OSFI can be found on OSFI's Web site at [www.osfi-bsif.gc.ca/eng/whoweregulate.asp](http://www.osfi-bsif.gc.ca/eng/whoweregulate.asp). <sup>2</sup> As at 31 March 2002 where available, otherwise 31 December 2001. <sup>3</sup> Total assets of the industries regulated by OSFI are not the simple sum of the above-noted figures. The figures for entities that report on a consolidated basis include subsidiaries whose assets may also be included in a different category.



THE THEME OF THIS YEAR'S ANNUAL REPORT IS  
**SUCCEEDING IN A CHANGING ENVIRONMENT.**

THE PAGES THAT FOLLOW HIGHLIGHT SEVERAL ASPECTS  
OF THAT ENVIRONMENT OVER THE PAST  
YEAR AND OSFI'S RESPONSE TO THEM.

## □ New Regulatory Environment in Canada

**In June 2001, Parliament passed Bill C-8, which incorporated changes to the legislation governing federal financial institutions.** Among the more significant provisions of the bill were initiatives making it easier to establish financial institutions, including allowing small banks that may be closely held and reducing the minimum capital required for start-up. The bill also enhanced operational flexibility by facilitating financial institution holding company structures and significantly expanding investment powers. In addition, it streamlined the regulatory approvals process. OSFI fully supported the new legislative package and the public policy objective of increased competitiveness that underlies it.

During the course of the year under review, work was undertaken to adapt OSFI's existing approval and supervisory processes to the new legislation. We adjusted our approach in considering applications in order to recognize the shift in the government's policy direction toward more support for a competitive environment, while not neglecting safety and soundness considerations. There has been some interest expressed in the creation of small banks and OSFI has been dealing with several interested parties. One application to establish a small bank was finalized in the second quarter of the 2002-2003 fiscal year.

In this new environment, OSFI believes it is important to be more transparent about our approach. Therefore, concurrent with the passage of Bill C-8, OSFI posted new incorporation guidelines for banks, trust and loan companies, and insurance companies on the OSFI Web

### **Streamlining approvals is an important part of a competitive regulatory regime that keeps compliance costs in check.**

site. These guidelines provide comprehensive criteria and instructions to assist potential applicants interested in establishing new financial institutions. We also started to publish the results of selected legislative interpretations that could be of general interest.

Streamlining approvals is an important part of a competitive regulatory regime that keeps compliance costs in check. OSFI was in a position to implement a fully tested, streamlined approvals process as a result of a pilot project implemented before passage of Bill C-8. In addi-

tion, updated transaction information guides for approvals by the Superintendent were posted on the OSFI Web site to provide administrative guidance to applicants. Experience to date with streamlining is very positive, with the majority of approvals being granted within the 30-day timeframe. Exceptions occur when financial institutions are unable to provide necessary information on a timely basis, or when an approval is part of a larger transaction and not required within the 30-day timeframe.

Bill C-8 also created the Financial Consumer Agency of Canada (FCAC), which has a mandate to ensure that federally regulated financial institutions comply with federal consumer protection laws and regulations. When FCAC began operating in late October 2001, OSFI relinquished its role of tracking enquiries and complaints related to financial institutions, and now limits responses to matters concerned with federally administered pension plans and issues of safety and soundness in the federal financial services sector.

Aside from changes brought about by the passage of new legislation, OSFI worked to enhance the domestic regulatory environment through revisions to the capital standards for insurance companies and the introduction of OSFI's general allowances policy for deposit-taking institutions. OSFI also commenced a review of the role of the appointed actuary in insurance companies to determine if it continues to be appropriate in light of industry developments, such as the new focus on enterprise-wide risk management.

## □ Impact of September 11<sup>th</sup>

### SUPERVISION ACTIVITIES IN RESPONSE TO SEPTEMBER 11<sup>TH</sup>

**On September 11, 2001, the world watched in horror as the World Trade Center in New York and the Pentagon in Washington, D.C. were attacked.** OSFI's primary focus on September 11<sup>th</sup> and immediately thereafter was to work with financial institutions, other authorities such as the Bank of Canada and other regulators in Canada and elsewhere, to monitor and take necessary action to promote the stability of the financial system. This included focussing on clearing and settlement arrangements, trading programs, back-up and contingency plans, and exposures of financial institutions to potential losses.

Financial institutions did an excellent job in reacting to the events of September 11<sup>th</sup>. Although a number of Canadian institutions had operations that were directly affected by the World Trade Center attacks, their contingency plans operated well and there was relatively little disruption.

In addition to working with institutions to conduct a *post mortem* on the effectiveness of their contingency plans and lessons learned, OSFI reviewed its own contingency arrangements. These, too, worked well, and additional enhancements have been made to further refine our effectiveness.

Ongoing activities include assessing any longer-term implications of losses incurred by financial institutions and monitoring risk-sharing arrangements in the insurance industry, including the distribution of catastrophe risk resulting from post-September 11<sup>th</sup> changes in the insurance marketplace.

#### **TERRORIST FINANCING**

Immediately after September 11<sup>th</sup> many governments, including Canada's, gave immediate and significant priority to reducing the possibility that the financial system would be used to support further terrorist activities. In this regard, OSFI issued its first advisory on September 21<sup>st</sup>, calling on federally regulated financial institutions to review their records for names of suspected terrorists. On October 2, 2001, the Government of Canada brought into force the *United Nations Suppression of Terrorism Regulations* (UNSTR). Under UNSTR regulations, Canadian financial institutions are required to search for and freeze the assets of designated terrorists or terrorist groups, and report on such assets to their regulator and law enforcement and intelligence authorities. Also, amendments to the Criminal Code implemented as a result of anti-terrorism legislation require financial institutions to report to OSFI on an ongoing basis that they are not in the possession or control of the property of a listed entity.

OSFI played a major role in advising financial institutions of their obligations under the United Nations resolutions and Canadian regulations. In addition to aggregating monthly reports on frozen assets from federally regulated financial institutions, OSFI agreed to coordinate the aggregation of similar information from provincial authorities and self-regulatory organizations. As a result of this action, federal authorities can monitor the extent of terrorist funds identified in Canada.

During the implementation of the new regulations, OSFI worked closely with various Government of Canada agencies and departments on collaborative efforts such as the timely publication of terrorist names. By March 31, 2002, OSFI had begun to issue regular commu-

### **Financial institutions did an excellent job in reacting to the events of September 11<sup>th</sup>.**

niqués on changes made to the lists of terrorists to help Canadian financial institutions meet their reporting obligations. These were published via facsimile and OSFI's Web site.

OSFI also took steps to augment its resources and methodology to assess institutions' compliance with terrorist financing and anti-money laundering requirements.

#### **ANTI-MONEY LAUNDERING EFFORTS**

Money laundering continues to receive increasing attention as nations attempt to deal with issues such as organized crime.

The Bank for International Settlements and the International Association of Insurance Supervisors issued international standards for customer due diligence in the fight against money laundering. In response to these initiatives, OSFI issued revised guidance on money laundering in 2002.

It is clear that money laundering and terrorist financing pose potential risks to the reputation of financial institutions, both individually and collectively. Damage to a financial institution's reputation, if severe enough, can result in financial loss. OSFI is implementing a formal program of assessing federally regulated financial institutions' compliance with their reporting obligations, as well as their adherence to customer due diligence standards.

Cooperation among government agencies involved in terrorist financing and anti-money laundering efforts is important. Although OSFI does not act as an intermediary between

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regulated financial institutions and law enforcement agencies, the Office is ready to assist where it can be helpful. In that vein, OSFI has held discussions with the Financial Transactions and Reports Analysis Centre of Canada (FINTRAC), the agency responsible for collecting, analyzing and disclosing information to assist in the detection and prevention of money laundering and terrorist financing under the *Proceeds of Crime (Money Laundering) and Terrorist Financing Act*. Should enabling legislation be passed by Parliament, OSFI and FINTRAC will be able to share information related to financial institutions' compliance.

## □ International Environment

**Part of the changing environment is the increased role of international organizations in setting rules and guidance for financial institutions and in promoting international financial stability.** OSFI continued to devote considerable resources to international supervisory policy development and rule setting in 2001, as these areas grew in importance. OSFI participates most actively in those areas either judged to be of greatest importance to Canadian financial institutions, where we in Canada can lever off rules developed internationally or where we have particular expertise to share.

The Basel Committee on Banking Supervision (BCBS) is the prime body bringing together supervisors and regulators of international banks from G-10 countries. It has taken a leadership role over a number of years in rule setting. The BCBS focussed its recent efforts on developing a new capital adequacy accord, which will significantly modernize the current agreement put in place in 1987, and will better relate capital requirements to the risks assumed

by institutions. The BCBS now expects the new capital accord to be finalized in 2003 and fully implemented in 2006.

OSFI believes these developments are highly desirable and supports the work of the BCBS as a member of the main committee and through our participation in a number of subcommittees tasked with making recommendations on different aspects of the proposed accord. OSFI also chairs the newly created BCBS Accord Implementation Group, whose purpose is to provide supervisors in G-10 and other countries with the ability to share information, thereby promoting consistency in their approaches to implementation.

Considerable work was undertaken during the year with representatives of the Canadian banking industry to help OSFI understand the impact of BCBS proposals and assess industry readiness. In addition, OSFI was active in developing revised proposals for capital requirements in such areas as securitization, operational risk, equity exposures, small business and credit card lending. Because of the significant challenges to implementation of the Accord, during the year OSFI created and staffed a group charged with implementation and has commenced the planning phase of this project. In addition, OSFI has been active on the BCBS accounting and e-banking task forces.

The International Association of Insurance Supervisors (IAIS) has also been active in its evolving role as a standard-setter for life and general insurance supervision. Over the year, it adopted papers on capital adequacy and solvency, reinsurance, exchange of information, anti-money laundering and disclosure. OSFI plays an important role in the work of the IAIS. It participates as a member of the Executive and Technical Committees and the Accounting, Investment and Solvency (chair) Subcommittees. It also provides representation to the

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Working Group on the Future and Financing Structure of the IAIS and the Task Force on Revision to the Insurance Core Principles and Methodology. As well, OSFI follows the progress of other industry and regulatory groups and comments regularly on their draft papers.

The demand from emerging market economies for assistance in financial regulation and supervision is rising. In 2001, OSFI decided to make a more focussed effort to assist selected emerging market economies to enhance their supervisory systems. This commitment, consistent with the Government of Canada's priorities and those of other countries, represents a practical and effective means of contributing to international financial stability. In early 2002, OSFI's International Advisory Group became fully operational. The Group, which receives funding through the Canadian International Development Agency, provides technical assistance to supervisors in the Caribbean, Asia and Latin America, in the areas of bank and insurance company supervision and regulation.



In addition, OSFI continues to support the Toronto International Leadership Centre for Financial Sector Supervision through its roles on the Board of Directors, the Executive Committee, the Banking Program Advisory Board and, more recently, through the secondment of an OSFI employee. Founded in 1998, the Centre is unique. Individuals with substan-

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tial experience in financial supervision from Canada and abroad help supervisors from around the world to acquire the knowledge and leadership skills to build effective supervisory regimes in their countries.

OSFI also plays an important role in a number of other international groups, including the Financial Stability Forum (FSF), an organization founded by the G-7 Finance Ministers and Central Bank Governors following the 1998 financial crisis, to promote international financial stability through information exchange and international cooperation in financial supervision and surveillance. The FSF is made up of senior representatives from finance ministries, central banks and regulators of G-7 countries and those with significant financial sectors, as well as international financial institutions and financial sector standards-setting bodies. The FSF met in September 2002 in Toronto.

## □ Enhancing the Supervisory Framework

**In August 1999, OSFI implemented a new Supervisory Framework to assess the safety and soundness of federally regulated financial institutions,** and to enhance our ability to intervene on a timely basis where OSFI considers an institution's practices to be imprudent or unsafe, or in contravention of legislative and regulatory requirements.

OSFI's approach to supervision is risk based, focussing on an institution's activities that are likely to materially affect its risk profile. OSFI expects financial institutions to have adequate risk management practices and controls in place to appropriately mitigate risks taken on by the institutions. The supervisory process assesses the effectiveness of an institution's corporate governance and oversight processes in mitigating risks and, where possible, uses the work of the institution's independent oversight functions to enhance the efficiency of the supervisory process.

In 2002, OSFI introduced Assessment Criteria to guide supervisory judgements in assessing the safety and soundness of institutions. The Assessment Criteria were developed with input from the supervised industries through their industry associations, as well as from information gathered through a review of corporate governance and control practices at some 40 institutions of different types and sizes in Canada.

Beginning with the 2002-2003 supervisory cycle, OSFI will be providing institutions with their Composite Risk rating, which represents OSFI's assessment of the overall level of risk in the institution. This rating considers the risks inherent in the institution's activities, the effectiveness of its risk mitigation, and the quality and adequacy of its capital and earnings.

The Composite Risk rating is primarily based on findings and observations from OSFI's on-site reviews of an institution's operations, and from ongoing monitoring activities. Not only will the Assessment Criteria provide guidance to supervisors in their work, it will also assist institutions in understanding the basis of the assessment and the significance of the rating.

The Assessment Criteria, combined with the ratings, will bring increased standardization and transparency to the risk assessment process, thereby improving the consistency and comparability of our assessments across different institutions and industry sectors. The Framework and the Assessment Criteria together provide a leading edge supervisory process, which will continue to be enhanced and refined.

The Composite Risk rating will be provided to management and boards of directors of financial institutions. To avoid misinterpretation and/or inappropriate use of the ratings, institutions will be required to keep their rating confidential, pursuant to the *Supervisory Information Regulations*.

Significant attention was given during the year to enhancing OSFI's monitoring processes by introducing new analytical tools and bringing a more disciplined approach to the process. These increased monitoring efforts allow OSFI to focus more quickly on emerging issues and to intervene more effectively in higher risk situations. OSFI is also better able to determine the implications of significant events, such as economic downturns, volatile capital markets and political or other events, such as those that occurred on September 11, 2001.

**Beginning with the 2002-2003 supervisory cycle, OSFI will be providing institutions with their Composite Risk rating, which represents OSFI's assessment of the overall level of risk in the institution.**

As part of the normal supervisory response to deteriorating market conditions, OSFI focussed more supervisory resources during the year on reviewing credit quality and the adequacy of credit risk management processes. We also reviewed the effect of risk transfer through mechanisms such as special purpose entities and credit derivatives. As well, we monitored the integration activities resulting from a number of significant acquisitions during the year, and the impact of weak operating results in the property and casualty insurance industry.

Pursuant to its early intervention mandate, during the year OSFI took control of Reliance Insurance Company, a branch of a foreign property and casualty insurer, following takeover of

the parent company by U.S. regulatory authorities. OSFI had previously taken other supervisory actions to minimize losses to the policyholders of Reliance.

Similarly, it was necessary for the Superintendent to take control of Alta Surety Company, a small closely held fidelity and surety insurance company, which was in run-off at the time

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control was taken, in order to protect the remaining policyholders and creditors of the company. The company was placed in liquidation in July 2001.

## □ Recent Corporate Failures

**The issues raised by the failure of Enron Corporation and other high-profile companies in the United States are of interest to regulators around the globe.** Although Enron was not a regulated financial institution and, therefore, not subject to a comprehensive regulatory and supervisory regime, its problems have led to a closer analysis of certain financial practices and the quality of corporate governance and auditing practices.

During the year, and prior to the Enron disclosures, OSFI completed a multi-year review of Special Purpose Entities (SPEs) used by financial institutions in asset securitization. As part of its follow-up activities, OSFI undertook enquiries to determine whether any issues similar to those at Enron could be identified. Our enquiries indicated these vehicles were being used appropriately and that adequate controls were in place regarding their creation and for ongoing monitoring at financial institutions regulated by OSFI.

OSFI also continued to refine a draft guideline on corporate governance for financial institutions. The guideline will not duplicate existing guidance produced by other regulators, stock exchanges and similar bodies, but will set out OSFI's expectations for behaviours of boards of regulated financial institutions in areas such as oversight of risks and risk management and audit committee relations with auditors and actuaries.

Given the reliance-based framework under which financial institutions operate, as well as the importance of continued public confidence in financial statements, OSFI, along with representatives of the Canadian Securities Administrators and other interested parties, worked to create a new Canadian Public Accountability Board to oversee auditors of public companies in Canada. These initiatives, which were announced in August 2002, will subject auditing firms to more frequent and rigorous inspection.

OSFI's work with the actuarial profession to create an independent, effective peer review system also reached a satisfactory conclusion. By the end of 2002, the Canadian Institute of Actuaries is expected to formally adopt a standard of practice on peer review developed during the year. OSFI has announced that, under this standard, it will require peer review of all

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required reports prepared by Appointed Actuaries of federally regulated insurance companies. Reviews will begin in 2002 with companies having the option to have reviews performed on a three-year cycle.

## □ Office of the Chief Actuary

**The Office of the Chief Actuary (OCA) has responsibilities that are different from those of the other sectors within OSFI.** Rather than fulfilling a regulatory or supervisory function, OCA provides actuarial services for a variety of programs. These programs include the Canada Pension Plan, Old Age Security, and pension and benefits plans for the federal Public Service, the Canadian Forces, the Royal Canadian Mounted Police, federal judges and Members of Parliament. In 2001, OCA also began to provide actuarial services to the Canada Student Loans Program.

In addition to preparing statutory actuarial reports on the financial status of the plans, OCA provides the relevant government departments with actuarial advice on the design, funding and administration of these plans. OCA clients include Human Resources Development Canada, Finance, Treasury Board, Public Works and Government Services, National Defence, the RCMP and Justice Canada.

The 18<sup>th</sup> Actuarial Report on the Canada Pension Plan (CPP) was tabled in Parliament in December 2001, confirming the long-term viability and financial sustainability of the CPP.

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This Report confirms that the 9.9 per cent combined employer-employee contribution rate, which will be reached in 2003, is expected to be sufficient to sustain the Plan indefinitely as larger numbers of Canadians reach retirement age. In March 2002, a panel of three experienced, independent actuaries completed a formal review of the 18<sup>th</sup> CPP report; OCA will work actively on the recommendations flowing from this review.

The Canadian Institute of Chartered Accountants now requires each government to recognize a liability and an expense in its financial statements for post-employment benefits that vest or accumulate as its employees render their services. OCA has prepared actuarial reports for the Government of Canada to estimate the liabilities for these benefits under the new rules.

In addition, during the year under review, OCA completed the first actuarial report on the Canada Student Loans Program as well as actuarial reports on a number of other government or government-sponsored pension plans. It also provided ongoing advice and support to the Public Sector Pension Investment Board and the Pension Advisory Committees of the Public Service, the Canadian Forces and the RCMP, each of which provides advice to the relevant Minister on the design, administration and funding of their respective plans.



## PRIORITIES GOING FORWARD

For the upcoming period, the Office has identified several major priorities. These include continually enhancing our ability to deal with more and more complex problem financial institutions situations, focussing on what matters, and continuing to have the resources necessary to meet our mandate.

- **Achieving success in these strategies** involves continually enhancing our capacity to effectively identify risks faced by federally regulated financial institutions and pension plans and promoting improved management of those risks, improved readiness to deal with problems consistent with our early intervention mandate and taking action so that our framework of guidance and rules remains relevant and meets or exceeds international minimums.
- **Ongoing, effective and innovative management** of OSFI's human and knowledge resources is also key to our success. OSFI has put a considerable focus in recent years on human resources initiatives, including the use of performance pay, development of competencies, enhanced focus on fair pay and performance evaluation and better recruiting practices. These will continue.
- **OSFI needs to make a better effort to use technology** and information management systems (IM/IT) more effectively. OSFI's efficiency and effectiveness can benefit from business process improvements that IM/IT investments facilitate. These investments can also reduce the compliance costs of regulation to financial institutions and pension plans. This will be a key priority for further enhancements.

## FINANCIAL STATEMENTS

### □ Financial Highlights for 2001-2002

#### IMPROVEMENTS TO FINANCIAL REPORTING

**Fiscal year 2001-2002 represents OSFI's second complete year of reporting its results of operations using full accrual accounting.** As a result, readers of the 2001-2002 financial statements can make comparisons with the previous year.

This year, for the first time, OSFI has prepared its Financial Statements by business line (Supervision of Financial Institutions, Supervision of Pension Plans and the operations of the Office of the Chief Actuary). This presentation shows how each business line contributes to OSFI's net results of operations.

#### NET RESULTS OF OPERATIONS

Supervision activities are funded primarily by the institutions OSFI regulates and revenue is matched to OSFI's costs of supervision. Some of OSFI's costs are funded by specific user-pay charges, which serve to reduce general industry assessments. These cover fees for transactions and, starting this year, surcharges for problem institutions. The Office of the Chief Actuary is funded from a combination of fees charged for actuarial services and parliamentary appropriations to cover actuarial services provided to the Government of Canada. OSFI completed the fiscal year 2001-2002 with a small net loss from operations. The loss is the result of timing differences between government funding and the recognition of expenses by the Office of the Chief Actuary.

#### EXPENSES

Total expenditures were \$64 million for the year ended March 31, 2002. Of this total, approximately \$57 million was accounted for by the program of supervision of federally regulated financial institutions, \$3.4 million by supervision of pension plans and \$3.8 million by the Office of the Chief Actuary. The expenses of the financial institution supervision program increased in total by some \$10.1 million from the previous year. Significant human resource

cost increases in 2001-2002 arose from growth in the number of employees at OSFI and adjustments to employee compensation to more closely reflect market levels. These cost factors are part of a strategy to ensure OSFI attracts and retains the people it needs, with the requisite range of experience and skills to meet its mandate.

During the year, OSFI increased the size of the conglomerate supervision groups and moved closer to full staffing of the specialist support sector. OSFI also allocated additional money to its performance pay regime. Expenses for the supervision of private pension plans were lower than in the previous year, primarily because of efficiencies achieved in this area.

In the Office of the Chief Actuary, the increase in expenses reflects additional functions assumed, including the valuation made in support of the government's student loan program.

#### REVENUE

During 2001-2002, assessment revenue from federally regulated financial institutions approached \$54 million, an increase of almost \$10 million from the previous year. However, user-pay revenue was lower than expected. This was due to fewer transactions than anticipated and changes in legislation and regulations that reduced the number of transactions requiring approval.

OSFI assessments are differentiated by industry, reflecting the costs incurred by each industry group. The chart below sets out the revenue and user-pay assessments by sector and for federally regulated pension plans. As shown below, the Banks, Trust and Loan industry experienced the largest increase in assessments, although assessments to the larger banks and insurance companies remained in the \$2-3 million range per institution. The smallest increase was experienced by the Property and Casualty Insurance industry. Indeed, a number of institutions, including many in the Property and Casualty Insurance sector, paid the minimum assessment of \$10,000.

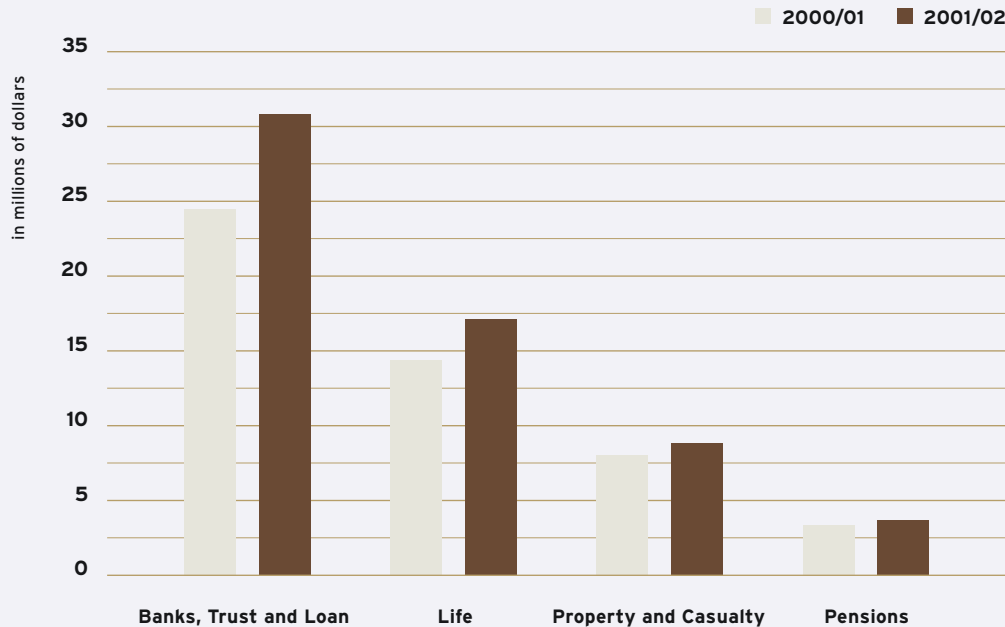
Revenue assessed from OSFI-regulated private pension plans matched expenses of \$3.4 million.

Revenues for the Office of the Chief Actuary in 2001-2002 were \$3.7 million, an increase of \$0.4 million over the previous fiscal year. These revenues comprised:

- 1) \$2.8 million in service charges for actuarial services to the federal government and various federal government agencies for the Canada Pension Plan, Old Age Security, Canada Student Loans Program and pension plans for employees of the federal government and various agencies.
- 2) \$0.9 million in parliamentary appropriations related to actuarial services for the pension plans for Members of Parliament and federal judges, and for the federal employees' insurance plans.



**BREAKDOWN OF REVENUE BY INDUSTRY**



Note 1: Revenue = assessments of federally regulated financial institutions and pension plans + user pay, including Memoranda of Understanding + appropriations from the Federal Government. Note 2: In addition to revenues from industry shown on the chart, there were revenues from Government and miscellaneous sources of \$5 million in both fiscal years.

**FINANCIAL PLANS FOR FUTURE YEARS**

In future years, OSFI will continue to strive to control its general operating cost increases while selectively increasing resources where necessary to meet our mandate. To achieve this, OSFI will limit staff growth by focussing on opportunities to further improve operational efficiency. OSFI has planned a significant investment in technology over the next three years. To maximize the benefits of this investment, we will review business processes with a view to identifying possibilities for streamlining that can be achieved through enabling technology. OSFI has offered to work with its stakeholders to ensure this investment results in efficiencies for them as well, for example, by reducing the costs of complying with OSFI data collection requirements.

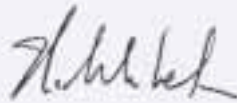
OSFI will continue to make progress on having a material amount of its costs recovered by means of charges to specific users, rather than through base assessments. OSFI will review existing user-pay charges and increase the use of Memoranda of Understanding to bill specific financial institutions for the costs associated with approving larger transactions or providing interpretations on capital instruments.

## □ Management's Responsibility for the Financial Statements

Responsibility for the integrity and objectivity of the accompanying financial statements and the consistency with all other information contained in this annual report rests with OSFI management.

These financial statements, which include amounts based on management's best estimates as determined through experience and judgement, have been prepared in accordance with Canadian generally accepted accounting principles. Management has developed and maintained books of accounts, records, internal controls, management practices, and information systems designed to provide reasonable assurance that the assets are safeguarded and controlled, resources are managed economically and efficiently in the attainment of corporate objectives, and that transactions are in accordance with the *Financial Administration Act* and regulations as well as OSFI policies and statutory requirements.

The Auditor General of Canada, the independent auditor for the Government of Canada, has audited the transactions and financial statements of OSFI, and reports on her audit to the Minister of Finance.



Nicholas Le Pan  
Superintendent



Donna Pasteris  
Assistant Superintendent  
Corporate Services

Ottawa, Canada  
May 24, 2002



AUDITOR GENERAL OF CANADA

VÉRIFICATEUR GÉNÉRAL DU CANADA

## AUDITOR'S REPORT

To the Minister of Finance

I have audited the statement of financial position of the Office of the Superintendent of Financial Institutions as at 31 March 2002 and the statements of operations and equity of Canada and cash flows for the year then ended. These financial statements are the responsibility of the Office's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with Canadian generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In my opinion, these financial statements present fairly, in all material respects, the financial position of the Office as at 31 March 2002 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

A handwritten signature in black ink, appearing to read 'John Wiersema'.

John Wiersema, CA  
Assistant Auditor General  
for the Auditor General of Canada

Ottawa, Canada  
24 May, 2002

## □ Statement of Financial Position

*As at March 31*

	2002	2001
<b>ASSETS</b>		
<b>Assets</b>		
Cash Entitlement	\$ 34,722,099	\$ 37,578,910
Accounts Receivable	1,260,864	304,324
Accrued Base Assessments	4,777,922	608,155
Capital Assets (note 4)	5,349,082	3,649,700
<b>Total Assets</b>	<b>\$ 46,109,967</b>	<b>\$ 42,141,089</b>
<b>LIABILITIES AND EQUITY OF CANADA</b>		
<b>Liabilities</b>		
Accounts Payable & Accrued Liabilities	\$ 2,456,561	\$ 4,114,362
Accrued Salaries and Benefits	8,306,154	3,830,235
Deferred Charges	1,534,604	282,866
Deferred Private Pension Plan Revenue	933,193	1,039,934
Employee Future Benefits other than pension (note 9)	5,341,842	5,284,723
	<b>18,572,354</b>	<b>14,552,120</b>
<b>Equity of Canada</b>	<b>27,537,613</b>	<b>27,588,969</b>
<b>TOTAL LIABILITIES &amp; EQUITY OF CANADA</b>	<b>\$ 46,109,967</b>	<b>\$ 42,141,089</b>

Commitments and Contingencies (note 6)



Nicholas Le Pan  
Superintendent of Financial Institutions

The accompanying notes are an integral part of the financial statements.

## □ Statement of Operations and Equity of Canada

*For the year ended March 31*

	2002	2001
<b>SUPERVISION OF FEDERALLY REGULATED FINANCIAL INSTITUTIONS</b>		
<b>Revenue</b>		
Base Assessments	\$ 53,577,359	\$ 43,257,461
User Fees and Charges	3,070,006	3,281,852
Cost Recovered Services	534,685	851,733
<b>Total Revenues</b>	<b>57,182,050</b>	<b>47,391,046</b>
<b>Expenses (note 10)</b>		
Supervision & Regulation	56,647,365	46,539,313
Cost Recovered Services	534,685	1,251,733
<b>Total Expenses</b>	<b>57,182,050</b>	<b>47,791,046</b>
<b>Net Results</b>	<b>–</b>	<b>(400,000)</b>
<b>SUPERVISION OF PRIVATE PENSION PLANS</b>		
Revenue	3,438,563	3,765,180
Expenses (note 10)	3,438,563	3,765,180
<b>Net Results</b>	<b>–</b>	<b>–</b>
<b>OFFICE OF THE CHIEF ACTUARY OF CANADA</b>		
Revenue	2,804,500	1,146,026
Expenses (note 10)	3,772,356	3,116,565
<b>Net Results</b>	<b>(967,856)</b>	<b>(1,970,539)</b>
<b>Net Results of Operations before Government Funding</b>	<b>(967,856)</b>	<b>(2,370,539)</b>
Government Funding (note 5)	916,500	2,173,106
<b>NET RESULTS OF OPERATIONS FOR THE YEAR</b>	<b>(51,356)</b>	<b>(197,433)</b>
<b>EQUITY OF CANADA, BEGINNING OF YEAR</b>	<b>27,588,969</b>	<b>27,786,402</b>
<b>EQUITY OF CANADA, END OF YEAR</b>	<b>\$ 27,537,613</b>	<b>\$ 27,588,969</b>

The accompanying notes are an integral part of the financial statements.

## □ Statement of Cash Flows

*For the year ended March 31*

	2002	2001
<b>OPERATING ACTIVITIES</b>		
<b>Net Results of Operations</b>	<b>\$ (51,356)</b>	<b>\$ (197,433)</b>
<b>Non-Cash items included in operations</b>		
Amortization of Capital Assets	1,760,267	1,363,641
Employee Related Liabilities	4,533,038	611,468
Gain on Disposal of Capital Assets	(9,248)	-
<b>Change in Assets/Liabilities</b>		
(Increase)/Decrease in Accounts Receivable	(956,540)	12,830,847
(Increase) in Accrued Base Assessments	(4,169,767)	(5,163,666)
Increase/(Decrease) in Accounts Payable and Accrued Liabilities	(1,657,801)	1,480,875
Increase in Deferred Charges	1,251,738	-
Increase/(Decrease) in Deferred Private Pension Plan Revenue	(106,741)	525,934
<b>Cash Provided by Operating Activities</b>	<b>593,590</b>	<b>11,451,666</b>
<b>INVESTING ACTIVITIES</b>		
Acquisition of Capital Assets	(3,459,649)	(1,908,735)
Proceeds of Disposal of Capital Assets	9,248	-
<b>Cash Applied to Investing Activities</b>	<b>(3,450,401)</b>	<b>(1,908,735)</b>
<b>INCREASE/(DECREASE) IN CASH ENTITLEMENT</b>	<b>(2,856,811)</b>	<b>9,542,931</b>
<b>CASH ENTITLEMENT, BEGINNING OF YEAR</b>	<b>37,578,910</b>	<b>28,035,979</b>
<b>CASH ENTITLEMENT, END OF YEAR</b>	<b>\$ 34,722,099</b>	<b>\$ 37,578,910</b>

The accompanying notes are an integral part of the financial statements.

## Notes to the Financial Statements, for the year ended March 31, 2002

### 1. AUTHORITY AND OBJECTIVE

i) The Office of the Superintendent of Financial Institutions (“OSFI”) was established by the *Office of the Superintendent of Financial Institutions Act* (“OSFI Act”) in 1987 to regulate and supervise all federally regulated financial institutions. For OSFI, a federally regulated financial institution is any entity that has been created or is allowed to offer financial services pursuant to one of the financial institution statutes promulgated by the federal government and includes banks, trust and loan companies, federally registered insurance companies, cooperative credit associations, fraternal benefit societies and pension plans. Pursuant to the *Financial Administration Act* (“FAA”), OSFI is a department of the Government of Canada for the purposes of that Act and is listed in schedule I.1 of the Act.

ii) The Office of the Chief Actuary (“OCA”), a division of OSFI, provides actuarial advice to the Government of Canada. The OCA performs actuarial services for a variety of public insurance and pension programs as required under the *Canada Pension Plan* and the *Public Pensions Reporting Act*.

iii) In addition, OSFI has responsibilities under the following legislation:

- Bank Act*;
- Cooperative Credit Associations Act*;
- Green Shield Canada Act*;
- Insurance Companies Act*;
- Trust and Loan Companies Act*; and
- Pension Benefits Standards Act, 1985*.

iv) Under previous provisions of the *Insurance Companies Act* and the *Winding-Up Act*, OSFI acted as liquidator of failed insurance companies when appointed by Court Order. Under these circumstances, the Superintendent hired agents to carry out the liquidation work in each case. However, under the new provisions of the *Winding-Up and Restructuring Act* (Section 23.3), the Superintendent can no longer be appointed as liquidator of a failed institution.

### 2. SPENDING AND BORROWING AUTHORITY

Pursuant to section 17 of the OSFI Act, the Minister of Finance may spend any revenues collected under sections 23 and 23.1 of the OSFI Act to defray the expenses associated with the

operation of OSFI. The Act also establishes a ceiling for the expenses and sets this ceiling at \$40,000,000 above the amount of revenue collected.

OSFI revenues comprise assessments, fees, and service charges. The expenses against which assessments may be charged include those in connection with the administration of the *Bank Act*, the *Cooperative Credit Associations Act*, the *Green Shield Canada Act*, the *Insurance Companies Act*, and the *Trust and Loan Companies Act*. The formula for the calculation of assessments is included in regulations.

The *Pension Benefits Standards Act, 1985* (“PBSA, 1985”) provides that fees may be charged for the registration and supervision of pension plans and for the supervision, including inspection, of registered pension plans. The amount of the fees is set annually by regulation pursuant to section 25 of the PBSA, 1985.

Section 23.1 of the OSFI Act provides that the Superintendent may assess against a person a prescribed charge (“service charge”) and applicable disbursements for any service provided by or on behalf of the Superintendent for the person's benefit or the benefit of a group of persons of which the person is a member. “Person” includes individuals, corporations, funds, unincorporated associations, Her Majesty in Right of Canada or of a province, and a foreign government. The service charges are detailed in the regulations.

Pursuant to section 16 of the OSFI Act, Parliament annually provides appropriations to support the operations of the Office of the Chief Actuary.

### 3. SIGNIFICANT ACCOUNTING POLICIES

#### a) Basis of Presentation

The financial statements of OSFI have been prepared in accordance with Canadian generally accepted accounting principles.

#### b) Revenue Recognition

Revenue is recorded in the accounting period in which it is earned whether or not it has been billed or collected.

OSFI charges interim base assessments calculated on its budgeted expenditures and forecast industry results. Final base assessments are billed in the subsequent fiscal year, calculated on the actual results from the prior year.

Pension plan fee rates are set annually based on budgeted expenditures, forecast pension plan membership and actual results from the previous year.

User fees and charges include revenues earned pursuant to *Service Charges Regulations* and surcharges assessed against federally regulated financial institutions assigned a “stage” rating pursuant to the *Guide to Intervention for Federal Financial Institutions*.

Cost recovered services are provided based on terms outlined in Memoranda of Understanding and preliminary billings are based on settlement estimates.



### c) Cash Entitlement

OSFI does not have its own bank account. The financial transactions of OSFI are processed through the Consolidated Revenue Fund (CRF) of Canada. OSFI's cash entitlement represents the amount the Office is entitled to withdraw from the CRF without further authority. This amount does not earn interest.

### d) Capital Assets

Capital assets are recorded at historical cost less accumulated amortization. Amortization is recorded using the straight-line method over the estimated useful lives of the assets as follows:

Assets	Useful life
Leasehold Improvements	Remaining life of the lease
Furniture and Fixtures	7 years
Office Equipment	4 years
Informatics Hardware	3 years
Informatics Infrastructure (Networks)	3 years
Informatics Software	5 years
Motor Vehicles	5 years

### e) Employee Future Benefits

**(i) Pension Benefits:** OSFI's eligible employees participate in the Public Service Superannuation Plan administered by the Government of Canada. Both the employees and OSFI contribute to the cost of the Plan. This amount is currently based on a multiple of the employee's required contributions, and may change over time depending on the experience of the Plan. These contributions represent the total pension obligations of OSFI and are charged to operations on a current basis. OSFI is not required under present legislation to make contributions with respect to any actuarial deficiencies of the Public Service Superannuation Plan.

**(ii) Severance Benefits:** On termination of employment, employees are entitled to certain benefits provided for under their conditions of employment through a severance benefits plan. The cost of these benefits is actuarially determined and is accrued as the employees render their services necessary to earn severance benefits.

The cost of the benefits is actuarially determined using the projected benefit method prorated on services. The valuation of the liability is based upon a current market discount rate and other actuarial assumptions which represent management's best long-term estimates of factors such as future wage increases and employee resignation rates.

#### f) Specified Purpose Account

OSFI has an interest-bearing specified purpose account within the Consolidated Revenue Fund for insurance company liquidations. Previous to recent amendments to the *Insurance Companies Act*, the courts appointed the Superintendent as the liquidator of several failed insurance companies. In this capacity, OSFI pays, on behalf of the remaining active institutions, all expenses related to the liquidation, and then recovers these costs from active institutions. The revenues and expenses related to these accounts are not included in the OSFI Statement of Operations and Equity of Canada.

#### g) Use of Estimates

These financial statements are prepared in conformity with Canadian generally accepted accounting principles, which require that OSFI management make estimates and assumptions that affect the amounts reported in these financial statements. Human resources related liabilities and the useful lives of capital assets are the most significant items for which estimates are used. Actual results could differ from those estimates.

#### 4. CAPITAL ASSETS

<b>Cost</b>	<b>March 31, 2001</b>	<b>Additions</b>	<b>Disposals</b>	<b>March 31, 2002</b>
Leasehold Improvements	\$ 724,879	\$ 748,373	\$	\$ 1,473,252
Furniture and Fixtures	1,412,754	117,230		1,529,984
Office Equipment	204,238	114,348		318,586
Informatics Hardware	1,300,210	132,317		1,432,527
Informatics Infrastructure	978,982	777,797		1,756,779
Informatics Software	3,342,731	1,569,584		4,912,315
Motor Vehicle	21,757		21,757	
	\$7,985,551	\$3,459,649	\$ 21,757	\$11,423,443
<b>Accumulated amortization</b>	<b>March 31, 2001</b>	<b>Amortization</b>	<b>Disposals</b>	<b>March 31, 2002</b>
Leasehold Improvements	\$ 232,865	\$ 262,964	\$	\$ 495,829
Furniture and Fixtures	443,561	210,195		653,756
Office Equipment	66,310	65,352		131,662
Informatics Hardware	701,426	348,199		1,049,625
Informatics Infrastructure	512,263	385,132		897,395
Informatics Software	2,357,669	488,425		2,846,094
Motor Vehicle	21,757		21,757	
	\$4,335,851	\$1,760,267	\$ 21,757	\$ 6,074,361
Net Book Value	\$3,649,700			\$ 5,349,082

## 5. GOVERNMENT FUNDING

OSFI receives an annual parliamentary appropriation pursuant to section 16 of the OSFI Act to support its mandate relating to the Office of the Chief Actuary. In this fiscal year, OSFI was granted \$916,500 (2001: \$2,173,106) in parliamentary appropriations to defray the expenses associated with the provision of service by the Office of the Chief Actuary. The 2001 figure included \$400,000 to help OSFI defray the cost of implementing the Government's Financial Information Strategy.

## 6. COMMITMENTS AND CONTINGENCIES

### a) Commitments

OSFI has entered into lease agreements for office space and office equipment in four locations across Canada. The minimum aggregate annual payments for future fiscal years are as follows:

2002-2003	\$ 4,041,548
2003-2004	3,764,347
2004-2005	348,335
2005-2006	90,343
2006-2007	22,586
	\$ 8,267,159

### b) Contingencies

OSFI is involved in claims and litigation for which provisions have been made to the extent determinable.

## 7. SPECIFIED PURPOSE ACCOUNT

During the year, the following activity occurred in this account:

### SPECIFIED PURPOSE ACCOUNT: INSURANCE COMPANY LIQUIDATIONS

	2002	2001
Opening Balance	\$ 6,712,292	\$ 88,147
Recoveries deposited	53,475	6,521,745
Interest earned	161,223	102,400
Distribution of assets from liquidated estates	(6,633,788)	-
Net disbursements in respect of liquidation expenses	(338,414)	-
Closing Balance	\$ (45,212)	\$ 6,712,292

Remaining active insurance companies are liable for all expenses related to the liquidation of failed insurance companies.

## 8. RELATED PARTY TRANSACTIONS

OSFI is related in terms of common ownership to all Government of Canada departments, agencies and Crown corporations. OSFI enters into transactions with these entities in the normal course of business and on normal trade terms.

OSFI recorded expenses of \$14,781,443 (2001: \$12,717,066) and revenues of \$6,660,558 (2001: \$3,008,329) from transactions in the normal course of business with other Government departments during the year.

As at March 31, accounts receivable and payable with other Government entities and unrelated external parties were as follows:

	Related Parties	External Parties	Total
<b>2002</b>			
Accounts Receivable	\$ 9,252	\$ 1,251,612	\$ 1,260,864
Accounts Payable	\$ 39,345	\$ 2,417,216	\$ 2,456,561
<b>2001</b>			
Accounts Receivable	\$ 65,928	\$ 238,396	\$ 304,324
Accounts Payable	\$ 610,077	\$ 3,504,285	\$ 4,114,362

## 9. EMPLOYEE FUTURE BENEFITS

### (i) Pension Benefits

The estimated contributions to the Public Service Superannuation Plan during the year were as follows:

	2002	2001
Employer	\$ 4,552,442	\$ 3,346,127
Employees	\$ 1,799,641	\$ 1,621,849

### (ii) Severance Benefits

The net expense for OSFI's severance benefits for the year ended March 31, 2002 was \$389,851.

The cost of benefits is actuarially determined using the projected benefit method prorated on services. The accrued benefit liability recognized in the balance sheet at March 31, 2002 in respect of these benefits is \$5,341,842.

The significant actuarial assumptions adopted in measuring OSFI's accrued benefit liability were as follows: a) liability discount rate of 5.95%; b) general economic increases of 3.00%

**10. EXPENSES BY MAJOR CLASSIFICATION**

	<b>2002</b>	<b>2001</b>
Human Resources	\$ 48,853,100	\$ 40,184,752
Professional Development	1,537,127	1,387,028
Travel	2,281,082	2,152,101
Professional Services	1,297,863	1,001,073
Facilities	4,878,084	4,391,595
Information Management/Technology	3,143,854	3,148,832
Administration	2,401,859	2,407,410
Total Expenses	\$ 64,392,969	\$ 54,672,791

**11. COMPARATIVE FIGURES**

Certain 2001 comparative figures have been reclassified to conform to the presentation adopted in 2002.

## □ Appendix 1 – Complaints and Enquiries

**This will be the last annual report in which OSFI reports on complaints and enquiries from consumers of financial institutions.** This responsibility was assumed by the new Financial Consumer Agency of Canada (FCAC), which was created with the proclamation of Bill C-8. Since it began its public operations on October 24, 2001, FCAC has been enforcing the consumer-oriented provisions of the newly expanded federal financial institution statutes.

OSFI's toll-free telephone service remained the most popular method for consumers to contact us; however, we also received complaints and enquiries through the mail and via the Internet. As indicated in the following tables, from April 1 through October 23, 2001, OSFI received 6,357 enquiries and 2,244 complaints, for a combined total of 8,601 contacts. These figures are slightly lower than those recorded for the corresponding period in the preceding year, when the number of enquiries and complaints reached 6,678 and 2,651 respectively, for a combined total of 9,329.

For the period October 24, 2001, through March 31, 2002, OSFI recorded an additional 4,618 contacts, bringing the grand total for the fiscal year to 13,219, down from 16,568 for the 2000-2001 fiscal year.

The following tables provide statistics for the period April 1 through October 23, 2001. Interested readers should turn to the Annual Report of the FCAC to view their figures for the balance of the fiscal year.

**OSFI ENQUIRIES AND COMPLAINTS TRACKING REPORT - SECTOR SUMMARY***For the period of 01/04/2001 to 23/10/2001*

	Banks	Trust	Life	P&C	Pensions	Loan	Co-op.	Others	TOTAL
<b>Complaints</b>									
ABMs	26	0	0	0	0	0	0	3	29
Accounts	363	14	1	0	0	0	0	21	399
Cost of Borrowing	3	0	0	0	0	0	0	1	4
Credit Cards	226	16	0	1	0	0	0	11	254
Estate Issues	6	3	0	0	0	0	0	0	9
Financial Status	2	0	3	0	0	0	0	0	5
Floating Issues	17	0	0	0	50	0	0	0	67
General Information	12	0	0	1	7	0	0	8	28
Insurance Policies	3	0	61	48	0	0	0	31	143
Investment Products	94	21	7	0	4	0	0	5	131
Legislation/Regulations/Guidelines	6	1	1	1	18	0	0	2	29
Loans/Mortgages	220	13	3	1	0	2	2	7	248
Non-OSFI Related Issues	30	2	1	1	0	0	0	57	91
OSFI Related Issues	1	0	3	0	2	0	0	4	10
Privacy Issues	15	0	0	0	0	0	0	2	17
Quality of Service/Internal Policies	489	29	17	3	8	1	1	61	609
Service Fees/Charges	153	5	0	0	0	1	0	2	161
Small Business Issues	9	0	0	0	0	0	0	0	9
Tied Selling Issues	1	0	0	0	0	0	0	0	1
<b>TOTAL COMPLAINTS</b>	<b>1,676</b>	<b>104</b>	<b>97</b>	<b>56</b>	<b>89</b>	<b>4</b>	<b>3</b>	<b>215</b>	<b>2,244</b>

## OSFI ENQUIRIES AND COMPLAINTS TRACKING REPORT - SECTOR SUMMARY

*For the period of 01/04/2001 to 23/10/2001*

	Banks	Trust	Life	P&C	Pensions	Loan	Co-op.	Others	TOTAL
<b>Enquiries</b>									
ABMs	8	0	0	0	1	0	0	1	10
Accounts	95	6	0	0	0	0	0	7	108
Cost of Borrowing	0	0	0	0	0	0	0	1	1
Credit Cards	46	8	0	0	0	0	0	4	58
Estate Issues	5	1	0	0	0	0	0	1	7
Financial Status	68	16	17	4	0	1	0	18	124
Floating Issues	10	0	1	0	201	0	0	138	350
General Information	569	106	100	59	433	11	1	477	1,756
Insurance Policies	1	0	46	11	1	0	0	37	96
Investment Products	52	5	2	0	79	0	0	15	153
Legislation/Regulations/Guidelines	174	14	14	4	214	1	0	193	614
Loans/Mortgages	33	1	3	0	0	1	0	6	44
Non-OSFI Related Issues	40	7	7	9	27	0	0	2,599	2,689
OSFI Related Issues	47	13	10	10	13	2	0	150	245
Privacy Issues	7	0	0	0	0	0	0	1	8
Quality of Service/Internal Policies	52	2	3	2	2	0	0	4	65
Service Fees/Charges	16	0	0	0	0	0	0	3	19
Small Business Issues	0	0	0	0	0	0	0	2	2
Terrorists	0	0	0	0	0	0	0	0	0
Tied Selling Issues	4	0	0	0	0	0	0	4	8
<b>TOTAL ENQUIRIES</b>	<b>1,227</b>	<b>179</b>	<b>203</b>	<b>99</b>	<b>971</b>	<b>16</b>	<b>1</b>	<b>3,661</b>	<b>6,357</b>



**OSFI ENQUIRIES AND COMPLAINTS TRACKING REPORT - SECTOR SUMMARY***For the period of 01/04/2001 to 23/10/2001*

	Banks	Trust	Life	P&C	Pensions	Loan	Co-op.	Other	TOTAL
<b>TOTAL</b>	<b>2,903</b>	<b>283</b>	<b>300</b>	<b>155</b>	<b>1,060</b>	<b>20</b>	<b>4</b>	<b>3,876</b>	<b>8,601</b>

**TRACKING REQUESTS BY REQUEST TYPE***For the period of 01/04/2001 to 23/10/2001*

Written	342
Telephone	7,647
Personal Interview	13
Internet	599
<b>TOTAL</b>	<b>8,601</b>

## □ Appendix 2 – Disclosure of Information

**Under the OSFI Act**, the Superintendent is required to report to Parliament each year on the disclosure of information by financial institutions and the state of progress in enhancing the disclosure of information in the financial services industry.

**OSFI'S ROLE IN ENHANCING DISCLOSURE**

OSFI contributes to and promotes effective disclosure by: publishing selected financial regulatory information on the OSFI Web site and through *Beyond 20/20* (formerly *Ivation Datasystems Inc.*), providing guidance to institutions on their disclosure, and being a member of international supervisory groups with similar objectives.

During the year under review, OSFI increased the volume and frequency of information published on its Web site.

OSFI published its Property and Casualty insurance disclosure guideline for implementation at December 31, 2001. Similar to 1997 guidelines for deposit-takers and life insurers, this guidance sets out requirements for financial, risk management and control practices information that supplements disclosures required under Canadian generally accepted accounting principles and other OSFI guidelines.

Demutualization of several large life insurers in 1999-2000 has increased the need for market understanding and the application of market discipline. Following a successful educational seminar for analysts in late 2000, OSFI and the Canadian Institute of Actuaries are now developing a model for disclosure of annual gains and losses by source. Embedded value disclosure is already a reporting feature of several large Canadian life insurers.

Internationally, OSFI participates in the Transparency Group of the Basel Committee on Banking Supervision and maintains a watching brief on the work of the Task Force on Enhanced Disclosure of the International Association of Insurance Supervisors. Both of these groups focus on promoting market discipline through such means as developing best-practice disclosure guidance. In addition, the Basel Committee's Transparency Group has conducted regular surveys of the annual report disclosures of large, internationally active banks and is participating in an International Accounting Standards Board improvements project on financial activities disclosures.

Finally, OSFI is monitoring closely the resolution of disclosure issues raised by the failure of Enron to assess the extent to which these are satisfactorily addressed, either through changes to generally accepted accounting principles or through additional regulatory guidance where appropriate. This work is being undertaken in coordination with provincial governments, other federal departments and industry.

## □ Consumer Information

### COMPLAINTS AND ENQUIRIES

**Consumers with questions or complaints** relating to federally regulated financial institutions can contact the new Financial Consumer Agency of Canada (FCAC), which started its public operations on October 24, 2001.

FCAC ensures that consumers, in their day-to-day dealings with federally regulated financial institutions, fully benefit from the consumer protection measures the government provides for in legislation. The agency has the authority to impose penalties on financial institutions for non-compliance with these measures. FCAC also monitors and reports on industry self-regulatory initiatives.

FCAC can be reached through its toll-free telephone service at 1-866-461-FCAC (3222). More information about FCAC can be obtained by visiting its Web site at [www.fcac-acfc.gc.ca](http://www.fcac-acfc.gc.ca).



## OFFICE OF THE SUPERINTENDENT OF FINANCIAL INSTITUTIONS

OSFI welcomes questions about its role and responsibilities as well as enquiries related to federally regulated pension plans.

Several methods are available to communicate with us:

**Toll-free Information Service:** OSFI operates a toll-free information service from 8:30 a.m. to 5:00 p.m., Eastern Time, Monday through Friday. It can be reached by calling 1-800-385-8647 or (613) 990-6011 for local (Ottawa/Gatineau) calls.

**Internet:** OSFI's Web site address is [www.osfi-bsif.gc.ca](http://www.osfi-bsif.gc.ca). The site provides timely access to a wide variety of OSFI information and documents, including speeches, news releases, guidelines, legislation, policy statements, bulletins, financial information and a listing of all financial institutions and pension plans regulated by OSFI.

**Publications:** OSFI publications are generally available on our Web site ([www.osfi-bsif.gc.ca](http://www.osfi-bsif.gc.ca)) or by contacting: Publications Distribution – Office of the Superintendent of Financial Institutions, 13<sup>th</sup> Floor, 255 Albert Street, Ottawa ON K1A 0H2, Telephone: (613) 990-7655, Facsimile: (613) 952-8219, E-mail: [pub@osfi-bsif.gc.ca](mailto:pub@osfi-bsif.gc.ca)

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