



Risk Management Report

September 2019

The following risks were updated:

Section 1 – Major Risks/Risk Profile: Risks 1-1 to 1-9 all reviewed and updated

Section 2 – Risks to be Monitored: Risk 2-17 added to the Risk Register
(Compensation Fund adequacy) – page 18

Section 3 – Emerging Risks: Risks 3-1 to 3-9 all reviewed and updated

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Current Risk Summary

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Risk Profile Grid (as at September 2019) – PACICC’s Risk Profile remains stable

Impact Rating	Very High	Financial Risk 1-1 Insolvency costs exceed risk limit-risk appetite				PACICC’s priority risks (risk profile) 1-1 A catastrophic earthquake or other factor causes a very large insurer to fail, or leads to multiple, smaller insolvencies; resulting insolvency costs exceed PACICC’s risk limit-risk appetite (twice our annual general assessment capacity) 1-2 Supervisory practices below minimum IAIS standards 1-3 Rate regulation causes insolvency 1-4 Outdated winding-up legislation 1-5 Adverse changes in insurance legislation 1-6 PACICC could be compelled to increase coverage and benefits 1-7 Risk 1-1 puts extraordinary demands on human resources 1-8 Lack of member financial data results in unexpected insolvency costs 1-9 Much of Canada’s accumulated P&C liquidation expertise has “retired”
	High		Regulatory Risks 1-5 New laws 1-6 Benefits enhanced			
	Medium		Operational Risks 1-7 Resource demands 1-8 Unexpected insolvency costs	Regulatory Risks 1-3 Rate regulation Operational Risks 1-9 Lack of liquidator expertise		
	Low				Regulatory Risks 1-2 Solvency supervision 1-4 Outdated winding up legislation	
		Very Low	Low	Medium	High	

Likelihood Rating

Impact Criteria Ranking	Low	Medium	High	Very High
a) Financial Risk	< \$ 5 million	\$5 to \$500 million	\$.5 to \$1.5 billion	>\$1.5 billion
b) Operational Risk	<\$100 thousand	\$.1 to \$1.0 million	\$1.0 to \$2.0 million	>\$2.0 million
c) Reputation Risk	Isolated complaints	Regulatory involvement	Wide media involvement	Government intervention
Likelihood Criteria Ranking	Very Low	Low	Medium	High
All risks	Occur < 1 / 100 years	Occur within 10 years	Occur within 5 years	Occur within 2 years

Responding to Significant Risks: Actions, Responsibility and Timing

The table below summarizes the nine risks in PACICC’s risk profile, with attention on mitigation strategies and actions; responsibility for implementation; and the expected timing for implementation, or the achievement of specific milestones.

Risk	Mitigation Strategies/Actions	Implementation Responsibility	Timing/Milestones
<p>1-1 A catastrophic earthquake or other factor causes a very large insurer to fail, or leads to multiple, smaller insolvencies; resulting insolvency costs exceed PACICC’s risk limit-risk appetite (twice our annual general assessment capacity)</p>	<p>The Federal Department of Finance announced it will consider “how to limit the system-wide risks an extreme earthquake could pose to federal P&C insurers.” It is still unknown whether government will agree to provide a financial backstop; in what form; and with what timing. If a backstop was provided to private insurers using public funds, government would expect repayment over time. In such case, PACICC and the industry would need to agree on some form of Extraordinary Levy. While insurance regulators have expressed support for one such proposal, industry consensus has not yet been achieved. If no backstop is provided, PACICC would engage up to its Risk Limit. However, that limit might be insufficient.</p>	<p>Alister Campbell Grant Kelly</p>	<p>Federal government timeline appears to focus on Fall 2019 for final recommendations to the Finance Minister. PACICC will work closely with IBC to ensure industry alignment and consensus on a Levy mechanism</p>
<p>1-2 Supervisory practices below minimum IAIS standards</p>	<p>PACICC’s strategy is to focus on three key provinces in addition to OSFI: Quebec, Alberta and B.C. These regulators cover the vast majority of solvency supervision in Canada. Approved intervention guidelines with these regulators, and the establishment of the PIRL Committee, bolster this strategy. (Ontario is a residual risk, as its approach to solvency supervision remains unclear).</p>	<p>Grant Kelly</p>	<p>Intervention guidelines are in place with Quebec, and OSFI; agreed in principle with B.C.; and in progress with Alberta (target completion by mid-year 2019)</p>
<p>1-3 Rate regulation causes insolvency</p>	<p>PACICC’s options for mitigating this risk are limited. (Residual risk factor remains “high”). Our strategy is to influence/strengthen the actuarial standards underpinning rate filing and rate adequacy.</p>	<p>Grant Kelly</p>	<p>PACICC continues to make its concerns known to insurance regulators</p>
<p>1-4 Outdated winding-up legislation</p>	<p>PACICC first proposed technical amendments to the <i>Winding-Up and Restructuring Act</i> nearly 10 years ago. To date, the Federal government has not updated the Act. Because PACICC rates the (financial) impact of this risk as “low,” the residual</p>	<p>Grant Kelly Ian Campbell</p>	<p>The current international emphasis on better resolution planning</p>

	risk to the Corporation is relatively modest. If the legislation remains unchanged, can the Board accept the residual risk?		may provide a window for change
1-5 Adverse changes in insurance legislation	PACICC seeks to mitigate this risk by working proactively with Canada's insurance regulators. Recent actions include establishing the PIRL Committee; and completing intervention guidelines with AMF and OSFI (with substantial progress being made in B.C. and Alberta).	Alister Campbell Grant Kelly	Completion of guidelines with B.C. is targeted for Fall 2019; Alberta timing is less clear
1-6 PACICC could be forced to increase coverage and benefits	PACICC considers the likelihood of a forced increase in benefits to be "low." However, the property claims incurred by members from the Fort McMurray wildfire demonstrates that a significant shortfall in PACICC's coverage could occur.	Alister Campbell Grant Kelly Ian Campbell	Coverage and benefits review is PACICC's 2019 priority (work is under way)
1-7 Risk 1-1 puts extraordinary demands on human resources	PACICC has a Board-approved Claims Management Contingency Plan in place to mitigate this risk. A recent review of the Plan demonstrated that it remains appropriate and up-to-date.	Ian Campbell	The Contingency Plan should be reviewed every 24 months (next review due by year-end 2019)
1-8 Lack of member financial data results in unexpected insolvency costs	The number of member companies (and percentage of covered premiums) for which PACICC does not have adequate financial data has been significantly reduced over the past 10 years. We rate the likelihood of this risk occurring as "low." By-Law amendments now require members to disclose their financial data to PACICC.	Grant Kelly Ian Campbell	CCIR has approved amendments to PACICC's By-Law to address this issue; these became operational as of the 2019 AGM
1-9 Much of Canada's accumulated P&C liquidation experience has "retired"	PACICC's ability to mitigate this risk is limited. It is largely the result of a sustained period of good financial health in Canada's P&C industry.	Alister Campbell Grant Kelly Ian Campbell	PACICC continues to make its concerns known to regulators and to the firms providing liquidation services

Risk Limit-Risk Appetite

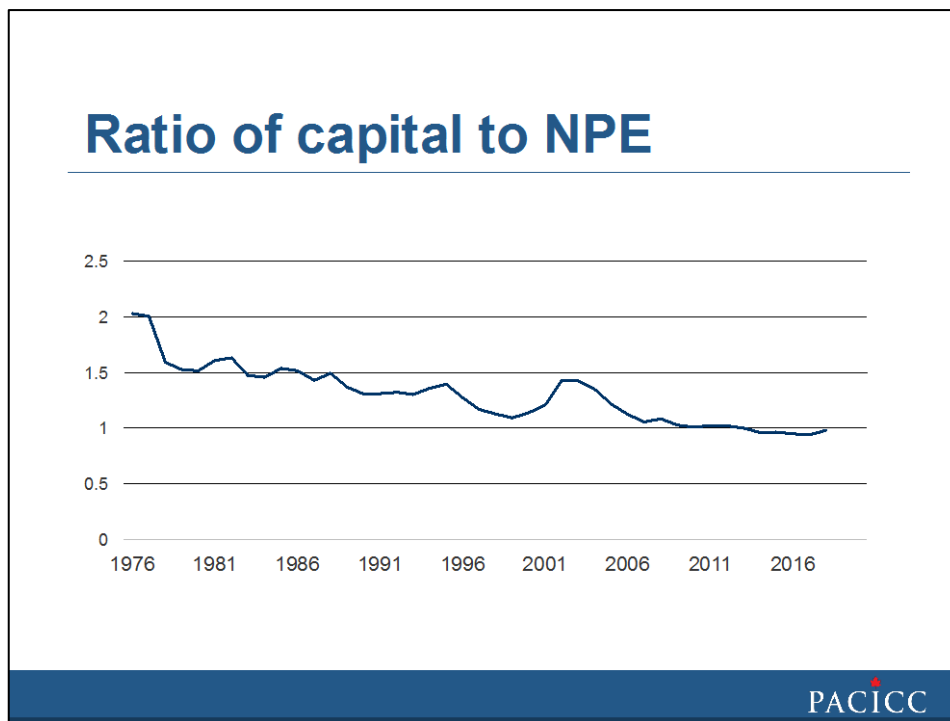
PACICC's current Risk Limit-Risk Appetite is \$1.81 billion. PACICC measures its Risk Limit-Risk Appetite in relation to its ability to collect funds from members over a two-year period to pay for the eligible claims of insolvent members.

PACICC's maximum annual assessment capacity is 1.5 percent of the total covered premiums of members. Based on the most recent annual industry results, 1.5 percent of covered premiums equates to \$903.7 million (as stated in Note 9 to PACICC's audited financial statements for the year ended December 31, 2018).

As of this Report, two times PACICC's annual assessment capacity of \$903.7 million thus yields a Risk Limit-Risk Appetite of \$1.81 billion.

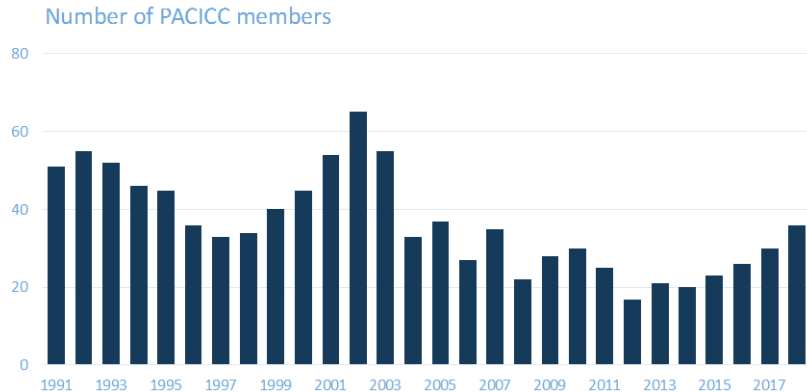
In addition, PACICC maintains a Compensation Fund to address liquidity issues in the period immediately following a member insolvency. The current market value of the Compensation Fund (as at August 31, 2019) is \$56.5 million.

Key indicators of P&C solvency risk



There has been a steady “deleveraging” of P&C premiums in relation to capital over the past 40 years – from a ratio of 2 to 1 in the mid-1970s, to an approximate 1 to 1 ratio now.

Insurers with large swings in premium volume



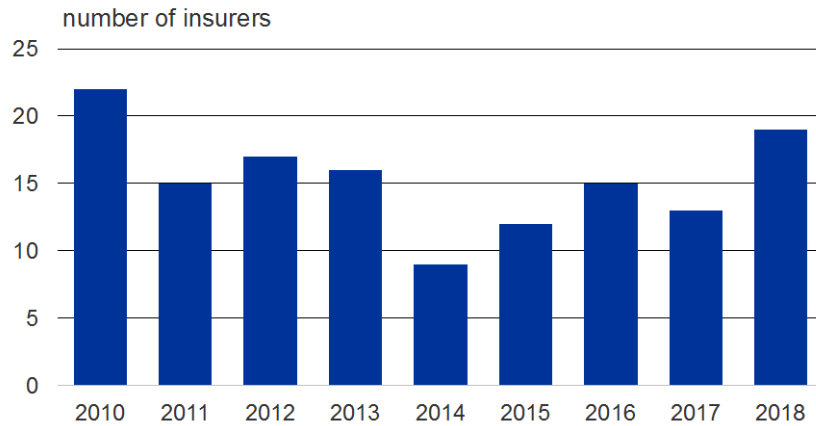
Insurers reporting change in net direct premiums written greater than +/- 33% in a single year.

2019-03-27

PACICC

Large swings in premium volume for individual insurers is a key indicator of solvency risk. (PACICC defines “large” in this context as greater than +/- 33% in a single year). This indicator of solvency risk peaked in 2002. It has been trending down in Canada for more than a decade, but has increased somewhat over the last four years.

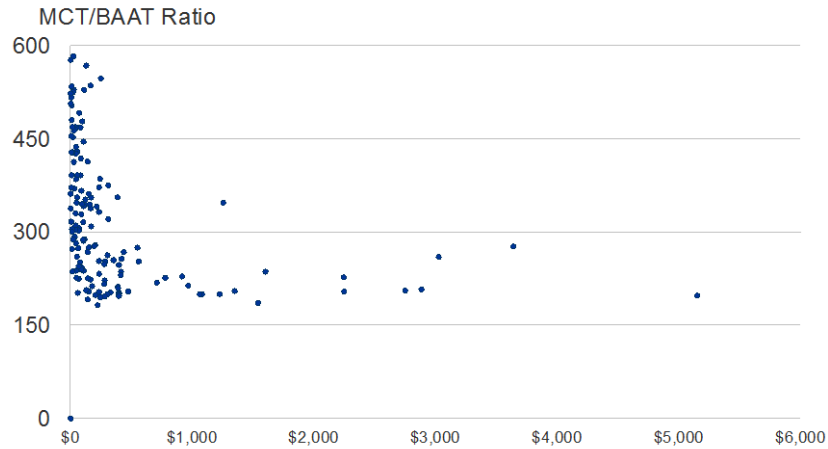
Losses in consecutive years



PACICC

Since 2010, the number of PACICC member insurers incurring losses in (two) consecutive years has trended down – although the last four years (2015-18) show an uptick.

MCT to DPW, 2018



PACICC

Most PACICC members currently maintain an MCT/BAAT ratio that is well above the regulatory minimum of 150%.

Section 1: Major Risks (red) and Significant Risks (yellow) to be addressed

Risk Priority Coding

	Major risks
	Significant risks
	Risks to be monitored
	Emerging risks

Risk No	Inherent Risk and Description	Triggers for adverse Impact	Mitigation/Controls	Rating	
				Impact	Likelihood
1-1	<p>Financial Risk:</p> <p>Insolvency costs exceed PACICC's risk limit-risk appetite (twice our annual general assessment capacity)</p>	<ul style="list-style-type: none"> ○ A catastrophic earthquake resulting in the insolvency of one of PACICC's 10-largest member companies (or their parent companies) ○ The failure of one of PACICC's largest (Top 5) member companies – irregardless of the cause(s) ○ Concurrent, multi-member insolvencies ○ An extensive major financial crisis leading to multiple insolvencies (triggering factors could include: higher inflation, adverse reaction to market volatility, and a sharp rise in interest rates) 	<ul style="list-style-type: none"> ○ The Federal Department of Finance announced it will consider “how to limit the system-wide risks an extreme earthquake could pose to federal P&C insurers.” It is still unknown whether the government will agree to provide a financial backstop; in what form; or with what timing. If a backstop was provided to private insurers using public funds, government would expect repayment over time. In such case, PACICC and the industry would need to agree on some form of Extraordinary Levy. If no backstop is provided, PACICC would engage up to its Risk Limit. However, it is entirely possible that this limit would be insufficient. ○ Prepared an extensive analysis of the industry's capacity to manage catastrophes (Natural Disasters and Catastrophes – 2013; a follow-up report was completed using 2016 industry data and released to PACICC members and other stakeholders in February 2017). ○ PACICC has done substantial work on a proposed Extraordinary Levy Mechanism, and has had favourable feedback from regulators on its recommended solution – but has not yet achieved industry consensus. Formally, PACICC was asked to put the Mechanism “on hold” until it became clear whether the industry (IBC) would succeed in securing a government backstop. (Note: this 	Very High	Very Low

Risk No	Inherent Risk and Description	Triggers for adverse Impact	Mitigation/Controls	Rating	
				Impact	Likelihood
			<p><u>potentially leaves the residual risk for PACICC Risk 1-1 unchanged for an indeterminate period).</u></p> <ul style="list-style-type: none"> ○ Staff have now been authorized by the PACICC Board to restart discussions with the industry toward approval of an Extraordinary Levy. ○ PACICC has a Compensation Fund of \$56 million under our control to meet immediate requirements ○ Regulators monitor insurer exposure to earthquake (OSFI Guideline B-9) ○ IBC has a committee reviewing impact of the costs of extreme earthquakes ○ PACICC commissioned RMS Canada to develop accurate estimates for a large earthquake that could trigger member insolvency ○ OSFI periodically conducts scenario stress testing exercises for correlated risks 		
1-2	Regulatory Risk: Certain provincial regulators have limited solvency supervision resources and expertise	<ul style="list-style-type: none"> ○ Insurance legislation and/or regulations at the provincial level do not contain adequate standards for insurance solvency supervision ○ Practices do not meet the minimum standards of the International Association of Insurance Supervisors (IAIS) ○ Failure to execute supervisory activities due to inadequate staffing and resources 	<ul style="list-style-type: none"> ○ PACICC advocates that P&C provincial solvency supervision meets IAIS standards ○ CCIR has a Solvency Supervisory working group ○ PACICC has developed an intervention guideline; updated its Model Winding-Up Order; developed information materials for distribution to all regulators; and conducted seminars with the regulators in B.C., Alberta, Ontario, Quebec and Newfoundland ○ PACICC's Pre-Insolvency Regulatory Liason (PIRL) Committee – consisting of the public Directors of the Board – facilitates sharing of sensitive information by regulators ○ Intervention guidelines have been completed by PACICC with AMF and OSFI (and are under discussion with Alberta and BC FICOM). While these initiatives may encourage provinces with weaker solvency supervision to strengthen their practices, PACICC remains concerned about under-resourcing of supervisory staff 	Low	High

Risk No	Inherent Risk and Description	Triggers for adverse Impact	Mitigation/Controls	Rating	
				Impact	Likelihood
1-3	Regulatory Risk: Regulation of insurance rates may contribute to member insolvency	<ul style="list-style-type: none"> Political pressure exerted on the rate filing/approval process (e.g. Ontario, to reduce auto insurance rates) Incorrect assumptions regarding what constitutes an adequate rate of return for an insurer Insurance companies are not permitted to challenge the decisions of rate regulators if they disagree Weak regulation of actuarial practices for pricing and loss reserving in some provinces Some politicians have discussed regulating property rates 	<ul style="list-style-type: none"> Scrutiny of insurance company financial condition by rating agencies, supplemented by PACICC's own financial analysis Use of risk-based supervision by regulators PACICC research on the relationship between solvency and rate regulation PACICC encourages senior staff at OSFI to communicate concerns regarding the regulation of rates (for example, automobile insurance rate reduction) to provincial supervisors when they deem it appropriate PACICC is seeking to strengthen provincial regulation of actuarial practices. It is also seeking more information about the role of consulting actuaries in the regulation of insurance rates 	Medium	Medium
1-4	Regulatory Risk: Insurance company winding-up and restructuring legislation and practices in Canada	<ul style="list-style-type: none"> Canada's Winding-up and Restructuring Act (WURA) has not undergone a comprehensive review in nearly 100 years Insolvency management and restructuring practices have evolved internationally more than in Canada 	<ul style="list-style-type: none"> PACICC made a detailed submission to Finance Canada proposing specific changes to modernize WURA. This was in response to the periodic (5-year) review of Federal financial legislation PACICC has initiated stakeholder discussions about the difficulties expected with a complex, conglomerate failure PACICC is examining ways of clarifying its early (pre-insolvency) resolution powers – this is the Corporation's strategic priority for 2020 	Low	High
1-5	Regulatory Risk: Adverse changes in insurance legislation	<ul style="list-style-type: none"> Government could enact legislation affecting aspects of PACICC's operations (e.g. membership eligibility, industry funding, reporting procedures, Board composition, regulatory oversight, etc.) PACICC could be compelled to add members in a line or lines of business inconsistent with its current mandate 	<ul style="list-style-type: none"> Review of policyholder coverage and benefits is scheduled as PACICC's 2019 strategic priority Maintain regular dialogue with industry regulators – jointly developed intervention guidelines (AMF and OSFI) support this Active monitoring of industry developments and financial performance Regular communication with stakeholders to ensure that PACICC's mandate is clearly understood 	High	Low

Risk No	Inherent Risk and Description	Triggers for adverse Impact	Mitigation/Controls	Rating	
				Impact	Likelihood
1-6	Regulatory Risk: Benefits unilaterally enhanced by government regulators	<ul style="list-style-type: none"> ○ Broader interpretation of insurance policy wording by courts and regulators ○ Regulators could require the industry to fund higher premium refunds than currently provided (maximum of \$700 per policy) ○ Benefits could be raised beyond reasonable limits ○ Regulators force coverage of certain specialty lines, where the assessment base could be insufficient to fund the insolvency costs 	<ul style="list-style-type: none"> ○ Maintain a good understanding of financial guarantee fund best practices in other countries (PACICC CEO is Deputy Chair of IFIGS – the International Forum of Insurance Guarantee Schemes) ○ Educate stakeholders on best practices ○ Continue to advocate that moral hazard risk be minimized and that protection apply to personal lines and business policyholders, but excluding large corporations 	High	Low
1-7	Operational Risk: Extraordinary demands on human resources with insolvency of larger member, group, or concurrent multiple member failures	<ul style="list-style-type: none"> ○ Large or multiple insurer failures could require: high volume of requests for claims settlement authority and/or resolution of related issues; complicated assessment process; extensive queries. ○ PACICC needs to outsource functions and could have difficulty administering with existing staff ○ Loss of “key persons” at PACICC could exacerbate this risk 	<ul style="list-style-type: none"> ○ PACICC has developed a Claims Management Contingency Plan to address this risk. The plan was approved by the Board in November 2010. Management believes the plan remains up-to-date and provides an effective framework for mitigating this risk ○ Regular dialogue takes place with regulators to discuss troubled members and to ensure adequate preparedness ○ New agreements on intervention guidelines (with AMF and OSFI) will improve PACICC’s ability to plan for adverse outcomes ○ Succession plan in place to help mitigate “key person risk” 	Medium	Low
1-8	Operational Risk: Insolvency costs greater than anticipated	<ul style="list-style-type: none"> ○ Member insolvency occurs, but PACICC has no or limited financial data and is unable to properly calculate insolvency costs in advance ○ Deficient loss reserves and/or inadequate pricing are key causes of insurer failure (deficient reserves are hard to detect in advance) 	<ul style="list-style-type: none"> ○ PACICC’s position is that regulators should make insurer financial data publicly available. ○ By-Law amendments (passed in April 2019) now require members to disclose financial data to PACICC ○ PACICC now has financial data for all but one (1) of its member companies as of September 2019 ○ We encourage provincial insurance supervisors to adopt the IAIS standards of solvency supervision 	Medium	Low

Risk No	Inherent Risk and Description	Triggers for adverse Impact	Mitigation/Controls	Rating	
				Impact	Likelihood
1-9	Operational Risk: Loss of liquidation expertise	<ul style="list-style-type: none"> ○ Ageing and recent retirements of licensed trustees in bankruptcy with experience liquidating P&C insurers ○ Firms have limited ability to assemble, on short notice, a full team of qualified professionals ○ A sustained period of good financial health in the P&C insurance industry has diminished opportunities to train successors 	<ul style="list-style-type: none"> ○ PACICC's concerns have been communicated to insurance supervisors and to the leading firms that provide insurance company liquidation services ○ PACICC's ability to mitigate this risk is limited. Although the estimated financial impact in a single calendar year may be modest, we consider the likelihood of occurrence to be "medium" (meaning the risk could occur within five years – especially in the event of a member insolvency) ○ Two new ideas were generated in a recent Board simulation/discussion: <ul style="list-style-type: none"> - PACICC could help create a pool of expertise to help mitigate this risk - PACICC could consider having a law firm draft its recommended legislative amendments to WURA – and then present these to Finance Canada 	Medium	Medium

Section 2: Risks to be monitored (not currently considered ‘Major’ or ‘Significant’)

Risk No	Inherent Risk and Description	Triggers for adverse Impact	Mitigation/Controls	Rating	
				Impact	Likelihood
2-1	Operational Risk: Collecting member assessments	<ul style="list-style-type: none"> Some members may not understand their payment obligations Deliberate non-payment due to disagreement or dissatisfaction 	<ul style="list-style-type: none"> Members are required by legislation to pay assessments. The rules are specified in the Memorandum of Operation PACICC notifies regulators to compel payment of overdue accounts 	Very Low	Low
2-2	Financial Risk: Economic downturn impacts member; i.e. liquidity, return on investments and business results	<ul style="list-style-type: none"> New financial products are poorly developed and generate large unexpected or unintended losses Investment capital held by insurers declines in value and yield Credit availability reduced 	<ul style="list-style-type: none"> Monitor the financial condition of members Monitor efforts by legislators and solvency regulators to address the underlying causes of economic downturn 	Low	Low
2-3	Financial Risk: Changes in interest rates and inflation (impact on PACICC)	<ul style="list-style-type: none"> Lower interest rates reduce rates of return on investments Poor investment choices reduce rate of return Ratings downgrade(s) could reduce the value of investments held 	<ul style="list-style-type: none"> Regular reviews (at least annually) of investment policy by Audit & Risk Committee PACICC uses a professional investment manager A senior PACICC manager is responsible for overseeing investment administration – including investment-policy compliance PACICC has estimated the potential “impairment” of its Compensation Fund investments due to a ratings downgrade at 0.47% of a \$56 million portfolio (or \$263,200). This estimate was generated to comply with IFRS 9 requirements Investment Policy was reviewed/updated most recently in April 2019 	Low	Low
2-4	Operational Risk: Property and liability insurance coverage	<ul style="list-style-type: none"> PACICC’s coverage could prove inadequate for insurable losses (e.g. business interruption, loss of records, cyber attack) 	<ul style="list-style-type: none"> Annual review of insurance policies and limits PACICC’s By-laws provide that member assessments can be made if claims exceeded the D&O insurance policy limit 	Low	Low

Risk No	Inherent Risk and Description	Triggers for adverse Impact	Mitigation/Controls	Rating	
				Impact	Likelihood
		<ul style="list-style-type: none"> Improper actions (e.g. breach of duty or conflict of interest) by officers or directors 			
2-5	Operational Risk: Operating expenses exceed budget	<ul style="list-style-type: none"> Unanticipated large capital or operating expenditure, e.g. IT Accounting changes (for example, Board decision to pay investment management fees from the operating budget rather than from the Compensation Fund) 	<ul style="list-style-type: none"> Operating Fund surplus (\$1.6 million) can, with Board approval, fund a short-term budget deficit without asking members to pay additional assessments 	Low	Low
2-6	Regulatory Risk: Use of unlicensed reinsurance in Canada	<ul style="list-style-type: none"> Unlicensed reinsurance is difficult to collect for an insolvent insurer Unlicensed reinsurers not subject to Canadian insurance regulation Unlicensed reinsurance contract may not contain an insolvency clause OSFI Guideline B-3 has removed the 25 percent limit on unlicensed reinsurance 	<ul style="list-style-type: none"> Monitor changes in the use of unlicensed reinsurance and review with OSFI changes in the share of unlicensed reinsurance OSFI Guideline B-3 requires each insurer file a Reinsurance Risk Management Plan (RRMP), which addresses use of unlicensed reinsurance 	Low	Low
2-7	Regulatory Risk: Non-profit tax exemption for investment income	<ul style="list-style-type: none"> Existing policies “reinterpreted” by the CRA to challenge the tax-free status of PACICC’s investment income from Compensation Fund CRA is conducting audits of non-profit corporations to check for activities <i>intended</i> to be profitable 	<ul style="list-style-type: none"> Maintain a good understanding of the tax treatment of guarantee funds in other countries Work with guarantee fund counterparts in Canada, should PACICC need to counter a tax-related threat 	Low	Low
2-8	Regulatory Risk: Regulators seek to exert more influence over PACICC governance	<ul style="list-style-type: none"> Insurance regulators seek to expand PACICC mandate to address restructuring Regulators are encouraged by other stakeholders to merge PACICC with larger financial guarantee funds 	<ul style="list-style-type: none"> PACICC has changed the terms of reference for its Board Chair. (The Chair will now be a public director on a permanent basis, and will serve a three-year term) 	Low	Low

Risk No	Inherent Risk and Description	Triggers for adverse Impact	Mitigation/Controls	Rating	
				Impact	Likelihood
		<ul style="list-style-type: none"> Regulator requires all Board members to be public (non-industry) directors 	<ul style="list-style-type: none"> Regulators invited to attend Board meetings and they receive copies of proceedings PACICC's <i>Code of Ethics and Business Practices</i> is attested annually by Directors International P&C guarantee fund boards typically have a majority of industry directors 		
2-9	Operational Risk: Attract and retain knowledgeable and experienced personnel	<ul style="list-style-type: none"> Senior staff leaves PACICC to accept other employment, for personal, financial or health reasons Lack of adequate succession planning 	<ul style="list-style-type: none"> Staff could be borrowed short-term from IBC, Assuris, CDIC, and/or members HR policies and procedures documented A management succession plan is overseen by the Governance and HR Committee of the Board The plan is scheduled to be reviewed by the Committee in Fall 2019 	Low	Low
2-10	Operational Risk: Reliance on IT outsourced operation	<ul style="list-style-type: none"> Service provider removes service Equipment issues not readily resolved Unauthorized access Cyber attack: viruses, hacker, data breach 	<ul style="list-style-type: none"> PACICC uses an externally hosted, secure, internet-based server that provides full back up and recovery All staff are equipped to work offsite when required using their own computers PACICC's supplier of IT services (F12.net) has conducted an independent audit of its "System and Organization Controls for Service Organizations" (SOC 2® Type 2 Report) and shared results with PACICC The SOC 2 audit findings confirm that F12 has taken reasonable steps to protect the security of client files PACICC will regularly review the cyber-security measures it has in place 	Low	Low
2-11	Operational Risk: Disaster Recovery Plan (DRP)	<ul style="list-style-type: none"> Power outage, ice storms, floods where entire community shut down affecting the availability of staff and infrastructure (as per recent actual events) Other possible events include: flu pandemic (SARS), terrorist attack, large-scale natural disaster 	<ul style="list-style-type: none"> HR policies and procedures in place, with outsource agreement with IBC Website available to communicate with stakeholders DRP is documented and in place, including off-site work arrangement (plan was 	Medium	Low

Risk No	Inherent Risk and Description	Triggers for adverse Impact	Mitigation/Controls	Rating	
				Impact	Likelihood
			<p>reviewed by the Governance & HR Committee in Fall 2018)</p> <ul style="list-style-type: none"> ○ Insurance in place ○ Fire-proof safe for protecting original documents 		
2-12	Operational Risk: Inadequate or insufficient resources and/or funding	<ul style="list-style-type: none"> ○ Failure to gather and analyze sufficient information regarding current industry practices ○ Inadequate coordination with other financial guarantee funds ○ Necessary functions not performed ○ Lack of controls leads to fraud, misappropriation, security breaches, inaccurate or incomplete reporting 	<ul style="list-style-type: none"> ○ PACICC is sharing information with domestic and international guarantee funds ○ Management ensures the Board is advised of operating issues 	Low	Low
2-13	Operational Risk: Ineffective governance	<ul style="list-style-type: none"> ○ Fraud not prevented or detected ○ Security breach not prevented or detected ○ Unauthorized access causes loss of data or compromises integrity ○ Incomplete or inaccurate reports prepared 	<ul style="list-style-type: none"> ○ PACICC Board places significant emphasis on good governance practices ○ PACICC has followed the lead by OSFI for enhancing governance in the industry – OSFI Guideline E-13 and CSA Guidelines 	Low	Low
2-14	Operational Risk: Insurers fail for various reasons	<ul style="list-style-type: none"> ○ Products not properly developed or rated ○ Products provide unexpected coverage, e.g. court interpretation ○ Losses greater than expected, e.g. claims staff not properly trained ○ Excessive concentrations of risk 	<ul style="list-style-type: none"> ○ Memorandum of Operation currently limits PACICC's coverage to seven classes of insurance. (Policies outside these classes are not covered) ○ PACICC has the ability to estimate liquidation costs through its own modeling ○ Coverage and Benefits review should address potential inadequacies in current limits ○ PACICC addressed the issue of excessive risk concentration in a 2015 submission to CCIR ○ PACICC has also initiated a discussion with the Alberta regulator concerning excessive risk concentration – with particular reference to the Fort McMurray wildfire 	Medium	Low

Risk No	Inherent Risk and Description	Triggers for adverse Impact	Mitigation/Controls	Rating	
				Impact	Likelihood
2-15	Operational Risk: Failure of a financial conglomerate involving multiple Guarantee Funds	<ul style="list-style-type: none"> International failure of organization with Canadian branch or subsidiary Domestic conglomerate with Life and or deposit-taking affiliates Powers of various Guarantee Funds are inconsistent, e.g. CDIC has more extensive powers and can create a “bridge bank” in the event of a failure 	<ul style="list-style-type: none"> While PACICC maintains regular contact with other financial guarantee funds in Canada (including CDIC), the organization’s ability to mitigate this risk is limited 	Medium	Low
2-16	Operational Risk: Key suppliers of services and outsourced arrangements	<ul style="list-style-type: none"> Unanticipated failure could impair PACICC operations in the short-term while alternate arrangements are made (new supplier contracted or new equipment sourced) <p>(Key outsourced service areas include: IT supplier, Accounts Payable, Investment Management, Banking and Legal)</p>	<ul style="list-style-type: none"> PACICC retains established, reputable suppliers with proven experience Service level agreements are in place (for example, IT, Investment Management, Accounts Payable) While the loss of service by a supplier could be disruptive in the short term, management believes that PACICC’s current outsourced service arrangements could be replaced quickly (in most cases within one month) Note: Refer also to Risk 2-10 	Low	Low
2-17	Financial Risk: Compensation Fund proves to be inadequate	<ul style="list-style-type: none"> Large failure results in UEP liabilities > the size of the current Fund Catastrophic event (e.g., a severe earthquake) results in sizeable UEP liabilities and triggers contagion (e.g., among smaller regional insurers in B.C. and Alberta) 	<ul style="list-style-type: none"> Federal government backstop is a potential mitigating factor Implementing an extraordinary levy mechanism could also mitigate contagion caused by a large catastrophic loss Use of monthly plans to pay premiums limits the extent of UEP liabilities, although failure of a large member could still exceed PACICC’s current Fund size Note: IBC has floated the idea of PACICC increasing the size of the Compensation Fund as part of the current discussions with Finance Canada relating to mitigating earthquake risk 	Medium	Medium

Section 3: Emerging Risks

Most of the risks below have been preliminarily rated “low.” As more information develops – particularly about the potential of these risks to cause solvency problems for PACICC members – the ratings could change.

Risk No	Inherent Risk and Description	Triggers for adverse impact	Comments	Rating	
				Impact	Likelihood
3-1	Operational Risk: Risk of non-covered policies impacting covered portfolios	<ul style="list-style-type: none"> Members that participate in the Nuclear Insurance pool in Canada incur major losses, leading to possible insolvency 	While covered lines are clearly defined in PACICC’s Memorandum of Operation, it is difficult to mitigate potential “spillover” solvency risk from non-covered lines. Analysis of potential impacts could help PACICC better understand this risk.	Low	Low
3-2	Financial Risk: PACICC coverage limits may prove inadequate	<ul style="list-style-type: none"> Price of homes increasing Price of insurance cover increasing (\$700 cap per policy on unearned premium refund may be inadequate) Claims limits could be inadequate, especially in the case of total property losses 	<p>PACICC’s coverages and benefits are currently undergoing comprehensive review.</p> <p>The Board can decide to cover losses beyond PACICC’s limits in exceptional circumstances.</p> <p>The potential for reputation damage due to a sizeable shortfall in PACICC coverage has been highlighted by loss claims from the Fort McMurray wildfire.</p> <p>Some Superintendents of Insurance have expressed concern that PACICC’s limits may be too low.</p> <p>PACICC has conducted a member survey (assisted by Eckler) estimating the current (2018) cost of covered claims.</p>	Medium	Low

Risk No	Inherent Risk and Description	Triggers for adverse impact	Comments	Rating	
				Impact	Likelihood
3-3	<p>Financial/Operational and Regulatory Risks:</p> <p>As new insurance product(s) emerge, PACICC's coverage may need to be clarified</p>	<ul style="list-style-type: none"> ○ Driverless cars ○ Drones (for commercial use) ○ Cyber-crime coverage (see comments in next column) ○ Flood insurance 	<p>Emerging risks/ policies in the four areas noted as triggers would appear to be covered by PACICC. Driverless cars are still several years away from wider commercial availability (5 to 10 years, according to experts). While the other three risks are already occurring, the potential to cause insurer solvency problems appears to be low. Cyber insurance may be an exception, though – particularly if the coverages offered turn out to be poorly understood by some insurers, and/or the pricing does not fully reflect the risks involved. Some critics question whether cyber risk is truly insurable – particularly if an attack occurred on a previously unprecedented level (a “9/11 moment in the cyberworld”)</p> <p>In addition, modernization of payment systems – particularly the shift to real-time payments – could contribute to greater funds-transfer fraud.</p> <p>Since cyber insurance is not explicitly excluded by PACICC (among the eight categories/classes of liability insurance reported under CCIR rules), it appears it would be covered.</p> <ul style="list-style-type: none"> ○ Is this what PACICC intended? ○ The issue will be addressed as part of PACICC's current review of coverage and benefits. 	Low	Low
3-4	<p>Regulatory Risk:</p> <p>Increased requirements for consumer education and awareness</p>	<ul style="list-style-type: none"> ○ Consumers not aware of coverage provided by PACICC ○ Financial Literacy initiatives of government ○ Increasing international regulatory initiatives 	<p>While this risk seems unlikely to pose significant financial cost to PACICC, the potential exists for reputation damage if government/ regulatory expectations increased.</p>	Low	Low

Risk No	Inherent Risk and Description	Triggers for adverse impact	Comments	Rating	
				Impact	Likelihood
3-5	Financial Risk: P&C industry consolidation	<ul style="list-style-type: none"> ○ P&C industry consolidation results in PACICC having a greater number of “large” member insurance companies ○ Could some PACICC members be “too small to succeed” in a rapidly consolidating, technology-driven environment? 	<p>Data show that P&C industry concentration in Canada has increased over the past decade. Comparing data from 2006 (earliest available from MSA) and 2016 reveals the following:</p> <p>DWP for Canada’s largest 10 P&C insurers increased from 37.9% of total premiums in 2006 to 52.3% in 2018.</p> <p>The number of PACICC member insurers reporting total unpaid claims reserves > twice PACICC’s annual assessment capacity (our risk limit-risk appetite) increased from 11 companies in 2006 to 14 companies in 2018.</p> <p>PACICC should probe the “too small to succeed” issue by examining key performance measures by size of firm.</p>	Low	Low
3-6	Regulatory Risk: Peer-to-peer commerce poses new and possibly disruptive insurance risks	<ul style="list-style-type: none"> ○ Peer-to-peer (P2P) service providers like Uber, Airbnb, et al. pose different insurance risks compared with traditional (and often more regulated) service providers. Will these risks be adequately covered by our industry? Could possible solvency risks emerge? ○ P2P insurance networks also have the potential to disrupt traditional forms of insurance. Part of their appeal is the prospect of lower costs, which advocates claim will come from dividends or return of premiums. 	<p>PACICC should continue to monitor developments in the P2P sector, particularly as they relate to insurance.</p> <p>Key issues relating to P2P insurance start-ups/networks include: how will they be licensed or regulated in Canada? (If undercapitalized, they could pose greater solvency risks). Will P2P insurers be required to join a Compensation Scheme like PACICC?</p>	Low	Low

Risk No	Inherent Risk and Description	Triggers for adverse impact	Comments	Rating	
				Impact	Likelihood
3-7	<p>Financial Risk:</p> <p>Could the rise of Insurtech, as a potential P&C insurance “disruptor,” introduce solvency risks?</p>	<ul style="list-style-type: none"> ○ P&C insurance companies that fail to adopt these new technologies (encompassing Artificial Intelligence, data analytics, and the Internet of Things) may be uncompetitive with respect to underwriting expertise and expenses, and out-of-step with younger customers ○ However, there may also be a risk of P&C insurance companies “over-leveraging” Insurtech as an attempt to gain competitive advantage. (Insurtech capabilities notwithstanding, underpricing and inadequate reserving remain the principal causes of P&C insurer insolvency). 	<p>Insurtech is both a potential disruptor (imagine a “digital” insurance company) and a loss prevention / cost reduction tool. The latter explains why established insurers are investing in and partnering with Insurtech start-ups.</p> <p>At this point, Insurtech developments do not appear to pose new solvency risks. This could change, however, if Insurtech’s evolve into standalone insurers, rather than functioning primarily as “aggregators” and partners of established (and regulated) insurance companies.</p> <p>One potential disadvantage is that Insurtech may encourage customers to focus so much on price and convenience that they neglect (or are not properly advised about) coverage.</p> <p>PACICC will continue to monitor Insurtech developments for potential industry disruption, new business products, and possible solvency implications.</p>	Low	Low
3-8	<p>Financial Risk:</p> <p>New financial technologies could pose risks to the stability of the financial system</p>	<ul style="list-style-type: none"> ○ FINTECH has the potential to disrupt the stability of bank funding, credit quality – and possibly even the stability of the broader economy ○ FINTECH developments appear to be outpacing the ability (and resources) of regulators to keep up. 	<p>Warnings related to the potential systemic risks of FINTECH have been sounded recently, for example, by the Financial Stability Board.</p>	Low	Low

Risk No	Inherent Risk and Description	Triggers for adverse impact	Comments	Rating	
				Impact	Likelihood
3-9	<p>Financial Risk:</p> <p>Institutional investors face growing pressures to address so-called ESG (environmental, social and governance) risks and opportunities in their investment policies and portfolios</p>	<ul style="list-style-type: none"> ○ Lack of regulatory clarity with respect to ESG factors may cause uncertainty ○ ESG-related regulatory constraints could be tightened ○ PACICC may be expected to mirror ESG best practices being followed by its members 	<p>PACICC does not have specific liabilities in the manner of an insurance company or a pension fund. ESG factors are therefore less likely to prevent PACICC from meeting its obligations to policyholders.</p> <p>PACICC's investment manager (CIBC Asset Management) follows ESG best practices and became a signatory to the <i>UN Principles for Responsible Investment</i> (UNPRI) in November 2017.</p>	Low	Low

Appendix

PACICC Risk Management Definitions

Note: The following definitions are based on the ISO 31000 2009 Plain English Risk Management Dictionary, with minor edits as appropriate for PACICC's risk management environment.

Risk

Risk is the “effect of uncertainty on objectives” and an *effect* is a positive or negative deviation from what is expected. Organizations strive to reduce uncertainty as much as possible.

Uncertainty is a state or condition that involves a deficiency of information and leads to inadequate or incomplete knowledge or understanding. In the context of risk management, uncertainty exists whenever the knowledge or understanding of an event, consequence, or likelihood is inadequate or incomplete.

Risk management (Enterprise Risk Management – ERM)

Risk management refers to a coordinated set of activities and methods that is used to direct an organization and to mitigate or control the many risks that can affect its ability to achieve objectives.

The term *risk management* also refers to the architecture that is used to manage risk. This architecture includes risk management principles, the risk management framework and risk management processes.

Risk management framework (Risk Management Statement)

A *risk management framework* is a set of components that support and sustain risk management throughout an organization. There are two types of components: foundations and organizational arrangements. *Foundations* include the risk management policy, goals and objectives, mandate, and commitment (Mission and Principles). *Organizational arrangements* include the plans, relationships, accountabilities, resources, processes and activities used to manage the organization's risks.

Risk management policy

A *risk management policy* documents an organization's commitment to risk management and clarifies its general direction and intention. Components include procedures, practices, controls, responsibilities and activities (including their sequence and timing).

Risk management process

A *risk management process* is one that systematically applies management policies, procedures, controls and practices to a set of activities intended to establish the context of risks, communicate with stakeholders and identify, analyze, evaluate, treat, monitor and review risks.

To establish the *context* means to define the external and internal parameters that organizations must consider when they manage risk. External context includes external stakeholders, local, national, and international environment, as well as any external factors that influence an organization's objectives. Key drivers and trends include stakeholder views, perceptions and relationships, as well as social, cultural, political, legal, regulatory, financial, technological, economic, natural, and the competitive environment factors.

Internal *context* includes an organization's internal stakeholders, the approach to governance, contractual relationships, capabilities, culture and standards. *Governance* includes the organization's structure, policies, objectives, roles, accountabilities and decision-making processes. Capabilities include knowledge and resources; human, technological and capital.

Risk assessment

Risk assessment is a three-part process consisting of risk identification, risk analysis and risk evaluation.

Risk identification is a process that is used to find, recognize and describe the risks that could affect the achievement of objectives. It also includes the identification of possible causes and potential consequences. Historical data, theoretical analysis, informed opinions, expert advice and/or stakeholder input could be used to identify an organization's risks.

Risk analysis is a process that is used to understand the nature, sources and causes of the risks that are identified, and to estimate the level of risk. Analysis is also used to study impacts and consequences and to examine the mitigation and controls that currently exist.

Risk evaluation is a process that is used to compare risk analysis results with risk appetite in order to determine whether or not a specified level of risk is acceptable or tolerable.

Risk Register (as defined by PACICC)

PACICC has compiled a *Risk Register* identifying risks that could cause PACICC not to meet its goals and objectives, including a brief assessment of each risk. More significant risks are then selected for in-depth review and, if deemed appropriate, escalated to PACICC's Risk Profile.

Risk Profile (as defined by PACICC)

PACICC's *Risk Profile* is a graphic presentation and written description of the major risks which could potentially have a significant, adverse impact on PACICC's ability to meet its goals and objectives. The description includes a comprehensive risk assessment (see definition), ranking of the impact and likelihood (probability) of the risk occurring, a description of consequences, and a description of the treatment (action plan) showing owners and timelines. The *Risk Profile* includes any risks that the organization must monitor and manage, regardless of type of risk (for example, financial, operational or reputational).

A *consequence* is the outcome of an event and has an effect on objectives. A single event can generate a range of consequences that can positively or negatively affect goals and objectives. Initial consequences can also escalate through ripple effects.

Likelihood (probability) is the chance of a risk occurring. *Likelihood* can be defined, determined, or measured objectively or subjectively; and it can be expressed qualitatively or quantitatively.

Severity refers to the magnitude of a risk. Severity is estimated by considering and combining consequences and likelihoods. It can be assigned to a single risk or to a combination of risks. Severity is described as Level of risk per ISO 39000.

Risk treatment is a risk modification process. It involves selecting and implementing one or more treatment options – for example, avoiding the risk, reducing the risk, removing the source of the risk, modifying the consequences, changing the probabilities, sharing the risk with others, or simply retaining the risk.

Risk appetite

(As defined by PACICC, with adaption / modification of ISO definitions of Risk Attitude and Risk Criteria)

Risk appetite is a point of reference used to assess and evaluate the significance or importance of an organization's risks. It is used to determine whether a specified level of risk is acceptable or tolerable. An organization's *risk appetite* also defines its general approach to risk, for example, whether risks should be retained, shared, reduced or avoided, and whether or not risk treatments are implemented or postponed.

Residual risk

Residual risk is the risk left over by determining the inherent risk of an activity, then reducing the risk based on the organization's governance and control processes, and specific risk-mitigation measures.

The key objective in monitoring risks on the Risk Profile is to ensure that action plans serve to reduce residual risk. Mitigation strategies may include removing the source of the risk, modifying the consequences, changing the probabilities, transferring the risk or retaining the risk.