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# Letter

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Title	Life Insurance Capital Adequacy Test (LICAT) Advisory
Date	November 27, 2020
Sector	Life Insurance and Fraternal Companies

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**To:** Federally Regulated Life Insurance Companies, Fraternal Benefit Societies, Holding Companies, and Companies Operating in Canada on a Branch Basis

Today OSFI is releasing an advisory to the LICAT guideline to formally include in the framework a smoothing technique for determining interest rate risk (IRR) requirements for participating business (par) that OSFI introduced and communicated in April 2020. Also included in the advisory is a clarification to OSFI's expectations related to negative DSRs (Dividend Stabilization Reserves or other similar experience leveling mechanisms). The advisory has an effective date of January 1, 2021.

Earlier this year, OSFI communicated that it had identified an aspect in the LICAT that, due to the methodology, could cause some unwarranted volatility in IRR requirements for par. Changes to the LICAT guideline to address this issue were proposed and communicated via a public consultation that launched in February 2020.

Because of the COVID-19 situation, as confirmed by OSFI in its March 27 letter, the public consultation and finalization of the proposed updates to the LICAT were put on hold. In its April 9 letter OSFI introduced a smoothing technique to mitigate possible unwarranted volatility in the LICAT calculation for IRR for par business. As the measure is sufficient in addressing unwarranted volatility in the test and considering feedback from stakeholders, OSFI decided to retain this measure until at least December 31, 2023. This decision was communicated in OSFI's *COVID-19 Measures – FAQs for Federally Regulated Insurers*.

The February 2020 public consultation of the LICAT also included a clarification on OSFI's expectations related to claiming par credit and the treatment of negative DSRs in Available Capital. Considering further input from some insurers, we have modified the clarification to address some implementation challenges.



This advisory complements the LICAT calculation for par business, and should be read in conjunction with the *LICAT 2019 guideline*.

With the issuance of this advisory, the draft LICAT 2020 published on OSFI's website in February will be removed.

Should you have any questions, please contact Michelle John, Director, Life Insurance Capital, Capital Division by email at [michelle.john@osfi-bsif.gc.ca](mailto:michelle.john@osfi-bsif.gc.ca).

Sincerely,

Ben Gully

Assistant Superintendent

Regulation Sector