Letter

Title	Internal Capital Adequacy Assessment Process (ICAAP) – Letter (2010)
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To: Banks, Bank Holding Companies, Federally Regulated Trust and Loan Companies

This guideline outlines OSFI's expectations with respect to an institution's ICAAP and supplements Guidelines A and A-1, **Capital Adequacy Requirements** (CAR). The principles embodied in the draft guideline are consistent with the *Supplemental Pillar 2 Guidance* included in the Basel Committee on Banking Supervision's July 2009 paper, **Enhancements to the Basel II Framework**. With this letter, OSFI issues the final version of guideline, unchanged from the August 2010 draft.

Capital requirements set out in the CAR guidelines are regulatory minimums that assume that an institution has a portfolio of risk exposures that is highly granular and widely diversified. Institutions can not assume that compliance with regulatory minimum capital requirements provides a safe harbour in a risk-based capital regime.

A thorough and comprehensive ICAAP is a vital component of a strong risk management program. The ICAAP should produce a level of capital adequate to support the nature and level of an institution's risk. Each institution is responsible for developing and implementing its own ICAAP for the purpose of setting internal capital targets and developing strategies for achieving those internal targets that are consistent with its business plan, risk profile and operating environment.

In the case of institutions using the standardized approach to credit risk, OSFI's Supervision Sector issues ICAAP letters that provide feedback from our reviews of institutions' ICAAPs. The letters, most recently issued in December 2009, also provide a foundation for structured discussions of ICAAP with these institutions.

OSFI recognizes the considerable systems development required to support the rollout of the ICAAP over the last 3 years. It also recognises that further systems development may be necessary as ICAAP systems mature. Because ICAAP is an institution-owned process and not an exercise in regulatory compliance, OSFI would expect institutions to prioritize any residual development work based on their assessment of risks arising from shortcomings or weaknesses in their own processes.

Questions concerning the guideline should be addressed to Aina Liepins, Capital Division, at (613) 991-5555, by facsimile at (613) 991-6822 or by e-mail at aina.liepins@osfi-bsif.gc.ca.

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