



1. Introduction

Industrial Alliance Trust Inc. (“iA Trust” or “the company”) is a trust and loan company subject to the *Trust and Loan Companies Act (Canada)*. iA Trust was initially a provincial charter company; it became a federal charter company in March 2005 and its main supervisory authority is the Office of the Superintendent of Financial Institutions (“OSFI”). It is a wholly-owned subsidiary of Industrial Alliance Insurance and Financial Services Inc. (“IAIFS”), a life and health insurance company that engages in business throughout Canada, as well as in the United States. IAIFS is listed on the Toronto Stock Exchange under the symbol IAG. iA Trust does not hold or control any subsidiary and the results presented for the company have not been consolidated with those of other entities.

iA Trust’s primary activities are distributing deposit products through demand deposits and guaranteed interest deposits with a 1- to 5-year term and issuing vehicle personal loans. iA Trust also acts as the trustee for registered products for companies of iA Financial Group. In this respect, it sometimes acts as a deposit-taking institution for sums held in cash in the accounts of clients for whom it is the trustee in the form of demand deposits.

The company has established an investment policy and a matching policy to monitor the deposits received and the loans issued. Thus, the company has put measures in place to manage the credit risk and structural interest rate risk of its portfolio. Cash management is subject to daily monitoring in order to support liquidity risk management. The company has very low market risk exposure and is in no way exposed to foreign exchange risk. It is also of the view that its exposure to counterparty risk is negligible because the assets held are of good quality; thus, the vast majority of the assets in the form of bonds are government bonds. Assets held in the form of loans include insured residential mortgage loans, vehicle loans and RRSP loans. The vehicle loans are secured by the vehicles over which the company can enforce its rights in case of default.

This document is designed to meet the disclosure requirements set by the OSFI pursuant to the proceedings of the Basel Committee on Banking Supervision. This disclosure is done according to the requirements of the third pillar of the Basel agreements.

2. Capital (Data as of March 31, 2017)

iA Trust is a wholly-owned subsidiary of IAIFS. Its capital consists primarily of two sources. The first is the share capital issued by the company, held by IAIFS. The second source corresponds to the company’s retained earnings. Thus the company’s capital consists solely of tier-1 capital; the company does not have any tier-2 capital such as preferred shares or subordinated debts. In these circumstances, the expression “total capital” used in relation to the company in this document refers only to tier-1 capital.

The company’s capital (in millions of \$) determined according to Basel III requirements is:

	2017-03-31	2016-12-31
Share capital	45.0	45.0
Retained earnings	7.0	6.8
Other capital components	0.5	0.2
Total – Capital	52.5	52.0

iA Trust is a trademark and business name under which Industrial Alliance Trust Inc. operates.

To manage its capital, iA Trust has put the following measures in place. Firstly, the company carries out an annual Internal Capital Adequacy Assessment Process (ICAAP) as required by OSFI. The ICAAP is intended to establish the proper capital level required by the company based on its risk profile. The ICAAP is prepared by the company’s senior management and presented to the board of directors for approval. The ICAAP serves as the basis for establishing the regulatory capital management framework. The framework is approved annually by the board of directors. The regulatory capital management framework has the following objectives:

- To set the minimum and maximum amounts and the target for capital. The minimum, maximum and target are set according to the ICAAP results and regulatory limits corresponding to the asset-to-capital ratio and the risk-based capital ratio.
- To file with the board of directors a quarterly report on the company’s capital development, including a capital projection based on anticipated events for the coming quarters.
- To define actions to be taken based on projections in order to maintain capital within the designated benchmarks (maximum and minimum).

With respect to calculations for determining the risk-based capital ratio based on the capital adequacy requirements set by the OSFI, the company has made the following choices:

- For credit risk, the company has chosen to take the standard approach. Thus, iA Trust uses evaluations made by credit rating organizations to determine risk weighting factors and uses the standard mapping process published by the OSFI. This approach was preferred to that based on internal ratings. Note that the company does not take part in securitization activities.
- For operational risk, the company has chosen to take the “basic indicator” approach. With this approach, risk assessment is performed by applying a formula based on the annual gross income of the past three years.
- For market risk, the company is not of the size to require the application of the formula prescribed by capital adequacy requirements for market risk.

The results for the company’s capital ratios are given below. Note that the OSFI’s requirement for the company is 10.5% for the risk-based capital ratio (tier-1 capital).

Ratios	2017-03-31	2016-12-31
• Leverage ratio	10.3%	10.3%
• Risk-based capital ratio	18.4%	18.4%

Taking into account existing OSFI capital adequacy requirements which are 10.5% for the risk-based capital ratio, the level of capital required according to capital adequacy requirements for credit risk, operational risk and market risk are (in millions of \$):

Capital requirements	2017-03-31	2016-12-31
• Credit risk	28.7	28.1
• Operational risk	1.1	1.2
• Market risk	0.0	0.0

iA Trust is a trademark and business name under which Industrial Alliance Trust Inc. operates.

3. Risk Management (Data as of September 30, 2016)

The following information is based on data gathered annually as part of the ICAAP. At the request of the OSFI, the ICAAP 2016 was carried out on September 30. The risk management data therefore reflect what was available as of September 30, 2016.

3.1 Credit risk

Credit risk management applies to the areas of investments and company loans (automobile, mortgage or RRSP):

Investments

Investments correspond to the assets held in the form of short-term securities and bonds. The company’s investment policy establishes the principles for credit risk management. Credit risk management is based on a prudent approach.

Similarly, the company uses the credit ratings established by a recognized credit agency and has a policy of not acquiring debt securities of a quality below BBB (low). The company has adopted a policy of not acquiring shares.

In order to adequately manage credit risk, the investment policy also calls for diversification measures by asset class as well as criteria for diversification within each asset class (limit by category of issuer, by type of issue, by credit rating, by issuer, Bloomberg classification sector).

Therefore, as of September 30, 2016, the securities portfolio structure reflects a prudent approach in order to manage credit risks:

- Short term \$13.3 million 100% in securities issued by the provinces with R-1 (high) and R-1 (middle) ratings.
- Bonds \$165.0 million 87% of the portfolio consists of securities issued by the Government of Canada, province, guaranteed or made by a province; 13% of the portfolio consists of corporate bonds (65% issued by financial institutions and 35% by companies).

As of September 30, 2016, the company has no security in default or under surveillance in its portfolio.

Bond portfolio maturities as of September 30, 2016, were as follows (in millions of dollars):

Maturity in less than 1 yr	14.4
Maturity in 1 to 5 yrs	100.1
Maturity in 5 to 10 yrs	50.2

Loans

The company is involved in personal loan activities through automobile, RRSP and mortgage loans.

With regard to mortgage loans, the company ceased to acquire new loans in late-2013, preferring to concentrate on vehicle lending. As of September 30, 2016, the mortgage loans in the portfolio stand at \$5.1 million, and consist exclusively of residential loans. The mortgage loans in the portfolio are acquired under an agreement with the parent company, Industrial Alliance Insurance and Financial Services Inc., which evaluates credit. Any loan that has a loan-to-value ratio that exceeds 80% is insured. The equivalent of 100% of the loans in effect is insured by CMHC or a private insurer. As of September 30, 2016, the company has no outstanding mortgage loans in its portfolio, and no provision has been taken for the portfolio.

Vehicle financing is intended for individual consumers through a network of company-certified auto dealers. Currently, distribution of these loan products is restricted to the provinces of Quebec, Ontario, Manitoba, British Columbia, Nova Scotia, iA Trust is a trademark and business name under which Industrial Alliance Trust Inc. operates.

New Brunswick, Newfoundland and Prince Edward Island. As of September 30, 2016, the company’s vehicle loan portfolio stands at \$285.8 million. The company holds a security interest in the vehicle acquired by the borrower. The credit risk is managed through the implementation of proper procedures concerning the evaluation of the client’s credit, the establishment of loan acceptance benchmarks and client follow-up in case of failure to make payments.

Approval limits have been established. The maximum limit for vehicle financing is \$150,000. Also, a limit of \$250,000 per client for all loans with the company is set. Since November 2015, the company only offers loans at regular rates. The specialized credit program for the issue of loans with increased rates for a short term: October 2014 to November 2015.

The company monitors outstanding loans in order to reduce occasional losses incurred by loans in default and to promptly exercise our rights to the security. The company maintains collective provisions for losses that are anticipated though not yet identified in our lending portfolio. The collective provision varies based on the nature and composition of the loan portfolio. This variation is based on the amount of the assets, the loss in the event of default, the likelihood of default and the latency period. The latency period represents the period between the occurrence of events that generate loss and the time when the company is able to detect the loss. The company used historic data and external data to determine the loss in the event of default and the likelihood of default. The company can always consider different adjustment factors of the collective provision. These adjustment factors are intended to address shifts in the economic cycle, sensitivity related to the composition of the portfolio or the level of effectiveness of underwriting policies or recovery methods. The collective provision as of September 30, 2016, is \$482.285.

The company also maintains a specific provision for loans identified by management as being in default. A specific provision is a provision for a loan considered suspect, at its amortized cost. After analyzing each loan in default, the company recorded a specific provision of \$364.920. The company holds \$1.459.843 in doubtful assets; the loans composing these suspect assets were used to determine the specific provision.

Loan portfolio maturities as of September 30, 2016, are as follows (in millions of dollars):

	Mortgage loans	Consumer loans
Maturity in less than 1 yr	2.8	0.7
Maturity in 1 to 5 yrs	2.2	126.4
Maturity in 5 to 10 yrs	0.0	158.1

3.2 Market risk

The company is of the view that it is not exposed to market risk, as it is not exposed to the stock market. The company also deems that it is not exposed to foreign exchange risk, as these investments are in Canadian dollars. The company does not have any derivatives that may indirectly expose it to market risk.

3.3 Operational risk

This risk is related to business processes as well as legal and regulatory compliance issues. The risk of business processes refers to the risk of loss that may result from internal processes, people or systems that are inadequate or at fault, or external events. The legal and regulatory compliance risk stems from the failure to abide by laws, regulations or directives governing the company as well as the risk of loss resulting in failure to conform to a contract. Outsourcing risk also falls under the operational risks category.

In order to mitigate this risk, the company has implemented internal control procedures as well as a variety of policies and procedures to properly manage the company’s business. These policies and procedures include, but are not limited to, a business continuity plan, an employee code of professional conduct and policies on how to process complaints and settle disputes. The company also benefits from the expertise of a parent company in various fields, including legal services, human resource management and IT services. Internal control is carried out by the internal audit department of IAIFS, which carries out this function for all the companies in iA Financial Group.

iA Trust is a trademark and business name under which Industrial Alliance Trust Inc. operates.

Since March 2016, iA Trust has entrusted the administration of its automobile financing activities to CTL Corp. (“CTL”), a subsidiary of IAIFS. In October 2015, IAIFS acquired CTL, which specializes in untraditional automobile loans. During the implementation of this strategy, employees of the company responsible for automobile loan sales and operations were transferred to CTL. Compliance, governance and accounting tasks are, however, are still performed by company employees.

The company outsources other parts of its operations to the parent company for the management of various products. Outsourcing is governed by agreements detailing the operations and responsibilities of each party. The agreements provide for the annual production of a certificate of compliance, thereby enabling the company to ensure operations are performed in keeping with expectations and obligations.

iA Trust has entrusted the management of its portfolio to an external manager, Industrial Alliance Investment Management Inc. The portfolio is managed in accordance with the investment policy in force. The manager reports quarterly to the company’s investment committee on investments, portfolio performance, and investment policy compliance.

3.4 Structural interest rate risk in the banking book

For the company, this risk corresponds to the risk of non-matching of cash flows. The risk of non-matching is primarily present for term deposit products issued by iA Trust. In order to manage this risk, the company uses an immunization approach to market risk by setting up a process for matching cash flows from assets and liabilities. The company’s investment policy includes a match policy that is at the base of the investment strategy for term deposit liabilities. The manager reports to management monthly and at each Board meeting on financial flow matching.

To quantify the risk of structural interest rate in the banking portfolio, a report on changes in the portfolio value is drafted based on more than one scenario of various movements in the interest curve. The calculation is done by taking into account both demand deposits and term deposits. The result of the various interest rate variation scenarios shows that the match strategy in effect helps to adequately determine the structural interest rate risk in the banking portfolio.

The September 30, 2016 report showed that the worst-case scenario corresponded to an increase equivalent to 25 bps in the rate of interest. As well, the loss incurred in such a scenario would be \$227,000 or 12 bps caused by a greater drop in the value of the assets than that of sums deposited.

iA Trust is a trademark and business name under which Industrial Alliance Trust Inc. operates.

3.5 Concentration risk

Within the investment policy, the company has set up diversification measures to weight each asset class within benchmarks that establish the weight of each type of security based on its quality (credit rating) and a maximum per issuer. Therefore, with the exception of government issuers or issuers that benefit from an equivalent direct or indirect guarantee, the policy sets limits on the concentration of direct or guaranteed investments by a single borrower or related borrowers.

Regarding personal loans, the company does business with retail clients having no ties with loan holders other than having obtained a loan through a company-certified auto dealer. The credit risk management policy includes a limit of \$250,000 in loans per client. It also includes a limit for loans that can be underwritten through the same dealer.

3.6 Financing and liquidity risk

Financing risk is essentially managed by the daily management of cash flow, by maintaining a close match between the financial structure of assets and commitments for term deposits, as well as by maintaining a high level of quality and negotiability of portfolio investments. The company does not use deposit liabilities as a financing source.

The company's investment policy provides measures for the diversification of investment vehicles in order to protect it from liquidity risk. Thus, with the exception of Government of Canada securities or provincial securities, the company has set a limit per issuer. For Guaranteed Trust Fund investments, the securities used are:

- Short-term investment (excellent liquidity);
- Bonds (higher level of liquidity, given the focus on government securities);
- Mortgage and vehicle loans (low level of liquidity).

In sum, the company's strategy applies as follows:

- Matching asset and liability cash flows in order to plan term deposit needs
- Maintaining a money market percentage for each matching block (cash and short-term securities). A higher percentage is used for demand deposit matching blocks than for term deposits
- Presence of negotiable securities in each matching block, with the exception of the block corresponding to guaranteed deposit certificates (term deposits).
- Access to two lines of credit for emergency financing:
 - line of credit with a Canadian bank
 - line of credit with the parent company, IAIFS.
- Presence of negotiable securities for assets invested from capital. The investment policy provides a target whereby most bond securities are provincial government securities and securities that are guaranteed by provincial governments.

OSFI put two new liquidity risk control measures in place in 2015: liquidity coverage ratio (LCR) and net cumulative cash flow (NCCF). The company calculated these values, and the results show very low liquidity risk exposure.

As of September 30, 2016, the results for the measures were:

- Liquidity coverage ratio (LCR)

The company's result was 4,879% as of September 30, 2016, considerably exceeding the OSFI requirement of 100%. The company has a 150% liquidity risk tolerance in the risk appetite and tolerance statement adopted by the Board of Directors on November 15, 2016.

iA Trust is a trademark and business name under which Industrial Alliance Trust Inc. operates.

- Net cumulative cash flow (NCCF)

The second control measure put in place also shows that the company's liquidity risk is well in hand. As of September 30, 2016, the NCCF after three months was \$140 million.

Regarding the net cumulative cash flow, the company has set a target of a four-month survival horizon while OSFI requires three months.

3.7 Business/strategy risk

Business risk is the risk of the income generated by the company not covering operating costs.

Strategic risk is the risk arising from business plans and their inadequate implementation or the inability to make decisions, allocate resources or adapt to business environment changes.

For operations, the company's strategy applies the following measures to mitigate business/strategy risk.

- iA Trust aims mainly to extend the iA Group product range and facilitate access to products in order to complement, not compete with, other Group subsidiaries. It uses the functions, services and distribution network of the parent company, iAIFS, for its development.
- The company's activities are carried out exclusively for iA Group.
- A permanent team sees to the company's compliance, governance and accounting activities.
- A specialized team sees to automobile loans via a service agreement with CTL.
- The availability of the parent company's human and technical resources supports adequate operations management in compliance with the requirements to which the company is subject.
- New domains are developed with proper management of business and strategic risk in accordance with the principles stated above. As such, development will involve known distribution networks and use of the parent company's human and technical support.

3.8 Reputation risk

Reputation risk is the risk that a negative reputation, whether true or not, will cause a loss of customers, costly litigation and/or lost revenue.

As mentioned, the company is active mainly in two business segments—*Agency Services* and *Retail Banking*.

The exposure to reputation risk lies mainly with our business partners where iA Trust delegates to agents the administrative duties for which it is responsible. These business relations are subject to agreements between iA Trust and the agents, who are all subsidiary members of the iA Group. Outsourcing services to the iA Group subsidiaries rather than external partners mitigates risks and, as a result, facilitates sound risk management.

For agency services, iA Trust is the fiduciary for products in registered plans developed and distributed by our business partners. If there are negative effects from releasing these products, we believe that the product designer and distributor will be most affected by reputation risk.

iA Trust is a trademark and business name under which Industrial Alliance Trust Inc. operates.

Automobile loan and deposit (GIC) activities for retail clients may increase reputation risk. Nonetheless, we do not believe that we need to quantify this risk independently, since operational and strategic risks have already been calculated.

3.9 Securitization risk

The company does not carry out securitization for its portfolio. As a result, the company believes that this risk has been adequately identified and does not require capital.

3.10 Residual risk

Residual risk is the risk that exists beyond the bounds of risk control or after risk mitigation measures have been applied.

The company believes this risk to be low and to not require capital.

4. Compensation practices (Data as of December 31, 2016)

The company's senior managers include all directors and senior management executives (president, director of finance and director of compliance). The company does not have a separate compensation committee or the necessary resources to implement a functional plan for deferred compensation and performance-based compensation.

The president is a senior manager of the company's only shareholder, IAIFS. He is paid directly by IAIFS, based on criteria established by the latter from time to time; a set amount that is determined annually and corresponds to a portion of the president's total compensation is paid by the company to IAIFS. IAIFS also pays the annual bonus to the president; consequently, the composition of the bonus is the sole shareholder's responsibility. The president's total compensation is, however, comparable to that of a key executive position in other major financial institutions. The vice-president, director of finance and director of compliance are paid a base salary and an annual discretionary bonus to align their overall compensation with that of similar positions in the industry according to the evaluation of their position. This evaluation is based on their experience and responsibilities. Independent directors receive annual compensation, plus a stipend for each meeting they attend. The five independent directors received a total of \$85,913 in 2016 (\$74,750 in 2015).

The compensation of directors and key management personnel for the year was as follows:

	2015	2015
Salaries, professional fees and other short-term benefits	\$2,116,039	\$2,796,450
Total compensation of key management personnel	\$540,697	\$1,369,232



iA Trust is a trademark and business name under which Industrial Alliance Trust Inc. operates.