May 23, 2019

To: All Deposit-Taking Institutions (DTIs) Issuing Covered Bonds

Subject: Revised Covered Bond Limit Calculation

OSFI is updating the covered bond limit calculation that was last revised in December 2014. At that time we updated the denominator of the calculation as a result of replacing the Assets to Capital Multiple (ACM) with the Basel Leverage Ratio in Q1 2015. Since then, a number of revisions to the Capital Adequacy Requirements Guideline and Leverage Requirements Guideline have necessitated changes to the formula for the ACM proxy of total assets described in the December 2014 letter.

To improve the simplicity of the covered bond limit calculation, we are replacing the ACM proxy of total assets with on-balance sheet assets as reported on the regulatory balance sheet return (M4). We are also taking this opportunity to update the numerator of the calculation to better reflect the amount of assets encumbered through covered bonds by capturing the overcollateralization associated with these instruments. By definition, this amount will always be higher than the notional amount of covered bonds issued.

The intent of these updates is to neither increase nor decrease the covered bond issuance capacity for DTIs. However, to account for overcollateralization requirements associated with these instruments, the level of the covered bond limit needs to be higher than the current 4% level, which limited notional amounts of covered bonds outstanding. Going forward, total assets pledged by a DTI for covered bonds must not, at any time, represent more than 5.5% of the issuer's on-balance sheet assets.

Effective August 1, 2019, the covered bond ratio calculation will be as follows:

$$\frac{\text{Total assets pledged for covered bonds}}{\text{Total on-balance sheet assets}} \leq 5.5\%$$

Where:

Total assets pledged for covered bonds = Canadian dollar equivalent of covered bonds outstanding multiplied by the level of overcollateralization, as calculated as per section 4.3.8 of the Canadian Registered Covered Bond Programs Guide and reported in the monthly investors' reports.

Total on-balance sheet assets = Total Assets reported on the Consolidated Balance Sheet (M4) return (DPA 1045).

In addition, OSFI will continue to impose the following conditions:

1. The covered bond limit, as defined above, must be met on an on-going basis. If at any time, the 5.5% limit is exceeded, the DTI must notify OSFI in a timely manner. Excesses due to factors beyond the control of the issuing institution, such as foreign exchange fluctuations, will not require the DTI to take action to reduce the amount outstanding. For other excesses, the DTI must provide a plan to OSFI showing how the DTI proposes to eliminate the excess quickly.

2. OSFI expects pledging policies of DTIs to specifically take into account the issuance of covered bonds and the pledging of additional collateral to meet higher overcollateralization requirements, consistent with the limits and conditions contained in this letter.

Questions on the covered bond limit calculation can be sent to Mounia Chakak, Capital Division by email at mounia.chakak@osfi-bsif.gc.ca.

Yours truly,

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