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# Advisory

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**Category: Capital**

**NOTICE\***

**Subject: Aggregate Limit on Tier 1-qualifying Preferred Shares and Innovative Instruments**

**Date: January 2008**

This advisory, which applies to federally regulated entities (FREs)<sup>1</sup>, complements the following OSFI guidance:

- Guideline A and A-1, Capital Adequacy Requirements (CAR) Banks/T&L/BHC
- Guideline A, Minimum Continuing Capital and Surplus Requirements (MCCSR) Life
- Guideline A-2, Capital Regime for Regulated Insurance Holding Companies and Non-operating Life Companies
- April 2003 Advisory: Tier 1 Capital Clarifications
- June 2007 Advisory: Innovative Tier 1 and Other Capital Clarifications – Revised Version

In Principle 1 of the Appendix: *Principles Governing Inclusion of Innovative Instruments in Tier 1 Capital*, “common shareholder’s equity (i.e., common shares, retained earnings, and participating account surplus, as applicable) should be the predominant form of a FRFI’s tier 1 capital. A strongly capitalized FRFI should not have innovative instruments and perpetual non-cumulative preferred shares that, in aggregate, exceed 25% of its net tier 1 capital”.

After taking into account the fundamental characteristics of tier 1 capital and reviewing guidance in other jurisdictions, OSFI has decided to increase this limit to 30%. The maximum amount of innovative tier 1 instruments that can be included in the aggregate limit calculation continues to be 15% of net tier 1.

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<sup>1</sup> In this Advisory, the term FRE refers to bank holding companies, banks, federally regulated trust and loan companies, federally incorporated or regulated life insurance companies and insurance holding companies. The Advisory does not, however, apply to property and casualty insurance companies.



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References to 25% in the April 2003 Advisory *Tier 1 Capital Clarifications* are amended to 30%. In addition, section 2(b) of the advisory is replaced by the following:

Tier 1 qualifying preferred shares and innovative instruments, at the time of issuance, should not normally exceed 30% of net tier 1 capital<sup>2</sup>. A FRE that wishes to include excess preferred share amounts in tier 1 capital must obtain OSFI's prior confirmation that this treatment is acceptable. The FRE must provide a supportable plan, acceptable to OSFI, outlining how it proposes to eliminate the excess.

**- END -**

\* Advisories describe how OSFI administers and interprets provisions of existing legislation, regulations or guidelines, or provide OSFI's position regarding certain policy issues. Advisories are not law; readers should refer to the relevant provisions of the legislation, regulation or guideline, including any amendments that came into effect subsequent to the Advisory's publication, when considering the relevancy of the Advisory.

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<sup>2</sup> Net tier 1 capital is defined as Tier 1 capital available after deductions for goodwill etc., as set out in OSFI's MCCR or CAR Guideline, as applicable.