Reference: Guideline for Banks (D-SIBs)

June 25, 2018

To: Domestic Systemically Important Banks (D-SIBs)

Subject: Domestic Stability Buffer

OSFI is providing greater transparency to the market surrounding the Domestic Stability Buffer currently held by D-SIBs against Pillar 2 risks associated with systemic vulnerabilities. OSFI is of the view that increased transparency will support banks' ability to use this capital buffer in times of stress by increasing the market's understanding of the purpose of the buffer and how it should be used.

Purpose & Design

The Domestic Stability Buffer applies only to D-SIBs and is intended to cover a range of systemic vulnerabilities that, in OSFI's supervisory judgement, are not adequately captured in the Pillar 1 capital requirements described in OSFI's *Capital Adequacy Requirements* (CAR) Guideline. Decisions on the calibration of the buffer are based on supervisory judgement, informed by analytical work on a range of vulnerabilities, and are made in consultation with the Financial Institutions Supervisory Committee[1].

Calibration

The level of the buffer will range between 0 and 2.5% of a bank's total risk-weighted assets (RWA), calculated under the CAR Guideline. The level will be the same for all D-SIBs and must be met with Common Equity Tier 1 (CET1) capital only. The buffer is currently set at 1.5% of total RWA.

The specific vulnerabilities covered by the buffer are expected to evolve over time. The decision to include a vulnerability will be based on whether it is measureable, material, cyclical and has a system-wide impact that could materialize in the foreseeable future.

[1] Established under section 18 of the *OSFI Act*, the Financial Institutions Supervisory Committee consists of the Superintendent of Financial Institutions, the Commissioner of the Financial Consumer Agency of Canada, the Governor of the Bank of Canada, the Chief Executive Officer of the Canada Deposit Insurance Corporation, and the Deputy Minister of Finance.

The set of vulnerabilities currently addressed by the buffer include: (i) Canadian consumer indebtedness; (ii) asset imbalances in the Canadian market; and (iii) Canadian institutional indebtedness.

OSFI will undertake a review of the buffer on a semi-annual basis, in June and December, and any changes to the buffer will be made public, along with supporting rationale. In exceptional circumstances, OSFI may make and announce adjustments to the buffer in-between scheduled review dates. The first review will occur in December 2018.

Decreases of the buffer will occur when OSFI identifies that D-SIBs' exposures to the vulnerabilities have diminished. Increases to the buffer will occur when OSFI is of the view that it would be prudent for D-SIBs to hold additional capital to protect against the identified vulnerabilities. Increases will be subject to a phase-in period; decreases will be effective immediately.

Capital Planning & Supervisory Intervention

The Domestic Stability Buffer is not a Pillar 1 buffer and breaches will not result in banks being subject to automatic constraints on capital distributions. If a D-SIB breaches the buffer (i.e. dips into the buffer when it has not been released), OSFI will require a remediation plan. Supervisory interventions pursuant to OSFI's Guide to Intervention would occur in cases where a remediation plan is not produced or executed in a timely manner satisfactory to OSFI.

Banks should continue to take into account the Domestic Stability Buffer in their internal capital planning. The Domestic Stability Buffer supplements the Pillar 1 buffers (Capital Conservation Buffer, D-SIB surcharge and the Countercyclical Buffer) outlined in Chapter 1 of the CAR Guideline. Banks may also be required to hold additional Pillar 2 capital, as warranted, to address idiosyncratic risks.

Disclosure

Consistent with other capital related disclosures, D-SIBs should include the Domestic Stability Buffer as part of their quarterly public disclosures beginning in the reporting period ending July 31, 2018, and include a brief narrative on any changes to the buffer level. Breaches of the buffer by an individual bank will require public disclosure pursuant to IFRS standards.

Questions concerning the Domestic Stability Buffer can be sent to Catherine Girouard, Director, Capital Division by email at catherine.girouard@osfi-bsif.gc.ca.

Yours truly,

Carolyn Rogers
Assistant Superintendent
Regulation Sector