Letter

Title	Capital Adequacy Requirements Guideline (2027) – Letter
Category	Capital Adequacy Requirements
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Sector	Banks Trust and Loan Companies

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Today, we are publishing the Capital Adequacy Requirements (CAR) 2027 Guideline. This guideline will take effect on November 1, 2026 or January 1, 2027 for institutions with a fiscal year ending October 31 or December 31, respectively.

We appreciate the stakeholder engagement and feedback received during the consultation period.

We reflected several revisions in the final guideline in response to stakeholder feedback related to credit risk, securitization, and market risk. Many of these revisions align the final guideline with the policy intent of the draft guideline. Additionally, some revisions align the final guideline with current practice, including the application of the Credit Valuation Adjustment (CVA) alternative treatment as outlined in Chapter 8.

We are implementing a streamlined application and approval process for Small and Medium-sized Banks (SMSBs) interested in applying to use the internal-ratings based (IRB) approach to credit risk. Alongside changes to Chapter 1 and Chapter 5 of the CAR Guideline in this regard, we are releasing an updated version of the Assessment of Regulatory Capital Models for Deposit-Taking Institutions implementation note. We also consolidated the IRB implementation notes on data maintenance, risk quantification, collateral management principles, validating risk rating systems, use of ratings and estimates of default and loss, and oversight expectations into a single document for ease of reference.

Below is a summary of the key changes related to credit risk, securitization, and market risk.

Credit risk requirements

Corporate exposures

We lowered the capital requirements under both the Standardized Approach (SA) for credit risk and the IRB approach for Corporate small and medium-sized enterprise (SME) exposures. Under the credit risk SA, we lowered the risk weight applied to Corporate SME exposures to 75% from 85%. Under the IRB approach, we increased the firm-size adjustment for corporate SMEs from 4% to 6%.

We also lowered the risk weights under the credit risk SA for exposures to unrated non-investment grade corporates from 150% to 135%, and increased the maximum exposure threshold of small business entities (SBE) that can qualify for the lower regulatory retail risk weights from $1.5 million to $2.5 million.

Exposures to Canadian Systemically Important Banks and Domestic Systemically Important Financial Institutions

We reduced the risk weight for exposures to systemically important banks (SIBs) and to certain provincially regulated deposit-taking institutions designated by their provincial regulators as a domestic systemically important financial institution (D-SIFI), from 20% to 15%. These lower risk weights also apply to covered bonds issued by these institutions.

Land Acquisition, Development, and Construction exposures

We made several changes to the capital treatment of Land Acquisition, Development, and Construction (ADC) exposures under the credit risk SA to increase the granularity and risk sensitivity of the capital treatment. These include:

- Allowing institutions to consider ADC projects with loan-to-values (LTVs) lower than 80% as substantially complete and apply the income producing commercial real estate (IPCRE) treatment, when a certificate of occupancy has been issued.
- Introducing a preferential risk weight of 110% for commercial ADC loans with 50% pre-sales or pre-leases, up to an LTV of 70%.
- Lowering the base risk weight for low-rise residential real estate from 150% to 130% to better reflect the lower risk nature of low-rise residential builds.
- Introducing a 90% risk weight for residential ADC (both high and low-rise) where the level of pre-sales is equal to or greater than 75%.
- Clarifying the definition for equity at risk and updating the definition of high-rise buildings to seven stories or more.

- Modifying the pre-sale and pre-lease thresholds to reference the value of contracts rather than the number of contracts

Downturn Loss Given Default (LGD) floor

We revised the formula under the IRB approach for the Downturn Loss Given Default (LGD) floor add-on to the institution's long-run LGD estimate for exposures secured by residential real estate by:

- Removing the Supplementary Capital Requirement Indicators calculation for the 11 metropolitan areas mentioned in Appendix 5-3 of Chapter 5 of the CAR Guideline, and
- Modifying the add-on formula such that it no longer peaks at an 80% current LTV but continues to increase above an 80% current LTV.

Exposures risk-weighted at 1250%

For certain exposures that receive a 1250% risk weight (specifically certain securitization exposures, equity investment in funds, and first-to-default credit derivatives), we modified the guideline to allow institutions the option to deduct the exposure from Common Equity Tier 1 (CET1) instead of applying a 1250% risk weight.

Securitization exposures

We modified the guideline to require originating institutions to notify OSFI of all synthetic securitization transactions within 30 days of the transaction being executed. Originating institutions will also be required to submit certain specified information along with their notification. Finally, we specified that, should OSFI determine at any point that the securitization exposure does not qualify for treatment under the securitization framework, the institution will have to revert any capital benefits accrued by treating a transaction as a securitization exposure.

We revised the scope of the standardized risk weight ceiling of 75% under the simple, transparent and comparable (STC) securitization framework to apply only to regulatory retail exposures, rather than all retail assets.

We also made several clarifications, including to the treatment of re-tranched securitizations, specific allowances when securitization exposure amounts are deducted from CET1 capital, and when selection of a rating agency is considered 'cherry-picking.'

Use of ratings

We clarified that the applicable long-term ratings may be used for unrated short-term exposures to investment grade entities, subject to the conditions in the CAR Guideline for the use of ratings.

Commitments

Finally, we have clarified that commitments include arrangements that can be cancelled by the institution if a third party fails to meet conditions set out in the facility documentation prior to any initial or subsequent drawdown under the arrangement (such as a regulator failing to approve a merger and acquisition transaction). As a result, institutions should hold capital for these types of commitments as soon as the commitment is made and accepted, irrespective of pending regulatory approvals.

Market risk requirements

Sovereign exposures

We modified the scope of Chapter 9 to allow all sovereign, central bank, and public service entity exposures funded in local currency and held in a local subsidiary or branch to be assigned a 0.5% default risk weight if the national authority assigns a zero risk weight.

To support the functioning of sovereign debt markets and reduce competitive disadvantages for Canadian institutions operating as US primary dealers, we modified Chapter 9 to permit movement between the trading book and banking book for US Treasury positions originated from US primary dealer underwriting activity at the settlement date.

Credit spreads in market risk capital

We capped risk weights applied on short credit positions, such that the risk weight will be the lower of the prescribed risk weight and the market spread on the credit instrument.

Maturity assignments for cash equity positions in market risk capital

We will allow institutions the option of assigning the same maturity to the cash equity position as the maturity of the derivative contract it hedges, and any unmatched cash equity positions should be assigned a maturity of 12 months. Alternatively, institutions will have the option of continuing to apply the current method.

Updates to ongoing monitoring and approval requirements

We updated various monitoring and approval requirements throughout the market risk capital framework. Updates are intended to reduce regulatory burden by removing formal approval requirements, while ensuring that institutions provide relevant material to OSFI.

Please refer to the summary of stakeholder comments and our responses.

Questions can be sent to BCLSD-DNFPLB@osfi-bsif.gc.ca.