Guideline

Subject: Capital Adequacy Requirements (CAR)

Chapter 1 – Overview of risk-based capital requirements

Effective Date: November 2023 / January 2024

Note: For institutions with a fiscal year ending October 31 or December 31, respectively.

Subsections 485(1) and 949(1) of the *Bank Act* (BA), subsection 473(1) of the *Trust and Loan Companies Act* (TLCA) require banks (including federal credit unions), bank holding companies, federally regulated trust companies, and federally regulated loan companies to maintain adequate capital. The CAR Guideline is not made pursuant to subsections 485(2) or 949(2) of the BA, or to subsection 473(2) of the TLCA. However, the capital standards set out in this guideline together with the leverage requirements set out in the Leverage Requirements Guideline provide the framework within which the Superintendent assesses whether a bank, a bank holding company, a trust company, or a loan company maintains adequate capital pursuant to the Acts. For this purpose, the Superintendent has established two minimum standards: the leverage ratio described in the *Leverage Requirements Guideline*, and the risk-based capital ratio described in this guideline.[1] The first test provides an overall measure of the adequacy of an institution's capital. The second measure focuses on risk faced by the institution. Notwithstanding that a bank, bank holding company, trust company, or loan company may meet these standards, the Superintendent may direct a bank or bank holding company to increase its capital under subsections 485(3) or 949(3) of the BA, or a trust company or a loan company to increase its capital under subsection 473(3) of the TLCA.

OSFI, as a member of the Basel Committee on Banking Supervision, participated in the development of the Basel capital framework on which this guideline is based. Where relevant, the Basel framework paragraph numbers are provided in square brackets at the end of each paragraph referencing material from the Basel framework.

[1] The capital and leverage requirements for domestic systemically important banks are supplemented by the requirements described in OSFI's *Total Loss Absorbing Capacity (TLAC) Guideline*.

Chapter 1 - Overview of risk-based capital requirements

The Capital Adequacy Requirements (CAR) for banks (including federal credit unions), bank holding companies, federally regulated trust companies, and federally regulated loan companies are set out in nine chapters, each of which has been issued as a separate document. This document should be read in conjunction with the other CAR chapters. The complete list of CAR chapters is as follows:

Chapter 1	Overview of Risk-based Capital Requirements
Chapter 2	Definition of Capital
Chapter 3	Operational Risk
Chapter 4	Credit Risk – Standardized Approach
Chapter 5	Credit Risk – Internal Ratings-Based Approach
Chapter 6	Securitization
Chapter 7	Settlement and Counterparty Risk
Chapter 8	Credit Valuation Adjustment (CVA) Risk
Chapter 9	Market Risk

Table of Contents

Chapter 1 – Overview of Risk-based Capital Requirements

1. Outlined below is an overview of the capital adequacy requirements for banks (including federal credit unions), bank holding companies, federally regulated trust companies, and federally regulated loan companies, collectively referred to as 'institutions'.

2. This chapter is drawn from the Basel Committee on Banking Supervision (BCBS) Basel Framework published on the Bank for International Settlements (BIS) website.[2] For reference, the Basel paragraph numbers that are associated with the text appearing in this chapter are indicated in square brackets at the end of each paragraph.[3]

1. 1. Scope of Application

3. The capital adequacy requirements outlined in this guideline apply on a consolidated basis to the following institutions:

a. all institutions designated by OSFI as domestic systemically important banks (D-SIBs); and
b. small and medium-sized deposit-taking institutions (SMSBs[4]), which fall into Categories I, II or III as defined in OSFI's SMSB Capital and Liquidity Requirements Guideline.[5]

4. The consolidated entity includes all subsidiaries except insurance subsidiaries. OSFI expects institutions to hold capital within the consolidated group in a manner that is consistent with the level and location of risk.

1. 2. Regulatory Capital

5. Total capital consists of the sum of the following elements:

i. Tier 1 capital, consisting of:
    a. Common Equity Tier 1 (CET1) capital; and
    b. Additional Tier 1 capital
ii. Tier 2 capital

2 The Basel Framework
3 Following the format: [Basel Framework, XXX yy.zz]
4 SMSBs are banks (including federal credit unions), bank holding companies, federally regulated trust companies, and federally regulated loan companies that have not been designated by OSFI as domestic systemically important banks (D-SIBs). This includes subsidiaries of SMSBs or D-SIBs that are banks (including federal credit unions), federally regulated trust companies or federally regulated loan companies.
5 SMSB Capital and Liquidity Guideline

6. The criteria for the capital elements comprising the two tiers, as well as the various limits, restrictions and regulatory adjustments to which they are subject, are described in Chapter 2.

1. 3. Total Risk-weighted Assets

7. Risk-weighted assets (RWA) make up the denominator of the risk-based capital ratios, and is calculated as the higher of:

a. the sum of the following three elements:
   i. RWA for credit risk;
   ii. RWA for market risk; and
   iii. RWA for operational risk; and
b. the adjusted RWA determined as per the capital floor described in section 1.5.

[Basel Framework, RBC 20.4]

1.3.1. Credit Risk

8. RWA for credit risk (including counterparty credit risk) is calculated as the sum of:
   a. Credit RWA for banking book exposures which, except the RWA listed in (b) through (e) below, is calculated using:
      i. the standardized approach (as set out in Chapter 4); or
      ii. the Internal Ratings-Based (IRB) approach (as set out in Chapter 5).
   b. RWA for counterparty credit risk from banking book exposures and trading book exposures (as set out in Chapter 7), except the exposures listed in (c) and (f) below.
   c. Credit RWA for equity investments in funds that are held in the banking book calculated using one or more of the approaches set out in Chapter 4:
      i. The look-through approach
      ii. The mandate-based approach
      iii. The fall-back approach
   d. RWA for securitization exposures held in the banking book, calculating using one or more of the approaches set out in Chapter 6:
      i. Securitization Standardized Approach (SEC-SA)
      ii. Securitization External Ratings-Based Approach (SEC-ERBA)
      iii. Securitization Internal Ratings-Based Approach (SEC-IRBA)
      iv. Securitization Internal Assessment Approach (SEC-IAA)
      v. A risk weight of 1250% in cases where the institution cannot use (i) to (iv) above.

e. RWA for exposures to central counterparties in the banking book and trading book, calculated using the approach set out in Chapter 7.
f. RWA for the risk posed by unsettled transactions and failed trades, where the transactions are in the banking book or trading book and are within the scope of the rules set out in Chapter 7.
g. RWA for credit valuation adjustment (CVA) risk for exposures in the trading and banking book, calculated as set out in Chapter 8 using either:
    i. The standardized approach for CVA; or
    ii. The advanced approach for CVA.

[Basel Framework, RBC 20.6]

9. Institutions that have total regulatory capital (net of deductions) in excess of CAD $5 billion, or that have greater than 10% of total assets or greater than 10% of total liabilities that are international,[6] are expected to use IRB approaches for all material portfolios and credit businesses in Canada and the United States.

10. Under the IRB approaches, exposure at default (EAD) is determined gross of all specific allowances. The amount used in the calculation of EAD should normally be based on book value, except for the following where EAD should be based on amortized cost:

- loans fair valued under the fair value option or fair value hedge; and
- debt and loans fair valued through Other Comprehensive Income.

11. Under the standardized approach, on-balance sheet exposures should normally be measured at book value, except the following where exposures should be measured at amortized cost:

- loans fair valued under the fair value option or fair value hedge;
- debt and loans fair valued through Other Comprehensive Income; and
- own-use property, plant and equipment

12. For own-use property that is accounted for using the revaluation model, reported exposures should be based on an adjusted book value that reverses the impact of:

- the balance of any revaluation surplus included in Other Comprehensive Income; and
- accumulated net after-tax revaluation losses that are reflected in retained earnings or as a result of subsequent revaluations

13. The approaches listed in paragraph 8 specify how institutions should measure the size of their exposures (i.e. EAD) and determine their RWA. Certain types of transactions in the banking book and trading book (such as derivatives and securities financial transactions) give rise to counterparty credit risk, for which the measurement of the size of the exposure can be complex. Therefore, the approaches listed in paragraph 8 include, or cross refer to, the following methods available to determine the size of the counterparty exposures (refer to section 7.1 of Chapter 7 for an overview of the counterparty credit risk requirements including the types of transactions to which the methods below can be applied):

[6] This includes assets and liabilities booked outside of Canada as well as assets and liabilities of non-residents booked in Canada.

a. The standardized approach for measuring counterparty credit risk exposures (SA-CCR), set out in section 7.1.7.
b. The comprehensive approach, set out in section 4.3.3(iii) of Chapter 4.
c. The value at risk (VaR) models approach, set out in section 5.4.1(iii) of Chapter 5.
d. The Internal Model Method (IMM), set out in section 7.1.5.

[Basel Framework, RBC 20.7]

14. For banks with OSFI approval to use IMM to calculate counterparty credit risk exposures, EAD for counterparty credit risk exposures must be calculated according to sections 7.1.3 through 7.1.5. [Basel Framework, RBC 20.8]

1.3.2. Market Risk

15. Market risk requirements, as outlined in Chapter 9, apply to internationally active institutions and all institutions designated by OSFI as D-SIBs. OSFI retains the right to apply the framework to other institutions, on a case-by-case basis, if trading activities are a large proportion of overall operations.

16. Institutions subject to market risk requirements must identify the instruments that are in the trading book following the requirements of Chapter 9. All instruments that are not in the trading book and all other assets of the institution (termed "banking book exposures") must be treated under one of the credit risk approaches. [Basel Framework, RBC 20.5]

17. RWA for market risk are calculated as RWA for market risk for instruments in the trading book and for foreign exchange risk and commodities risk for exposures in the banking book, calculated using:

i. The standardized approach, as described in section 9.5; or

ii. The internal models approach set out in section 9.6.

[Basel Framework, RBC 20.9]

1.3.3. Operational Risk

18. All institutions are subject to operational risk requirements, as described in Chapter 3.

19. RWA for operational risk are calculated using either:
a. The Simplified Standardized Approach, set out in section 3.3; or
b. The Standardized Approach, set out in section 3.4.

20. D-SIBs and SMSBs that report adjusted gross income[7] greater than $1.5 billion must use the standardized approach. SMSBs with annual adjusted gross income less than $1.5 billion must use the simplified standardized approach, unless they have received approval from OSFI to use the standardized approach, as set out in section 3.2.

[7] Adjusted gross income is defined in section 3.3

1. 4. Approval to use Internal Model Based Approaches

21. Institutions must receive explicit prior approval from OSFI in order to use any of the following model-based approaches for regulatory capital purposes: the Foundation and Advanced IRB Approaches to credit risk, the IMM to counterparty credit risk, and the Internal Models Approach (IMA) to market risk. The steps involved in the application for approval of these approaches are outlined in OSFI Implementation Notes.

22. OSFI will consider approval with conditions for those institutions that have made a substantial effort and are found to satisfy most requirements of the internal model regime. The institution must also be able to provide out of sample back-testing and parallel reporting consistent with OSFI's capital models implementation note.[8] Institutions that do not receive approval will be required to employ a form of the Standardized Approach.

23. An institution achieving approval with conditions for one of the model-based approaches will normally be allowed to use the approach (in some cases only after OSFI confirms closure of certain deficiencies) but may be required to adhere to a higher initial capital floor. Once it achieves full compliance with all rollout and data requirements, and OSFI has agreed, the institution may proceed to the capital floor of 72.5% described in section 1.5. In either case, OSFI will not rule out the possibility of requiring floors on individual asset classes or reviewing approval conditions based on implementation progress.

24. Once approved, institutions are expected to meet the qualitative and quantitative requirements for the internal model approach as set out in the guideline and the supporting implementation notes on an ongoing basis.

1.4.1. Approval to use the IRB Approaches to Credit Risk

25. For IRB credit risk approval, besides meeting the qualitative and quantitative requirements for an IRB rating system, institutions will need, at a minimum, to satisfy the following requirements to obtain approval with conditions (with a possibly higher initial floor):

- The institution is meeting the IRB use test principles.[9] The use test prohibits institutions from using default and loss estimates from their own internal ratings that are developed for the sole purpose of calculating regulatory capital, these systems must be used in other operations of the institution.
- On implementation, the institution will have rolled out the Advanced IRB (AIRB) or Foundation IRB (FIRB) approach to approximately 80% of its consolidated credit exposures, as of the end of the fiscal year prior to the fiscal year in which the institution receives approval to use the IRB approach, measured in terms of gross exposure and total credit RWA.

[8] Implementation Note - Assessment of Regulatory Capital Models for Deposit-Taking Institutions

[9] The Use of Ratings and Estimates of Default and Loss at IRB Institutions – Implementation Note

26. Once an institution has received an approval to use the IRB Approach, OSFI will monitor, on a quarterly basis, the institution's compliance with the 80% IRB threshold for its consolidated credit exposures for which an IRB approach is permitted. In the post-approval period, compliance will be measured in terms of gross exposure and total credit risk-weighted assets as at the applicable quarter.

1. 5. Capital Floor–Internal Model Based Approaches

27. To reduce excessive variability of RWA and to enhance the comparability of risk-based capital ratios, institutions using internal model-based approaches for credit risk, counterparty credit risk, or market risk are subject to a floor requirement that is applied to RWA. The capital floor ensures that institutions' capital requirements do not fall below a certain percentage of capital requirements derived under standardized approaches. The calculation of the floor is set out below for institutions that have implemented the IRB approach for credit risk, IMM for counterparty credit risk, or IMA for market risk. Institutions that have only implemented the standardized approaches for credit risk, counterparty credit risk, and market risk are not subject to the capital floor.

Institutions that have implemented one of the internal model-based approaches for credit risk, counterparty credit risk, or market risk must calculate the difference between:

i. the capital floor as defined in section 1.5.1, and

ii. an adjusted capital requirement as defined in section 1.5.2.

[Basel Framework, RBC 20.11]

28. If the capital floor amount is larger than the adjusted capital requirement (i.e. the difference is positive), institutions are required to add the difference to the total RWAs otherwise calculated under this guideline. This adjusted RWA figure must be used as the denominator in the calculation of the risk-based capital ratios.

1.5.1. The Capital Floor

29. The base of the capital floor includes the standardized approaches to credit risk and operational risk as described in paragraphs 31 through 35. The specific approach for market risk is described in paragraph 33. The capital floor is derived by applying an adjustment factor to the net total of the following amounts:

i. total risk-weighted assets for the capital floor, less

ii. 12.5 times the amount of any general allowance that may be recognized in Tier 2 capital following the standardized approach methodology as outlined in Chapter 2 of this guideline.

30. The adjustment factor is normally set at 72.5%. However, OSFI may set a higher or lower adjustment factor for individual institutions. This factor will be phased-in over three years, starting at a 65% factor in 2023 and rising 2.5% per year to 72.5% in 2026.

Table 1: Capital Floor Transition				
Fiscal year				
	2023	**2024**	**2025**	**2026 +**
Floor adjustment factor	65%	67.5%	70%	72.5%

31. Credit risk RWAs are calculated using the standardized approach as outlined in Chapter 4 of this guideline for all asset classes except securitization. The treatment of securitization exposures under the capital floor is outlined in section 6.11 of Chapter 6. Credit risk RWAs also include charges for central counterparty (CCP) exposures and non-Delivery-versus-Payment (DvP) trades outlined in Chapter 7, and credit valuation adjustment (CVA) outlined in Chapter 8 of this guideline.

32. For the exposure values used in the calculation of credit risk RWAs, the treatment of credit risk mitigation should follow the standardized approach outlined in section 4.3 of Chapter 4 of this guideline, while counterparty credit risk exposures must be determined using the standardized approach to counterparty credit risk outlined in section 7.1.7 of Chapter 7 of this guideline. Additionally, in order to reduce the operational complexity of implementing the capital floor, institutions may choose to apply the IRB definition of default for IRB portfolios rather than applying the standardized approach default definition.

33. Prior to November 2023/January 2024,[10] market risk RWAs are calculated using the value at risk (VaR) and standardized approaches as outlined in Chapter 9 of the 2019 CAR guideline, excluding the comprehensive risk measure (CRM, section 9.11.5.2), the incremental risk charge (IRC, Appendix 9-9), and stressed VaR (SVaR, paragraph 194i) capital charges. After November 2023/January2024, market risk RWAs are calculated using the standardized approach as outlined in Chapter 9 of this guideline.

34. Operational risk RWAs are calculated using either the Standardized Approach or the Simplified Standardized Approach, outlined in Chapter 3 of this guideline.

35. The following approaches are not permitted to be used, directly or indirectly, in the calculation of the capital floor:

a. IRB approach to credit risk;
b. SEC-IRBA;
c. the IMA for market risk;
d. the VaR models approach to counterparty credit risk; and

[10] For institutions with a fiscal year ending October 31 or December 31, respectively.

e. the IMM for counterparty credit risk.[11]

[Basel Framework, RBC 20.12]

1.5.2. Adjusted Capital Requirement

36. The adjusted capital requirement is based on application of all of the chapters of this guideline and is equal to the net total of the following amounts:

i. total risk-weighted assets, plus

ii. 12.5 times the provisioning shortfall deduction, less

iii. 12.5 times excess provisions included in Tier 2, less

iv. 12.5 times the amount of general allowances that may be recognized in Tier 2 in respect of exposures for which the standardized approach is used.

37. The provisioning shortfall deduction, excess provisions included in Tier 2, and general allowances in Tier 2 in respect of standardized portfolios are defined in section 2.1.3.7 of Chapter 2 of this guideline.

1. 6. Calculation of OSFI Minimum Capital Requirements

1.6.1. Risk-Based Capital Ratios for D-SIBs and Category I and II SMSBs

38. Institutions are expected to meet minimum risk-based capital requirements for exposures to credit risk, operational risk and, where they have significant trading activity, market risk. Total risk-weighted assets are determined by multiplying the capital requirements for market risk and operational risk by 12.5 and adding the resulting figures to risk-weighted assets for credit risk. The capital ratios are calculated by dividing regulatory capital by total risk-weighted assets. The three ratios measure CET1, Tier 1 and Total capital adequacy and are calculated as follows:

$$\textbf{\textit{Risk Based Capital Ratios}} = \frac{Capital}{RWA}$$

Where:

Capital = CET1, Tier 1, or Total capital as set out in Chapter 2.

RWA = Risk-weighted assets, calculated as described in paragraph 7.

39. Table 2 provides the minimum CET1, Tier 1 and Total capital ratios for institutions before application of the capital conservation buffer.

[11] There are two exceptions to this rule. One is that banks who have approval to use the IMM and who are currently using the Standardized CVA (S-CVA) approach are permitted to use the IMM EADs and maturities in the calculation of the S-CVA for purposes of the capital floor. The other is that banks currently using the Advanced CVA (A-CVA) approach for purposes of the capital floor may continue to do so. Both of these exceptions expire when the revised CVA framework is implemented in the first fiscal quarter of 2024.

Table 2: Minimum capital requirements (in RWA)	
CET1	4.5%
Tier 1	6.0%
Total	8.0%

1.6.2. Simplified Risk-Based Capital Ratio for Category III SMSBs

40. Category III SMSBs are subject to a Simplified Risk-Based Capital Ratio (SRBCR), calculated as follows:

$$\boldsymbol{SRBCR} = \frac{Capital}{Adjusted\ Total\ Assets + \boldsymbol{RWA_{Operational\ Risk}}}$$

Where:

Capital = CET1, Tier 1, or Total capital as set out in Chapter 2.

Adjusted Total Assets = Total Assets from the Balance Sheet, less the aggregate of all adjustments to regulatory capital as set out in Chapter 2.

RWA $_{\text{Operational Risk}}$ = Risk-Weighted Assets for operational risk, calculated as detailed in Chapter 3.

41. Table 3 provides the minimum CET1, Tier 1 and Total capital ratios for Category III SMSBs before application of the capital conservation buffer.

Table 3: Minimum Capital Requirements (measured as SRBCR)	
CET1	4.5%
Tier 1	6.0%
Total	**8.0%**

1. 7. Mandated Capital Buffers

42. In addition to the minimum capital ratios, institutions are required to hold a capital conservation buffer and, where applicable, a countercyclical buffer.

43. Outside of periods of stress, institutions should hold buffers of capital above the regulatory minimum. The intent of these buffers is to increase institutions' resilience going into a downturn and provide a mechanism for rebuilding capital during the early stages of economic recovery. Retaining a greater proportion of earnings during a downturn will help to ensure that capital becomes available to support the ongoing business operations of institutions through periods of stress. [Basel Framework, RBC 30.20]

44. When buffers have been drawn down, there is a range of actions that can be taken to rebuild buffers including reducing discretionary distributions of earnings. This could include reducing dividends or other discretionary payments on shares or other capital instruments, share buy-backs and, to the extent they are discretionary, staff bonus payments.[12] Institutions may also choose to raise new capital from the private sector as an alternative to conserving internally generated capital. Should buffers be drawn down, institutions should implement a capital restoration plan for rebuilding buffers within a reasonable timeframe or, where the breach is expected to be corrected promptly, a plan that provides assurance that the capital conservation buffer will be restored on a sustained basis. The capital restoration plan should be discussed with OSFI as part of the capital planning process. [Basel Framework, RBC 30.21]

45. Greater efforts should be made to rebuild buffers the more they have been depleted. In the absence of raising capital in the private sector, the share of earnings retained by institutions for the purpose of rebuilding capital buffers should increase the nearer their actual capital levels are to the minimum capital requirements. [Basel Framework, RBC 30.22]

46. It is not acceptable for institutions which have depleted their capital buffers to use future predictions of recovery as justification for maintaining generous distributions to shareholders, other capital providers and employees. These stakeholders, rather than depositors, must bear the risk that recovery will not be forthcoming. It is also not acceptable for institutions that have depleted their capital buffers to use the distribution of capital as a way to signal their financial strength. [Basel Framework, RBC 30.23]

1.7.1. Capital Conservation Buffer

47. The capital conservation buffer establishes a safeguard above the minimum capital requirements and can only be met with CET1 capital. The capital conservation buffer is 2.5% of RWA.[13] Table 4 provides the minimum capital ratios plus the 2.5% capital conversation buffer. [Basel Framework, RBC 30.2]

Table 4: Capital conservation buffer (as % of RWA)	
Capital conservation buffer	2.5%
Minimum capital ratios plus the 2.5% capital conservation buffer	
CET1	7.0%
Tier 1	8.5%
Total	**10.5%**

48. Capital distribution constraints will be imposed on an institution when capital levels fall within the buffer conservation range. Institutions will be able to conduct business as normal when their capital levels fall within the buffer range as they experience losses. The constraints imposed

[12] Applies only to performance bonuses issued to institutions' senior management. The term "senior management" is defined in OSFI's *Corporate Governance Guideline*.

[13] For Category III SMSBs, the capital conservation buffer is 2.5% of [Adjusted Total Assets + $RWA_{\text{Operational Risk}}$]

relate only to distributions, not the operations of the institution. The distribution constraints increase as institutions' capital levels approach the minimum requirements. By design, the constraints imposed on institutions with capital levels at the top of the range would be minimal. This reflects an expectation that institutions' capital levels may fall into this range from time to time. [Basel Framework, RBC 30.2 and 30.3]

49. Table 5 sets out the minimum capital conservation ratios an institution must meet at various levels of CET1 capital.[14] The applicable conservation ratio must be recalculated at each distribution date. Once imposed, conservation ratios will remain in place until such time as capital ratios have been restored. If an institution wants to make payments in excess of the constraints set out in Table 5, sufficient capital must be raised in the private sector to fully compensate for the excess distribution. This alternative should be discussed with OSFI as part of an institution's Internal Capital Adequacy Assessment Process (ICAAP). For the purposes of determining the minimum capital conservation ratio, the CET1 ratio includes amounts used to meet the 4.5% minimum CET1 requirement, but excludes any additional CET1 needed to meet the 6% Tier 1 and 8% Total Capital requirements, as well as any CET1 capital needed to meet D-SIBs' Total Loss Absorbing Capacity (TLAC) requirements where applicable. For example, an institution with 8% CET1 and no Additional Tier 1 or Tier 2 capital would meet all minimum capital requirements, but would have a 0% capital conservation buffer and therefore be subject to the 100% constraint on capital distributions. [Basel Framework, RBC 30.4]

Table 5: Minimum capital conservation ratios for corresponding levels of CET1

CET1 Ratio	Minimum Capital Conservation Ratios (expressed as percentage of earnings)
4.5% - 5.125%	100%
>5.125% - 5.75%	80%
>5.75% - 6.375%	60%
>6.375% - 7.0%	40%
>7.0%	0%

50. If an institution's capital ratio falls below the levels set out in Table 4, capital conservation ratios will be imposed that automatically limit distributions. As outlined in Table 5, these limits increase as an institution's capital levels approach the minimum requirements. For example, an institution with a CET1 capital ratio in the range of 5.125% to 5.75% would be required to maintain the equivalent of 80% of its earnings in the subsequent payment period (i.e. pay out no more than 20% in capital distributions). For clarity, where an institution's disclosed ratio is within the ranges where restrictions apply, distributions for the following payment period will be constrained based on the most recently reported ratio irrespective of the current capital position of the institution. Restrictions will remain in place until the capital conservation buffer is restored. [Basel Framework, RBC 30.4]

[14] Similar capital conservation ratios apply where an institution breaches its Tier 1 capital or Total capital requirements. In the event that an institution simultaneously breaches more than one capital requirement (e.g. 7% CET1, 8.5% Tier 1, 10.5% Total capital) it must apply the most constraining capital conservation ratio.

51. Items considered to be distributions include dividends and share buybacks, discretionary payments on CET1 and Additional Tier 1 capital instruments and discretionary bonus payments to staff. Payments that do not result in a depletion of CET1, which may for example include certain stock dividends, are not considered distributions. The distribution restrictions do not apply to dividends which satisfy all of the following conditions:

(a) the dividends cannot legally be cancelled by the institution;
(b) the dividends have already been removed from CET1; and
(c) the dividends were declared in accordance with the applicable capital conservation ratio set out in Table 5 at the time of the declaration.

[Basel Framework, RBC 30.5]

52. Earnings are defined as distributable profits calculated prior to the deduction of elements subject to the restriction on distributions. Earnings are calculated after the tax which would have been reported had none of the distributable items been paid. As such, any tax impacts of making such distributions are reversed out. Where an institution does not have positive earnings and has a shortfall in its CET1, Tier 1, or Total Capital ratio, it will be restricted from making positive net distributions. [Basel Framework, RBC 30.5]

1.7.2. Countercyclical Buffer

53. The countercyclical buffer aims to ensure that banking sector capital requirements take account of the macro-financial environment in which institutions operate. It will be deployed when excess aggregate credit growth is judged to be associated with a build-up of system-wide risk to ensure the banking system has a buffer of capital to protect it against future potential losses. [Basel Framework, RBC 30.7]

54. The countercyclical buffer regime consists, in Canada, of the following elements:

(a) OSFI, in consultation with its Senior Advisory Committee[15] (SAC) partners, will monitor credit growth and other indicators[16] that may signal a build-up of system-wide risks[17] and make an assessment of whether credit growth is excessive and is leading to the build-up of system-wide risks. Based on this assessment, a countercyclical buffer requirement, ranging from 0% to 2.5% of total risk-weighted assets,[18] will be put in place when

[15] SAC is a non-statutory body chaired by the Deputy Minister of Finance. Its membership is the same as the Financial Institutions Supervisory Committee ("FISC"), i.e. OSFI, the Department of Finance, the Bank of Canada, the Canada Deposit Insurance Corporation, and the Financial Consumer Agency of Canada. The SAC operates as a consultative body and provides a forum for policy discussion on issues pertaining to the financial sector.

[16] The document entitled *Guidance for national authorities operating the countercyclical capital buffer*, sets out the principles that national authorities have agreed to follow in making buffer decisions. This document provides information that should help institutions to understand and anticipate the buffer decisions made by national authorities in the jurisdictions to which they have credit exposures. [BCBS Consolidated framework RBC 30.10]

[17] The Bank of Canada will be the primary source of public information on macro-financial developments and the state of vulnerabilities in Canada with regard to the countercyclical buffer, including as published in its Financial System Review (FSR).

[18] For Category III SMSBs, the countercyclical buffer requirement would be applied as a % of [Adjusted Total Assets + $RWA_{\text{Operational Risk}}$]

circumstances warrant. This requirement will be released when OSFI, in consultation with its SAC partners, assesses that system-wide risks have dissipated or crystallized.

(b) Institutions with private sector credit exposures outside Canada will look at the geographic location of those exposures and calculate their consolidated countercyclical buffer requirement as a weighted average of the countercyclical buffers that are being applied in jurisdictions to which they have credit exposures.

(c) The countercyclical buffer to which the institution is subject will be implemented by way of an extension of the capital conservation buffer described in section 1.7.1. Institutions will be subject to restrictions on distributions of earnings if they breach the extended buffer.
[Basel Framework, RBC 30.8]

55. Institutions must meet the countercyclical buffer with CET1. Consistent with the capital conservation buffer, the CET1 ratio in this context includes amounts used to meet the 4.5% minimum CET1 requirement, but excludes any additional CET1 needed to meet the 6% Tier 1 and 8% Total Capital requirements as well as D-SIBs' minimum 21.5% TLAC requirement. [Basel Framework, RBC 30.17]

56. Table 6 provides the minimum capital conservation ratios an institution must meet at various levels of the CET1 capital ratio.[19] [Basel Framework, RBC 30.17]

Table 6: Individual institution minimum capital conservation standards

CET1	Minimum Capital Conservation Ratios (expressed as a percentage of earnings)
Within first quartile of buffer	100%
Within second quartile of buffer	80%
Within third quartile of buffer	60%
Within fourth quartile of buffer	40%
Above top of buffer	0%

57. The consolidated countercyclical buffer will be a weighted average of the buffers deployed in Canada and across BCBS member jurisdictions and selected non-member jurisdictions[20] to which the institution has private sector credit exposures. [Basel Framework, RBC 30.14]

58. Institutions will look at the geographic location of their private sector credit exposures and calculate their consolidated countercyclical buffer as a weighted average of the buffers that are being applied in each jurisdiction to which they have such exposures. The buffer that will

[19] Similar constraints apply with respect to breaches of Tier 1 capital and Total capital requirements. Institutions should apply the most constraining capital conservation ratio where they breach more than one requirement.

[20] Institutions are expected to reciprocate the buffers implemented by every jurisdiction listed on the dedicated page of the BIS website: Countercyclical capital buffer (CCyB). Reciprocity is mandatory, for all Basel Committee member jurisdictions, up to a maximum of 2.5% RWA, irrespective of whether host authorities require a higher add-on. [BCBS Consolidated framework RBC 30.13 FAQ3 and FAQ4]

apply to an institution will thus reflect the geographic composition of its portfolio of private sector credit exposures.[21] [Basel Framework, RBC 30.13]

59. The weighting applied to the buffer in place in each jurisdiction will be the institution's credit risk RWA that relates to private sector credit exposures in that jurisdiction divided by the institution's credit risk RWA that relates to private sector credit exposures across all jurisdictions.[22] [Basel Framework, RBC 30.14]

60. Institutions will be subject to a consolidated countercyclical buffer that varies between 0%, where no jurisdiction in which the institution has private sector credit exposures has activated a buffer, and 2.5% of total RWA.[23] The consolidated countercyclical buffer applies to consolidated total RWA (including credit, market, and operational risk) as used in the calculation of all risk-based capital ratios, consistent with it being an extension of the capital conservation buffer. [Basel Framework, RBC 30.12 FAQ1]

61. Private sector credit exposures in this context refers to exposures to private sector counterparties, including non-bank financial sector counterparties, which attract a credit risk capital charge in the banking book and the risk-weighted equivalent trading book capital charges for specific risk, the incremental risk charge, and securitization. Interbank exposures and exposures to the public sector are excluded. [Basel Framework, RBC 30.13 FAQ1]

62. When considering the jurisdiction to which a private sector credit exposure relates, institutions should use an ultimate risk basis. Ultimate risk refers to the jurisdiction where the final risk lies[24] as opposed to the jurisdiction of the immediate counterparties or where the exposure is booked. [Basel Framework, RBC 30.14]

63. The decision to activate, increase, decrease or release the countercyclical buffer will be formally communicated. The Superintendent may exempt groups of institutions, other than D-SIBs and foreign bank subsidiaries in Canada, from the countercyclical buffer requirements if the

[21] The geographic location of an institution's private sector exposures is determined by the location of the counterparties that make up the capital charge irrespective of the institution's own physical location or its country of incorporation. The location is identified according to the concept of ultimate risk (i.e. based on the country where the final risk lies, not where the exposure has been booked). The geographic location identifies the jurisdiction whose announced countercyclical buffer add-on is to be applied by the institution to the corresponding credit exposure, appropriately weighted. [BCBS Consolidated framework RBC 30.13 FAQ2 and 30.14 FAQ1]

[22] For Category III SMSBs, the weighting will be based on the institution's private sector credit exposures in a particular jurisdiction divided by its total private sector credit exposures across all jurisdictions.

[23] For Category III SMSBs, the consolidated countercyclical buffer requirement would be applied as a % of [Adjusted Total Assets + RWA $_{\text{Operational Risk}}$].

[24] For purposes of determining the country of residence of the ultimate obligor, guarantees and credit derivatives are considered but not collateral with the exception of exposures where the lender looks primarily to the revenues generated by the collateral, both as the source of repayment and as security for the exposure, such as *Project Finance*. The location of a securitization exposure is the location of the underlying obligor or, where the exposures are located in more than one jurisdiction, the institution can allocate the exposure to the country with the largest aggregate unpaid principal balance.

application would not meet the stated objectives of the countercyclical buffer.[25] [26] The scope of application and the rationale would be described in the OSFI communication. To give institutions time to adjust to a buffer level, OSFI will pre-announce its decision, to activate or raise the level of the countercyclical buffer, by up to 12 months but no less than 6 months. Conversely, decisions to release the countercyclical buffer will normally take effect immediately. Institutions with foreign exposures are expected to match host jurisdictions' implementation timelines unless the announcement period is shorter than 6 months in which case compliance will only be required 6 months after the host's announcement.[27] [Basel Framework, RBC 30.11]

64. The maximum countercyclical buffer relating to foreign private sector credit exposures will be 2.5% of total RWAs.[28] Jurisdictions may choose to implement a buffer in excess of 2.5%, if deemed appropriate in their national context; in such cases the international reciprocity provisions will not apply to the additional amounts. In addition, institutions are not expected to replicate sectoral buffers or similar measures adopted by foreign jurisdictions that depart from the internationally agreed countercyclical buffer. [Basel Framework, RBC 30.9] Institutions must ensure that their countercyclical buffer is calculated and publicly disclosed with at least the same frequency as their minimum capital requirements. In addition, when disclosing their buffers, if any, institutions must also disclose the geographic breakdown of their private sector credit exposures used in the calculation of the buffer. [Basel Framework, RBC 30.19]

1. 8. Domestic Systemically Important Bank (D-SIB) Surcharge

65. OSFI has designated six Canadian institutions as D-SIBs: Bank of Montreal, Bank of Nova Scotia, Canadian Imperial Bank of Commerce, National Bank of Canada, Royal Bank of Canada, and Toronto-Dominion Bank.[29] D-SIBs will be subject to a CET1 surcharge equal to 1% of RWAs. The 1% capital surcharge will be periodically reviewed in light of national and international developments. This is consistent with the levels and timing set out in the BCBS D-SIB framework. [BCBS Consolidated framework RBC 40.7 to 40.23]

66. The 1% surcharge will be implemented through an extension of the capital conservation buffer. This is in line with the treatment of the higher loss absorbency requirement for global systemically important banks (G-SIBs) prescribed by the BCBS.[30] Table 7 below sets out the minimum capital conservation ratios a D-SIB must meet at various CET1 capital ratios and Tier 1 leverage ratios.[31] D-SIBs will thus be subject to a pre-determined set of restrictions on the

[25] The Superintendent will consider factors such as whether an institution's business model involves providing credit through intermediation of funds or whether the conditions that give rise to financial system-wide issues are explicitly addressed in a robust manner in the institution's internal capital targets.

[26] The countercyclical buffer is to be computed and applied at the consolidated FRFI parent level, i.e. OSFI regulated deposit-taking institutions who are subsidiaries of an OSFI regulated deposit-taking institution are not subject to the countercyclical buffer.

[27] The pre-announced buffer decision and actual buffer in place will be published on the BIS website.

[28] For Category III SMSBs, the countercyclical buffer would be applied as a % of [Adjusted Total Assets + RWA $_{\text{Operational Risk}}$].

[29] Annex 1 contains additional details around OSFI's process for designating Canadian institutions as D-SIBs.

[30] BCBS Consolidated framework RBC 40.1 to 40.6

[31] Similar capital conservation ratios apply where a D-SIB breaches its Tier 1 capital or Total capital requirements. In the event that a D-SIB simultaneously breaches more than one capital requirement (e.g. 8% CET1, 9.5% Tier 1, 11.5% Total Capital) it must apply the most constraining capital conservation ratio.

ability to make distributions, such as dividends and share buy-backs, if they do not meet these requirements (see relevant provisions of section 1.7.1).

Table 7: Minimum capital conservation ratios for D-SIBs at various ranges of CET1 or Tier 1 Leverage Ratios

CET1 Ratio	Tier 1 Leverage Ratio	Minimum Capital Conservation Ratio
4.5% - 5.375%	3%–3.125%	100%
>5.375% - 6.250%	> 3.125%–3.25%	80%
>6.250% - 7.125%	> 3.25%–3.375%	60%
>7.125% - 8.0%	> 3.375%–3.50%	40%
>8.0%	> 3.50%	0%

1. 9. Domestic Stability Buffer

67. In addition to the buffers described in sections 1.7.1, 1.7.2, and 1.8, D-SIBs are subject to a Domestic Stability Buffer (DSB).[32] The DSB 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 this guideline. In addition to the DSB, D-SIBs may be required to hold further Pillar II capital, as warranted, to address idiosyncratic or systemic risks that are not adequately captured by the Pillar I requirements and buffers. Decisions on the calibration of the DSB 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 (FISC).[33]

68. The level of the DSB will range between 0 and 4.0% of a D-SIB's total RWA calculated under this guideline. The level of the DSB will be the same for all D-SIBs and must be met with CET1 capital.

69. Unlike the other buffers described in this guideline, the DSB is not a Pillar 1 buffer and breaches will not result in D-SIBs being subject to the automatic constraints on capital distributions described in section 1.7. 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*[34] would occur in cases where a remediation plan is not produced or executed in a timely manner satisfactory to OSFI.

[32] Details related to the OSFI's DSB are included on OSFI's website: Domestic Stability Buffer

[33] 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.

[34] Guide to Intervention for Federally Regulated Deposit-Taking Institutions

70. D-SIBs should take into account the DSB in their internal capital planning process. Additionally, D-SIBs should report the DSB in their quarterly public disclosures, and include a brief narrative on any changes to the buffer level. Breaches of the buffer by an individual D-SIB will require public disclosure pursuant to International Financial Reporting Standards (IFRS).

71. The specific vulnerabilities covered by the DSB are expected to evolve over time, as they are based on current market conditions in combination with forward-looking expectations around the materialization of risks to key vulnerabilities, and will be communicated as part of the semi-annual DSB level-setting announcements. The decision to include a vulnerability will be based on whether it is measurable, material, cyclical and has a system-wide impact that could materialize in the foreseeable future.

72. OSFI will undertake a review of the buffer on a semi-annual basis, and any changes to the buffer will be made public, in June and December, along with supporting rationale. In exceptional circumstances, OSFI may make and announce adjustments to the buffer in-between scheduled review dates. Transparency in setting the DSB will support institutions' ability to use this capital in times of stress by improving the understanding of the purpose of the buffer and how it should be used.

73. Decreases of the buffer may occur in a situation when OSFI identifies that D-SIBs' exposures to the vulnerabilities have diminished or that risks have materialized. In the latter case, a decrease would be intended to allow D-SIBs to continue to provide loans and services to credit worthy households and businesses and/or to incur losses without breaching their capital targets. Increases to the buffer may 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.

1. 10. Capital Targets

74. In addition to the minimum capital requirements described in section 1.6, OSFI expects all institutions to maintain target capital ratios equal to or greater than the minimum capital ratios plus the conservation buffer.[35] For SMSBs, this means target ratios of at least 7% for CET1, 8.5% for Tier 1 and 10.5% for Total capital. D-SIBs are expected to maintain target capital ratios equal to or greater than the minimum capital ratios plus the sum of the conservation buffer, the D-SIB surcharge and the DSB. For D-SIBs, this equates to target ratios of least 8% for CET1, 9.5% for Tier 1, and 11.5% for Total capital *plus* the DSB.[36] The target capital ratios for SMSBs and D-SIBs are summarized below in Table 8 below and illustrated in Annex 2.

[35] The conservation buffer is the sum of the 2.5% capital conservation buffer plus any countercyclical buffer add-ons, where applicable.

[36] As an example, where the DSB is set to 2% of RWA, D-SIBs' target capital ratios would be at least 10% for CET1, 11.5% for Tier 1 and 13.5% for Total capital. This reflects a conservation buffer of 2.5% and a D-SIB surcharge of 1.0%.

Table 8: Target Capital Ratios		
	SMSBs	**D-SIBs**
Target CET1 capital	7.0%	8.0% *plus* DSB
Target Tier 1 capital	8.5%	9.5% *plus* DSB
Target Total capital	10.5%	11.5% *plus* DSB

75. These targets are applicable to all institutions and are triggers for supervisory intervention consistent with OSFI's *Guide to Intervention*.[37] If an institution is offside the relevant target ratios, supervisory action will be taken proportional to the shortfall and circumstances that caused the shortfall and may include a range of actions, including, but not limited to, restrictions on distributions.

76. The Superintendent may set higher target capital ratios for individual institutions or groups of institutions where circumstances warrant, including in respect of idiosyncratic and/or systemic risks that are not adequately captured by institutions' Pillar I capital requirements and buffers. The need for Pillar II capital and corresponding higher target capital ratios would consider how robust existing capital ratios are in light of an institution's allowances, stress testing program, and ICAAP results.[38]

[37] *Guide to Intervention for Federally Regulated Deposit-Taking Institutions*

[38] For OSFI's expectations refer to Guideline E-18: Stress Testing and Guideline E-19: Internal Capital Adequacy Assessment Process (ICAAP).

Annex 1 Domestic Systemic Importance and Capital Targets

1. The framework[39] for dealing with D-SIBs set out by the BCBS indicates that domestic systemic importance should be assessed with reference to the impact that an institution's failure could have on the domestic economy. Further, it notes that this assessment should consider institution-specific characteristics of systemic importance, such as size, inter-connectedness and substitutability, which are correlated with the systemic impact of failure. Accordingly, OSFI's assessment of domestic systemic importance for Canadian institutions considers a range of indicators such as asset size, intra-financial claims and liabilities, and an institution's roles in domestic financial markets and in financial infrastructures. This section describes OSFI's inferences from various measures of systemic importance.

Size

2. In general, an institution's distress or failure is more likely to damage the Canadian financial system or economy if its activities comprise a large share of domestic banking activity. When Canadian institutions are compared according to their size as measured by total consolidated assets, and by place of booking of assets, that is, according to whether the assets are booked in Canada or abroad, the data show that:

- the largest six banks account for more than 90% total banking assets;
- the differences among the largest banks are smaller if only domestic assets are considered; and
- relative systemic importance declines rapidly after the top five banks and after the sixth bank.

Inter-connections

3. The more inter-connected an institution is to other financial institutions, the greater is the potential for the failure of that institution to transmit problems throughout the financial system and to the broader economy. As a result, measurements of inter-connectedness also inform institutions' systemic importance. Comparing Canadian institutions according to measures of intra-financial assets (i.e. claims on other financial institutions) and intra-financial liabilities (i.e. obligations to other financial institutions) again points to the dominance of the largest Canadian banks. The rank-ordering among these banks, however, depends on the specific inter-connectedness measure under consideration.

Substitutability

4. The systemic impact of an institution's distress or failure is greater the less easily it can be replaced as both a market participant and a financial service provider. As a result, OSFI's identification of D-SIBs also takes into account the types of roles that institutions play in domestic financial markets and in domestic financial infrastructures, which inform views regarding substitutability. For example, this includes underwriter rankings in Canadian financial

[39] A framework for dealing with domestic systemically important banks (BCBS: October 2012)

markets, and an institution's shares of Canadian dollar payments made through Canada's Large Value Transfer System (LVTS) and the Automated Clearing and Settlement System (ACSS).[40] Again, activity and volume in both LVTS and ACSS are dominated by the largest Canadian banks, and bank relative importance varies according to the measure of interest. The largest banks are also the dominant participants in CDSX, the clearing and settlement system for securities transactions in Canada. Some large Canadian banks also play key roles as members of the CLS Bank, the global institution that settles foreign exchange transactions between banks in Canadian dollars and other major currencies.[41] For example, the Royal Bank of Canada and the Canadian Imperial Bank of Commerce are the key Canadian-dollar liquidity providers for settling Canadian dollar foreign exchange transactions through the CLS network.

5. A variety of additional information has been assessed and recurring themes across the range of evidence are the following:

- The five largest banks are by far the dominant banks in Canada, and consistently play central roles in a range of activities in the Canadian financial system; and
- The rank-order importance of the largest banks, as well as the relative differences between them, varies somewhat according to the measure considered.

6. This suggests that there are strong grounds for treating these banks in the same way, rather than relying on arbitrary weights to develop a single index of systemic importance. Further, distinguishing reliably between the adverse effects on the Canadian economy from individual D-SIB failures is largely moot, given the difficulty of credibly differentiating between the large adverse impacts on the Canadian economy from the failure of any one of the largest banks. This also argues against making distinctions between identified Canadian D-SIBs to assign degrees of systemic importance.

7. Given these various considerations, the Canadian D-SIBs are judged to be Bank of Montreal, The Bank of Nova Scotia, Canadian Imperial Bank of Commerce, Royal Bank of Canada, and The Toronto-Dominion Bank, without further distinction between them. National Bank of Canada has also been designated as a D-SIB given its importance relative to other less prominent banks and in the interest of prudence given the inherent challenges in identifying ahead of time which banks are likely to be systemic in times of stress. The designation of D-SIB status will be periodically reviewed and updated as needed.

Higher Loss Absorbency Targets

8. The goal of a higher loss absorbency target is to reduce further the probability of failure of a D-SIB relative to non-systemic institutions, reflecting the greater impact that a D-SIB failure may have on the domestic financial system and the economy. This surcharge takes into account the structure of the Canadian financial system, the importance of large banks to the financial architecture, and the expanded regulatory toolkit required to resolve a troubled financial

[40] ACSS handles all Canadian dollar payments not processed by the LVTS.

[41] CLS Bank provides a real-time global network that links a number of national payments systems to settle the foreign exchange transactions of its member banks

institution. The BCBS D-SIB framework provides for national discretion to accommodate characteristics of the domestic financial system and other local features, including the domestic policy framework. The additional capital surcharge for banks designated as systemically important provides credible additional loss absorbency given:

- extreme loss events as a percentage of RWA among this peer group over the past 25 years would be less than the combination of the CET1 (2.5%) capital conservation buffer and an additional 1%; and
- current business models of the six largest banks are generally less exposed to the fat tailed risks associated with investment banking than some international peers, and the six largest banks have a greater reliance on retail funding models compared to wholesale funding than some international peers – features that proved beneficial in light of the experience of the 2008-2009 financial crisis.

From a forward-looking perspective:

- Canadian D-SIBs that hold capital at current targets plus a 1% surcharge (i.e. 8%) should be able to weather a wide range of severe but plausible shocks without becoming non-viable; and
- the higher loss absorbency in a crisis scenario achieved by the conversion to common equity) of the 2% to 3% in Additional Tier 1 and Tier 2 NVCC capital instruments promoted by Basel III also adds to the resiliency of banks.

Relationship with Basel Committee G-SIB Framework

9. OSFI has adopted the Basel Committee's framework on the assessment methodology for G-SIBs. The assessment methodology for G-SIBs follows an indicator-based approach agreed by the BCBS that will determine which institutions are to be designated as G-SIBs and subject to additional loss absorbency requirements that range from 1% to 3.5% RWA, depending on an institution's global systemic importance.[42] For Canadian D-SIBs that are also designated as G-SIBs, the higher of the D-SIB and G-SIB surcharges will apply.[43]

Supervisory Implications

10. Canadian D-SIBs are expected to have advanced practices in terms of the design and operation of oversight functions and internal controls. OSFI expects these practices to continue to improve as supervision becomes more intensive and international best practices evolve. The institutions designated as D-SIBs have historically had, and will continue to be subject to, more intensive supervision because of their larger size, broader and more complex business models and consequently more significant risk profiles. The principles of risk based supervisory intensity are reflected in OSFI's Supervisory Framework.[44] The Framework is applied on a consolidated basis to all Canadian institutions and requires OSFI supervisors to determine the

[42] BCBS Consolidated framework RBC 40.1 to 40.6 and SCO 40.1 to 50.20

[43] Details related to G-SIB's annual public disclosure requirements are included in OSFI's Global Systemically Important Banks – Public Disclosure Requirements Advisory

[44] OSFI's Supervisory Framework (OSFI: February 2011)

level, extent and intensity of the supervision of institutions based on the size, nature, complexity and risk profile of the institution. OSFI's enhanced supervision of D-SIBs includes the following:

- extensive use of supervisory colleges to share and coordinate supervision, including the execution of supervisory plans, with the relevant host country authorities of Canadian D-SIBs' major foreign subsidiaries and affiliates;
- greater frequency and intensity of on- and off-site monitoring of institutions' risk management activities and corporate governance, including more granular reporting to OSFI and more structured interactions with boards and senior management;
- more extensive use of specialist expertise relating to credit risk, market risk, operational risk, corporate governance, and AML/compliance;
- stronger control expectations for important businesses, including the use of 'advanced' approaches credit, market and operational risks;
- greater use of cross-institution reviews, both domestically and internationally, in order to confirm the use of good risk management, corporate governance and disclosure practices;
- selective use of external reviews to benchmark leading risk-control practices, especially for instances where best practices may reside outside Canada;
- regular use of stress tests to inform capital and liquidity assessments;
- setting, monitoring, and enforcing minimum and target TLAC ratios as set out in OSFI's *TLAC Guideline*; and
- assessing D-SIBs' recovery and resolution plans, as well as discussion of such plans with FISC partners and at crisis management groups.[45]

Information Disclosure Practices

11. Canadian D-SIBs are expected to have public information disclosure practices covering their financial condition and risk management activities that are among the best of their international peers.[46] Enhanced disclosure of institutions' risk models and risk management practices can play a helpful role in enhancing market confidence. As a result, D-SIBs are expected to adopt the recommendations of the Financial Stability Board's (FSB) Enhanced Disclosure Task Force,[47] future disclosure recommendations in the banking arena that are endorsed by international standard setters and the FSB, as well as evolving domestic and international bank risk disclosure best practices.

---

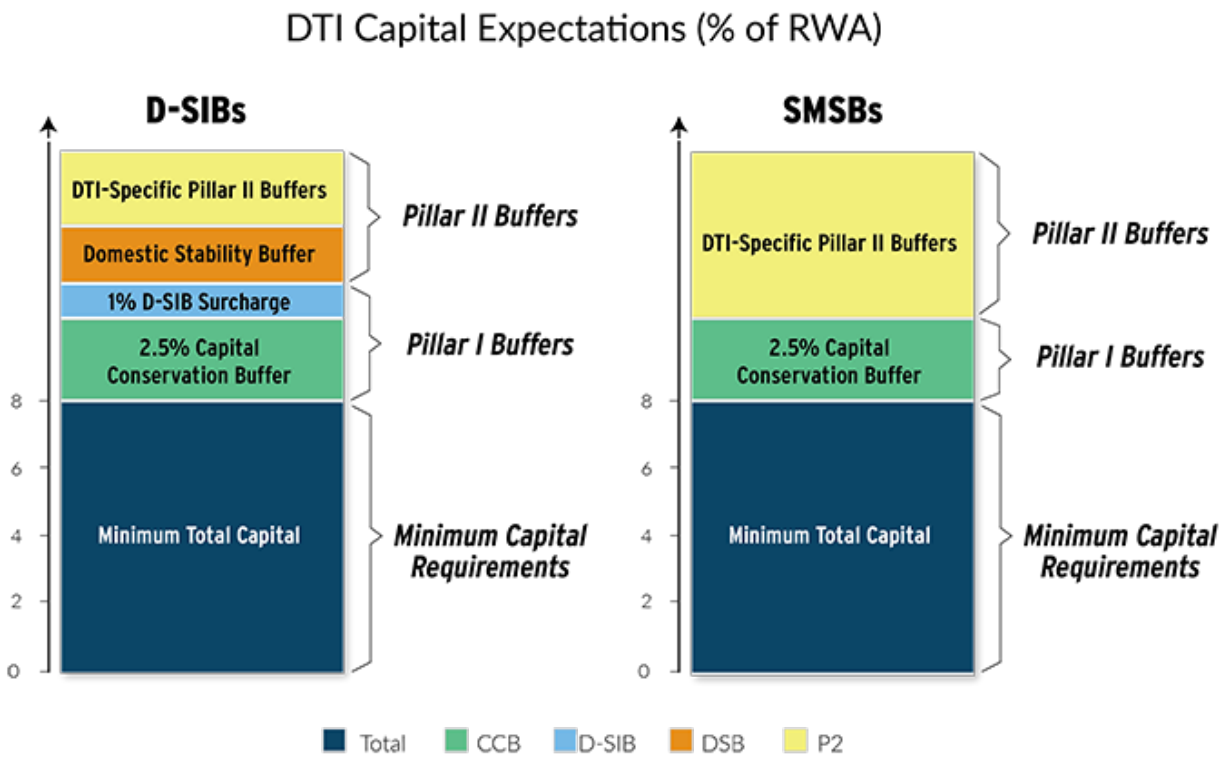
[45] Consistent with the Financial Stability Board's *Key Attributes of Effective Resolution Regimes for Systemically Important Financial Institutions*. OSFI is responsible for leading the assessment of recovery plans. The Canada Deposit Insurance Corporation is responsible for leading the assessment of resolution plans.

[46] OSFI's Pillar 3 Disclosure Guideline for D-SIBs: this guideline provides expectations for the domestic implementation of all three phases of the Pillar 3 Framework.

[47] Enhancing the Risk Disclosures of Banks (FSB: October 2012).

Annex 2 Supervisory Target Capital Requirements

Figure 1



Notes:

i. The size of DTI-specific Pillar II buffers will vary by institution as they are determined by each institution.

ii. Where applicable, the size of institutions' Countercyclical Buffer add-ons will vary.

iii. Calibration of the DSB is reviewed by OSFI semi-annually and is set between 0% to 4.0% of RWA.

iv. For Category III SMSBs, the DTI capital expectations in the chart are as a % of [Adjusted Total Assets + RWA Operational Risk]