CANADIAN BANKERS ASSOCIATION

Focus: Global Banking Regulations and Banks in Canada

Focus Sheet

FAST FACTS

- During the 2007/08 global financial crisis, unlike banks in many other countries, no Canadian banks were bailed out or in danger of failing. Similarly, Canadian banks remained resilient during the failure of three U.S. institutions in early 2023.
- The 2007/08 crisis resulted in a series of significant regulatory changes for the international banking sector. Regulators are also considering the implications of the recent demise of the three U.S. institutions.

The Bottom Line

The World Economic Forum has consistently ranked Canada's banks as among the soundest in the world. Canada's prudent banks, combined with effective regulation and supervision, form a model of stability in the global financial system.

Significant regulatory change continues

During the 2007/08 global financial crisis there was significant turmoil in the global financial system and a number of banks in other countries became insolvent and either failed or received taxpayer-funded bailouts. However, no Canadian bank was in danger of failing or needed a government bailout.

Canadian banks also remained resilient in the midst of market uncertainty caused by the failure of three U.S. institutions.

Canada's banks were well-capitalized, well-managed, and well-regulated going into the global financial crisis, and remain so to this day, During the pandemic, Canada's

What is Basel III?

Basel III was developed and agreed to by members of the Basel Committee on Banking Supervision (BCBS). This is a longstanding committee of the Bank for International Settlements (BIS) that is mandated to review and develop banking guidelines and supervisory standards at a global level.

Basel III is a framework that sets out global regulatory rules for bank capital and liquidity. These rules were originally published in December 2010 in response to the global financial crisis and are subject to ongoing review and updates. In December 2017, the BCBS issued some notable updates entitled '*Basel III: Finalising post-crisis reforms*'.

The phase-in of Basel III capital rules began in 2013. Canada implemented these changes in January 2013, well ahead of many other countries and well ahead of the Basel III timeline. The phase-in of Basel III's liquidity rules began in 2015. Canada began implementation of the Basel III reforms in April 2023 with the final elements of the reforms implemented in November 2023.

For more information, go to [bis.org](bis.org).

banks also played a critical role in supporting the Canadian economy and the financial well-being of Canadians and demonstrated their ongoing resiliency.

While banks in Canada are extremely unlikely to fail, Canadian banks have developed "recovery and resolution plans" that would help the bank recover from financial distress or bring about an orderly resolution in the event of their failure.

However, the global financial crisis led to a series of significant regulatory changes to international banking rules, which are designed to reduce the risk of another financial crisis occurring. While these rules are developed internationally, it is up to domestic regulators to put them in place and enforce them.

There are many important participants – including Canadian policymakers and regulators – involved in shaping and adapting these regulatory changes for Canada's financial system. [See Table of Main Participants below.]

The most significant changes to global banking rules have been in the areas of capital and liquidity. Both the quantity and quality of capital – which helps banks absorb losses – have been increased. In addition, new liquidity requirements have been put in place to help ensure that banks can meet their financial obligations, even in times of stress.

Financial markets are globally integrated. So, in the end, the aim is that consistent implementation of these regulatory changes in countries around the world will result in a better functioning global financial system.

Banks in Canada – through and with the Canadian Bankers Association – are working closely with domestic and global regulatory organizations to implement all of these international regulatory changes.

Regulatory Changes

The most significant changes to global banking rules have occurred in the area of capital and liquidity. These changes are described in greater detail below.

1. Capital

“Capital” is the money that bank owners have invested in the bank through the purchase of shares or is generated by the bank in the form of retained earnings. A bank holds capital to help protect depositors and other stakeholders against losses in the event that a borrower defaults. Capital is a cushion against the negative impacts of bank-specific and market-related activities that could jeopardize a bank’s ability to stay solvent and continue to serve Canadians.

Basel III capital rules

- There are several categories of rules related to capital under Basel III. Taken together, these rules now require Canadian banks to hold enough capital to equal at least 10.5% of their total risk-weighted assets.

Global and domestic systemically important banks

- In 2013, the Office of the Superintendent of Financial Institutions (OSFI) named the six largest banks in Canada as “domestic systemically important banks” (D-SIBs). As a result, these six banks are required to hold an additional one per cent of capital as of January 1, 2016 (D-SIB surcharge), and are also subject to a Domestic Stability Buffer (DSB) that ranges from 0 to 4.0 per cent of capital along with more intense supervision and enhanced disclosure requirements. The current level of the DSB is 3.5%.

- The Royal Bank of Canada and Toronto-Dominion Bank were designated by the Financial Stability Board as "global systemically important banks" (G-SIBs) in 2017 and 2019 respectively, but are not subject to any additional capital requirement beyond the existing D-SIB surcharge and DSB.
- The G-SIBs and D-SIBs are treated the same by OSFI given the potential impacts that a failure of any one of them would have on global and domestic economies.
- For small and mid-sized banks, OSFI has developed proportional capital and liquidity requirements reflecting the more limited systemic risk associated with smaller financial institutions.

Basel III capital rules as they relate to banks in Canada

- The Capital Adequacy Requirements (CAR) - Guideline reflects how OSFI is implementing the Basel III capital rules in Canada. In December 2012, OSFI issued a revised CAR Guideline to incorporate earlier Basel III reforms and made further updates in subsequent years. OSFI began implementing the latest version of the Basel III reforms in April 2023 with the final elements of the reforms implemented in November 2023 via the CAR Guideline.
- Under the CAR Guideline, OSFI already expects banks to meet target capital levels that equal or exceed the 2019 Basel III minimum capital requirements.

Under a separate Leverage Requirements - Guideline, OSFI expects institutions to maintain a leverage ratio that meets or exceeds 3 per cent at all times. OSFI also prescribes authorized leverage ratio requirements for individual institutions.

2. Liquidity

"Liquidity" refers to the ease with which assets can be converted into cash (i.e., liquidated) and sold. For banks, good liquidity is important because it bolsters their resilience to internal and external shocks.

Basel III liquidity rules

- The Basel Committee on Banking Supervision (BCBS) has developed two minimum rules for liquidity – the Liquidity Coverage Ratio (LCR) that has a 30-day horizon, and the Net Stable Funding Ratio (NSFR) that has a time horizon of one year. Both metrics have now been fully implemented in Canada, and were updated as of April 2023 with the Basel III reforms

- The LCR rules are meant to ensure banks have sufficient, high-quality liquid assets to withstand a period of economic stress.

How OSFI is implementing liquidity rules for banks in Canada

- OSFI issued a revised Liquidity Principles Guideline B6 and updated the liquidity metrics (e.g. LCR/NSFR) for the Basel III reforms in the Changes to the Liquidity Adequacy Requirements Guideline that was implemented in April 2022. These guidelines describe how the regulator assesses the strength of a bank's liquidity risk management framework and whether the bank would have adequate liquidity under stressed conditions.

3. New forms of risk

Banks and regulators around the world, including OSFI, are now shifting focus towards new and evolving forms of risks in relation to technological innovation and climate change.

- OSFI continues to evolve its regulatory and supervisory approach as part of its strategic goal to improve banks' preparedness for, and resiliency to, non-financial risks. In doing so, OSFI recognizes the importance of banks providing innovative financial services to Canadians while also fostering trust and confidence in the financial sector.

- In 2020, as part of its work on non-financial risks, OSFI sought feedback through a discussion paper on a broad range of issues related to technology risk. In 2022 ,OSFI subsequently issued a new Guideline B-13, Technology and Cyber Risk Management and in 2023 OSFI issued a revised Guideline B-10, Third-Party Risk Management.

- In March 2023, OSFI issued Guideline B-15 on Climate Risk Management that addresses governance and risk management expectations, as well as climate-related financial disclosures. More recently, OSFI began consulting on a Standardized Climate Scenario Exercise (SCSE).

- As part of its work on non-financial risk, OSFI is also seeking feedback from the industry on the incorporation of the BCBS' principles for operational resilience and the revised principles on operational risk management into domestic guidance. The OSFI revised Guideline E-21, Operational Resilience and Operational Risk Management is expected to be finalized in 2024.

4. Other notable developments

- OSFI issued a new Integrity and Security Guideline in January 2024 under its expanded mandate from the federal government to supervise financial institutions to determine that they have adequate policies and procedures to protect themselves against threats to integrity and security, including foreign interference.

- Key milestones:
  i. July 31, 2024 – Submit a comprehensive action plan for OSFI's review, on new and expanded expectations, which includes interim deliverables to achieve compliance.
  ii. January 31, 2025 - Observe all new or expanded expectations except on background checks.
  iii. July 31, 2025 - Observe new expectations on background checks.

Table of Main Participants

A number of organizations are involved in aspects of the regulatory changes underway. The table outlines the main participants and their role(s) in global regulations as it pertains to banks in Canada.

NAME OF PARTICIPANT	ROLE(S) IN REGULATION
Global	
Bank for International Settlements (BIS)	Swiss-based organization of which many central banks – including Canada's – are members. BIS and its committees lead much of the global regulatory work stemming from the global financial crisis. BIS was created in 1930. bis.org
Basel Committee on Banking Supervision (BCBS)	The BCBS is one of the committees of the BIS. It is the global standard setter for the prudential regulation of banks. Its mandate is to strengthen the regulation, supervision and practices of

	banks worldwide with the purpose of enhancing financial stability. Basel Committee members include OSFI and the Bank of Canada. The Basel Committee was established in 1974. bis.org/bcbs
Financial Stability Board (FSB)	Global group created by the G20 countries in 2009 to monitor and make recommendations about the global financial system. The FSB coordinates the work of national authorities and international standard setters (such as the BCBS) and develops policies to enhance financial stability. Canadian FSB members include the Department of Finance, Bank of Canada, and OSFI. fsb.org
Domestic	
Office of the Superintendent of Financial Institutions (OSFI)	The prudential regulator of Canadian banks and other federally regulated financial institutions. Also responsible for implementing Basel Committee principles and guidance in Canada. osfi-bsif.gc.ca
Bank of Canada	Canada's central bank, responsible for setting monetary policy and promoting a stable and

	efficient financial system. bankofcanada.ca
Department of Finance	Responsible for the legislative framework governing banks and other federally regulated financial institutions in Canada. canada.ca/en/department-finance.html
Canada Deposit Insurance Corporation (CDIC)	CDIC is a federal Crown corporation created by Parliament in 1967 to protect deposits made with member financial institutions in case of their failure. CDIC insures deposits of up to $100,000. CDIC also oversees bank resolution planning and has the authority to intervene in a failing institution. cdic.ca

1 “Leverage Requirements Guideline”, October 2014
2 “Basel III: The Liquidity Coverage Ratio and liquidity risk monitoring tools”, January 2013, www.bis.org
3 “Basel III: The Net Stable Funding Ratio”, October 2014; and “Basel III International framework for liquidity risk measurement, standards and monitoring”, December 2010, bis.org

The Canadian Bankers Association is the voice of more than 60 domestic and foreign banks that help drive Canada’s economic growth and prosperity. The CBA advocates for public policies that contribute to a sound, thriving banking system to ensure Canadians can succeed in their financial goals.

Canadian Bankers Association **www.cba.ca**

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