



February 14, 2012

**By Mail**

Mr. Joe Morin  
Chair  
Canadian Bond Investors' Association  
39 River Street  
Toronto, ON M5A 3P1

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Dear Mr. Morin:

**Subject: Non-Viability Contingent Capital**

Julie Dickson asked me to respond to your letter dated January 23, 2012 in which you expressed the concerns of the Canadian Bond Investors' Association (CBIA) in respect of non-viability contingent capital (NVCC) as well as other potential changes to the regulation of financial institutions in Canada.

OSFI is a member of the Basel Committee on Banking Supervision (BCBS) and has participated in the development of the Basel 3 framework<sup>1</sup>, including the NVCC requirements.<sup>2</sup> In addition, all BCBS member countries, including Canada, agreed to implement Basel 3, including the NVCC requirements, on January 1, 2013 subject to the transitioning of certain elements of the framework by 2019 and the phase-out of non-qualifying capital instruments by 2023.

Given the importance of these reforms and OSFI's ongoing commitment to keep market participants informed of pending changes to the regulatory landscape for Canadian financial institutions, we issued a letter<sup>3</sup> to the industry on February 1, 2011 setting out our plans for implementing Basel 3. The NVCC Advisory issued in August 2011 is part of those plans and was the product of more than eighteen months of informal and formal consultations with market participants, including investors, rating agencies, tax and legal professionals, and financial institutions. The rationale for this approach was to ensure the final NVCC requirements consider the diverse perspectives of all stakeholders while ensuring Canada meets its Basel 3 obligations. The early release of the Advisory last August was also intended to give prospective issuers

<sup>1</sup> *Basel III: A global regulatory framework for more resilient banks and banking systems* and *Basel III: International framework for liquidity risk measurement, standards and monitoring* published by the BCBS on 16 December 2010 and amended on 1 June 2011.

<sup>2</sup> *Minimum requirements to ensure loss absorbency at the point of non-viability* published by the BCBS on 13 January 2011

<sup>3</sup> OSFI Letter dated February 1, 2011. *Basel III Implementation – Capital Adequacy and Liquidity Requirements* ([http://www.osfi-bsif.gc.ca/app/DocRepository/1/eng/guidelines/capital/advisories/cptlq\\_e.pdf](http://www.osfi-bsif.gc.ca/app/DocRepository/1/eng/guidelines/capital/advisories/cptlq_e.pdf))



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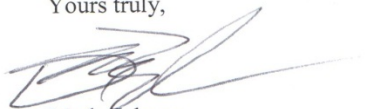
sufficient time to construct marketable NVCC instruments and to address impediments to their issuance. To further enhance investors' awareness and understanding of the NVCC requirements, OSFI also participated in several sessions over the last few months, which enabled us to clarify various technical issues, respond to questions, and to better understand investors' perspectives and concerns.

It is also important to note that, while the NVCC Advisory enables financial institutions to issue NVCC in advance of the January 1, 2013 implementation date mandated by the BCBS, it does not require them to do so. Furthermore, institutions also have the flexibility to meet their tier 1 and total capital requirements under Basel 3 with common equity only and, as such, they are not required to issue NVCC to satisfy any regulatory requirements. Notwithstanding this, where an institution opts to issue non-common capital to satisfy its capital requirements on or after January 1, 2013, such capital must satisfy the BCBS' NVCC requirements as implemented in Canada.

As the CBIA correctly points out, the NVCC requirements are just one piece of the regulatory roadmap. OSFI appreciates the desire of market participants to understand the full regulatory roadmap for Canadian financial institutions so that they can take informed business and investment decisions. However, given that Canadian financial institutions are generally recognized to be in a strong financial condition, our priority is to finalize the capital requirements on a going-concern basis, meaning the appropriate level of common equity Tier 1 capital that should be held by federally-regulated deposit-taking institutions, bearing in mind actions being taken by other jurisdictions in this area. In addition, we are also very busy focusing on the implementation of other Basel 3 requirements, including the NVCC requirements, in accordance with the prescribed timeline. We will turn our attention to other going-concern capital requirements, such as bail-in debt instruments, after this work has been completed. While this work is ongoing, please be assured that OSFI and other federal agencies are cognizant of the potential relationships between these policy streams and we are working diligently to ensure that the market has adequate opportunity to provide input on and prepare for any major changes to the regulatory landscape.

In closing, I wish to express OSFI's appreciation for the efforts the CBIA is making to represent the interest of fixed income investors in Canada. I'd also like to reiterate OSFI's commitment to maintaining an open dialogue with all market participants. As such, OSFI strongly encourages the CBIA and other market participants to continue monitoring domestic and international regulatory developments affecting financial institutions and to share your views with us.

Yours truly,



Mark Zelmer  
Assistant Superintendent, Regulation Sector