

# Capital Modernization

## Information Session – What We Heard

June 26, 2024

**BCFSA** BC Financial  
Services Authority

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səl'ílwətaʔt (Tsleil-Waututh Nation)

# Speakers

## JF TREMBLAY

Senior Vice  
President,  
Supervision &  
Deposit Insurance

## DERRICK LAU

Vice President,  
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## REBECCA LOWREY

Director, Reporting  
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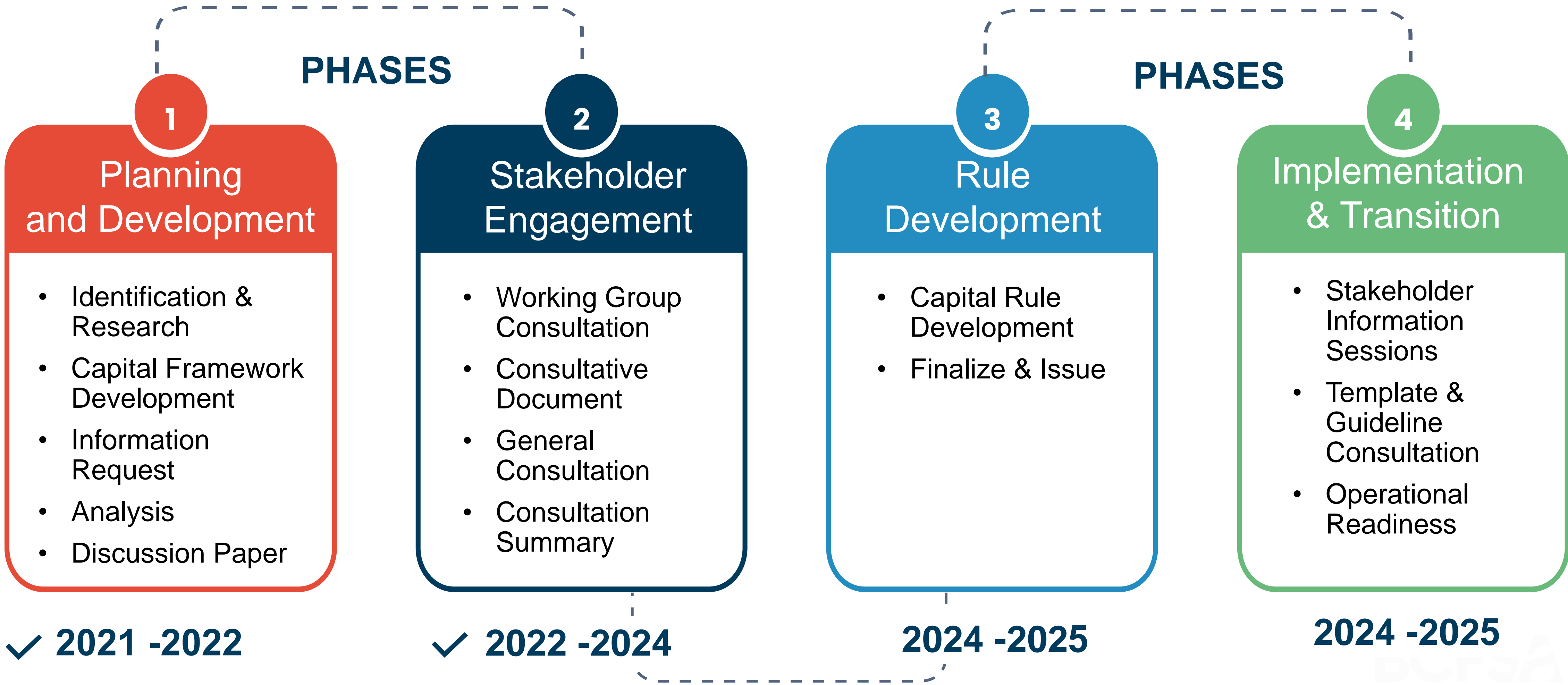


# Agenda

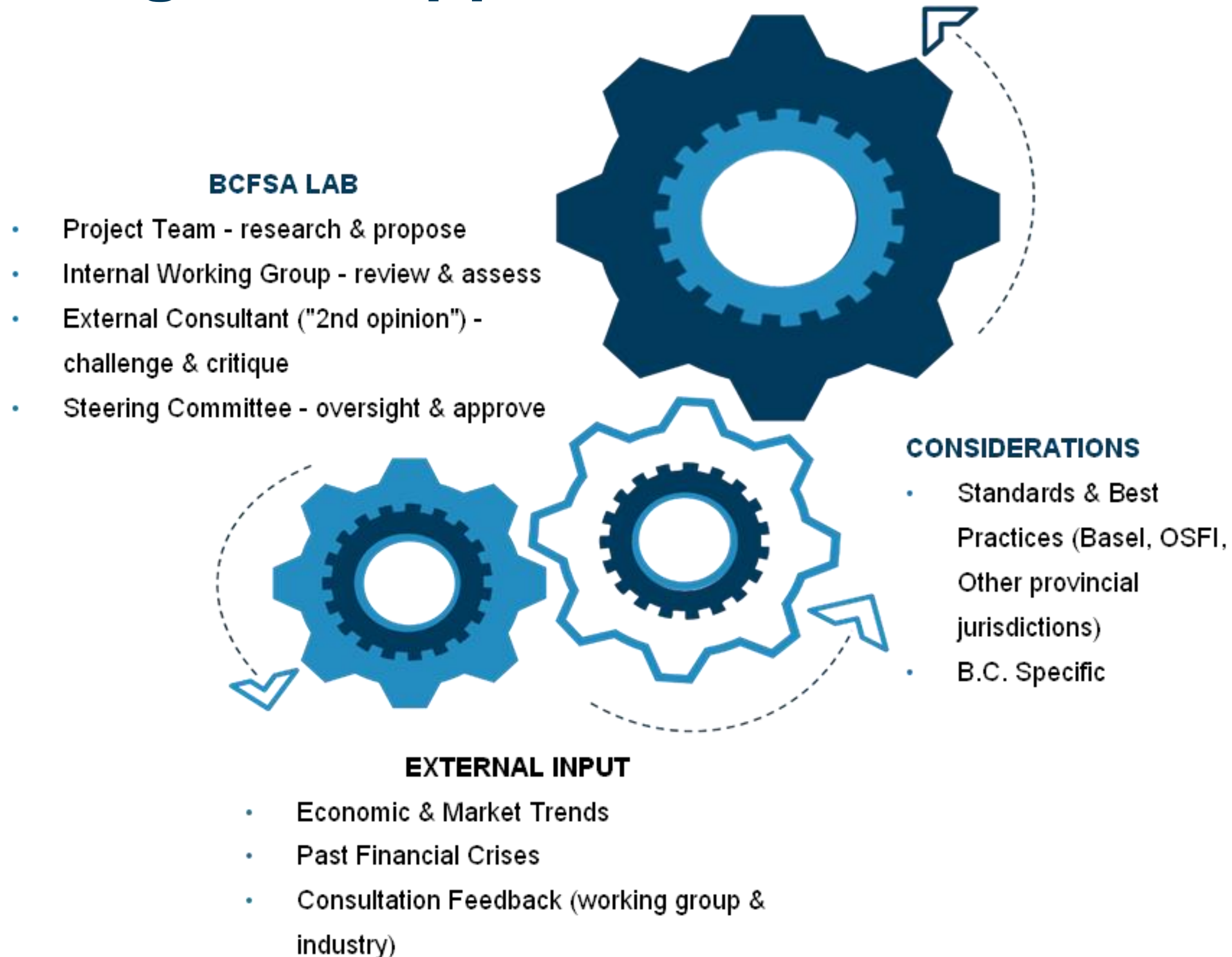
1. Capital Modernization Project Overview
2. Highlights of the Capital Framework
3. Consultation Feedback Themes
4. Key Changes Made Based on Feedback
5. What's Next
6. Q&A

# Capital Modernization Project

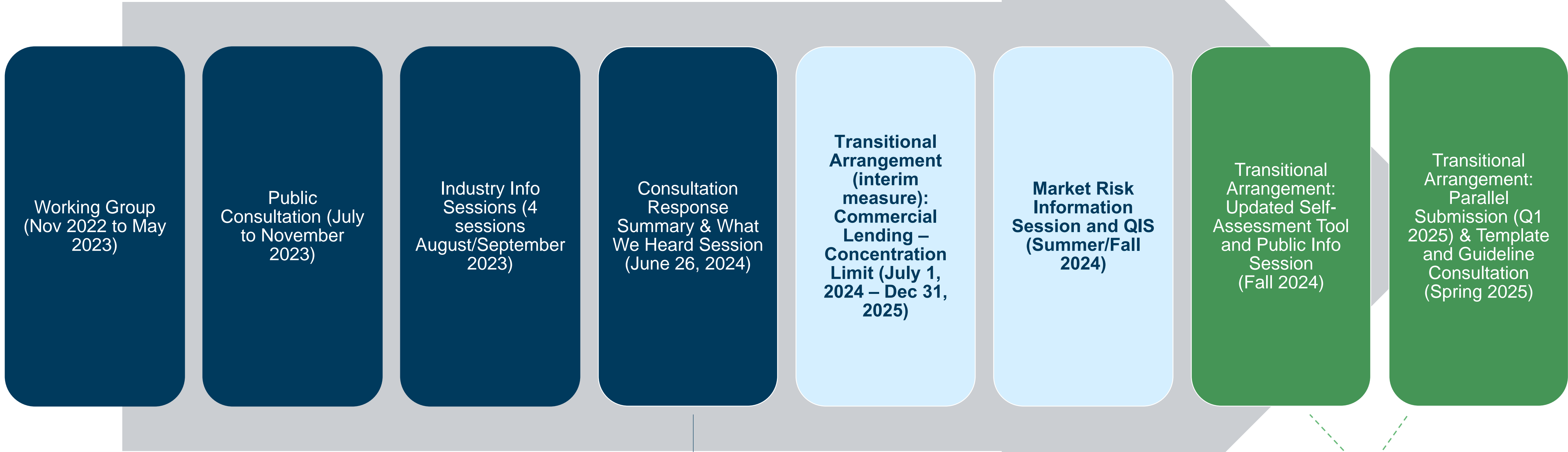
(Capital Rule effective Jan 1, 2026)



# BCFSA Integrated Approach



# Stakeholder Engagement Timeline (Fall 2023 – Spring 2025)



End of Phase II

Phase IV  
Preparation

# Highlights of the Capital Framework



# Highlights of the Capital Framework

## MEASURES TO STRENGTHEN THE CAPITAL FRAMEWORK

- Adopted Basel standards focusing on high-quality banking capital
- Adopted consolidated approach to risk assessment
- Updated minimum capital requirements and capital targets
- Mandated capital conservation buffer
- Introduced standardized approach to address credit risk
- Introduced leverage ratio
- Introduced comprehensive operational risk capital requirements





# Highlights of the Capital Framework

## MEASURES TAILORED FOR B.C. CREDIT UNIONS

- Maintained membership shares capital treatment
- Developed new B.C. specific capital composition
- New commercial and residential lending categories, assessment factors, and risk weights
- Introduced B.C. specific regulatory retail portfolio and general commercial lending risk weights
- Updated transitional arrangement including an interim measure of thresholds on commercial lending





# Consultation Feedback Themes



# Key Consultation Feedback Themes in Response to 2023 Consultation Paper

1. Positive feedback to framework and collaborative approach
2. Implementation challenges
3. Concern about potential competitive disadvantages
4. General feedback
5. Transitional arrangements





# Concern about Potential Competitive Disadvantage:

- Respondents noted proposals are not aligned with the requirements for similar provisions under OSFI or Basel III
- Respondents commented on the additional complexity of using multiple risk factors in residential and commercial lending. Commercial lending categories are more granular than those used in other jurisdictions
- Respondents advised the increased data collection requirements, beyond what is required by banks, would negatively impact their members' experience and place credit unions at a disadvantage

## BCFSA Positions

- High exposure to real estate lending – 80 per cent of segment assets – distinguishes B.C. credit unions from banks
- Proposed framework targets the risks associated with B.C.'s real estate market e.g., market volatility, geographic supply constraints, speculative activities
- B.C. tailored approach captures the most material exposures

# Implementation Challenges:

- Respondents are concerned about the additional costs and resources required to implement significant changes for system upgrade, data collection, and lending processes
- Respondents are worried about how members will react to the new data requirements
- Respondents are concerned about the impact on their reputation from expected lower capital adequacy ratio
- Respondents requested a longer transitional time to get ready for the new framework

## BCFSA Positions

- Acknowledge the operational and resource challenges
- Introduced new and updated transitional measures to support the adjustment period



# General Feedback:

- Respondents asked for details on how distributions would be constrained if a credit union's capital falls below the capital conservation buffer
- Respondents asked if the new requirements replaces ICAAP

## BCFSA Positions

- Provided details on a capital conservation buffer including constraints for distributions, consistent with other jurisdictions
- Comprehensive review of ICAAP is scheduled for Q4 2024/25

# General Feedback:

## continued

- Respondents asked how the proposed capital framework will affect the CUDIC assessment
- Respondents requested clarification on treatment of market risk
- Respondents expressed desire to phase out system capital over an extended period to help credit unions adopt to the new requirements

## BCFSA Positions

- CUDIC will perform an impact assessment after the Capital Rule is in place
- Market risk information session and quantitative impact study scheduled for summer/fall 2024
- System capital is not loss-absorbing in stressed situations. This item is removed from regulatory capital on January 1, 2026

# Key Changes Made Based on Feedback

**NOTE:** Item numbers have been added for  
information. Items refer to the Capital  
Modernization Consultation Summary Report



# Key Changes - Capital

- Adopted Basel III risk weights on: [\(Item 20\)](#)
  - Claims on sovereigns
  - Claims on Public Sector Entities
  - Claims on Deposit Taking Institutions and Banks
  - Claims on Corporates
- Introduced a simplified threshold approach to address investments in the common equity of financials or other total loss-absorbing capacity instruments:
  - Non-significant investments [\(Item 1\)](#)
  - Significant investments [\(Item 1\)](#)
- Adopted a single threshold approach for deferred tax assets arising from temporary differences [\(Item 2\)](#)





# Key Changes - Credit Risk

- Introduced B.C. specific regulatory retail portfolio criterion (Item 20.3)
- Introduced capital treatment for:
  - Repurchase agreements and reverse-repurchase agreements (Item 12)
  - Covered bonds, project finance (Item 13)
- Updated treatment of HELOCs to align with term mortgages (Item 14)
- Reduced CRE Lending Land-Only (Speculative) risk weight from 150 per cent to 140 per cent (Item 17.3)
- Removed the General Commercial Lending table and introduced revised treatment of general commercial lending (Item 18)





# Transitional Arrangements

- Extended implementation timeframe from two years to three years.
- Relief from full deduction of investments in the common equity of financials through the introduction of a threshold and a transitional arrangement
- Parallel reporting will assist credit unions to assess the impact and their readiness for new reporting requirements

**(See Items 28-34)**





See Items 28 & 34 and Appendix B in the Summary Report

# Revised Transitional Arrangements:

Risk-Based Capital Target Ratio				
Components of Capital (Capital Rule effective Jan 1, 2026)	Year 0 (Jan 1, 2026)	Year 1 (Jan 1, 2027)	Year 2 (Jan 1, 2028)	Year 3 (Jan 1, 2029)
Tier 1 Capital	4.5%	5.0%	5.5%	6.0%
Capital Conservation Buffer	1.0%	1.5%	2.0%	2.5%
Tier 1 Capital with Buffer	5.5%	6.5%	7.5%	8.5%
Total Capital (Tier 1 Capital plus Tier 2 Capital)	8.0%	8.5%	9.5%	10.5%
Software Intangibles	No deduction	No deduction	No deduction	Full deduction
Non-Significant Investments in Financials	No Deduction Risk Weight Applies	No Deduction Risk Weight Applies	No Deduction Risk Weight Applies	Full Deduction Subject to 10% Threshold
Leverage Ratio	3%	3%	3%	3%

# Transitional Arrangements: Parallel Reporting

- BCFSA will provide an enhanced self-assessment tool that builds on proposals contained in the July 2023 Consultation Paper and revisions outlined in the Summary Feedback Report
- Enables credit unions to evaluate the impact of the new framework on their capital requirements and any adjustments to align with the new reporting requirements
- Reporting based on current and proposed framework with proportionality for size of credit unions
- Targeted release in Fall 2024 to provide a full 12-month period before the effective implementation date (i.e. January 1, 2025 – January 1, 2026)
- BCFSA will host an Information Session about completing the new reporting requirements

**See Item 32**

# Transitional Arrangements: Commercial Lending – Concentration Limit

- BCFSA will introduce an interim measure to adjust the concentration limit for Commercial Loans and Leases
- Allows credit unions to start adapting lending portfolios and practices in anticipation of commercial lending under the new regime
- Encourages credit unions to start strengthening credit assessment and loan underwriting practices in anticipation of more risk-based commercial lending risk weightings under Capital Modernization.
- This interim measure will be in effect July 1, 2024 until the implementation of the Capital Rule.

Commercial Loans and Leases (as a % of Total Assets)	Current Risk Weighting %	Risk Weighting % Effective July 1, 2024 – Dec 31, 2025
≤ 30%	100	100
> 30% and ≤ 35%	150	100
> 35%	200	200



# What's Next



# Capital Modernization Project

## WHAT'S NEXT?

### June 2024

- ✓ Publication of Consultation Summary Report
- ✓ Information session – What We Heard
- Capital Rule development and drafting

### Summer/Fall 2024

- Market Risk Information Session and Quantitative Impact Study

### Fall 2024

- Updated Self-Assessment Tool
- Information Session

### Spring 2025

- Reporting Template Consultation
- Internal Capital Adequacy Assessment Process (“ICAAP”)





# Questions?

Contact: [CUCapital@bcfsa.ca](mailto:CUCapital@bcfsa.ca)





# Thank you.