



Guideline Impact Analysis Statement

Guideline A-3 Transitional Period Capital Floor Requirement for Institutions Using the Internal Ratings Based Approach to Credit Risk

November 2007

I. Background

On November 1, 2007, Capital Adequacy Requirements (CAR) Guideline A-1 will come into effect, which reflects the requirements set out in the *International Convergence of Capital Measurements and Capital Standards* (the Basel II Framework). This Guideline requires institutions implementing the internal ratings based (IRB) approach to credit risk to calculate a floor amount on the total capital requirement, based on the requirements that were in effect prior to the implementation of the Basel II Framework. These previous requirements are contained in CAR Guideline A (2001) Parts I and II, but this Guideline will be withdrawn on January 1, 2008.

II. Problem Identification

Institutions using the IRB approach to credit risk must have clear guidance on how to calculate the capital floor requirement based on the previous (Basel I) requirements. The calculation of risk-weighted assets and deductions from capital under the previous requirements differs substantially from the calculation of these amounts under CAR Guideline A-1.

III. Objective

The objective of releasing Guideline A-3 is to ensure that federally regulated deposit-taking institutions implementing the IRB approach have access to up-to-date guidance to assist their calculation of capital floors during the transition period. Institutions should not have to refer to a Guideline that is no longer in force in order to determine any amount used in the calculation of required capital under a Guideline that is current, i.e., Guideline A-1.

IV. Options

OSFI considered two options for the release of Guideline A-3:

Option 1: *Include the detailed transitional floor period capital floor requirements within CAR Guideline A-1.*

This option would have lowered the number of guidelines released by OSFI in order to implement the Basel II Framework. However, following this option would have substantially lengthened CAR Guideline A-1, and could have caused confusion due to having, within the same Guideline, two different methods for calculating credit risk-weighted assets, market risk-weighted assets and deductions from capital.

Option 2: Release the transitional period capital floor requirements as a separate Guideline.

This option does not require OSFI to integrate the previous CAR Guideline A (2001) into the new CAR Guideline A-1. Furthermore, OSFI will be able to modify or withdraw this Guideline in 2010, if required, without having to change CAR Guideline A-1.

V. Consultations

OSFI released a draft revised version of CAR Guideline A-1 on September 13, 2007. In the cover letter to this draft Guideline, it was stated that the existing CAR Guideline A (2001) would be revised and renamed Guideline A-3 upon implementation of the Basel II Framework so that institutions would be able to determine the capital floor. There are no material differences in the determination of risk-weighted assets and deductions from capital under Guideline A-3 and under CAR Guideline A (2001) Parts I and II.

VI. Recommendation

It is recommended that OSFI issue a separate Guideline specifying the calculations of risk-weighted assets and deductions from capital that were previously contained in CAR Guideline A (2001), for the purpose of allowing institutions implementing the IRB approach to credit risk under CAR Guideline A-1 to calculate the transitional period capital floors.