



EXPERTISE CANADA BANKS ON
LA RÉFÉRENCE BANCAIRE AU CANADA

Introduction

The Canadian Bankers Association welcomes the opportunity to respond to the second consultation paper issued by the Department of Finance as part of its Review of the Federal Financial Sector Framework. The CBA 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 satisfying their financial goals while obtaining banking products and services through existing and evolving channels.

Canadian banks are a key driver of economic growth, representing approximately two-thirds of the business lending market and roughly one-quarter of the overall business financing market in Canada. In 2016, total authorized credit to businesses surpassed \$1 trillion, of which \$214 billion was authorized to and in support of small and medium-sized businesses. The contribution of the banking industry to Canada's GDP has grown by more than 20 percent over the past seven years, accounting for approximately 3.4 percent, or close to \$60 billion, of GDP as of December 2016. Canadian banks have contributed to job creation by employing more than 275,000 Canadians in a workforce that reflects the diverse fabric of Canadian society and labour market. Banks and their subsidiaries paid \$27.5 billion in salaries and benefits in 2016.

Canadian banks have always been very active in the development of technologically enabled financial innovation that provides solutions to meet the changing financial needs of Canadian consumers. Canadians are embracing these new technologies as more are using online and mobile channels as their preferred means of banking. Constantly looking to the future, banks continue to innovate, working with innovation hubs, launchpads, and non-bank fintech companies to pursue, design, and deliver digital innovations and solutions for their bank customers.

During the first phase of the consultation process, the CBA provided recommendations in light of the dynamic, transformative changes in how banks and non-bank fintech entities deliver financial services to consumers. Banks are strong proponents of a competitive and innovative financial services sector. Banks recognize that the recent emergence of companies that focus on financial technology has had positive impacts on the marketplace by heightening competition and accelerating innovation to benefit consumers. Technology also continues to change the way banks interact with their clients, and it is critical that the legislative and regulatory framework that governs the banking sector evolve to support it. To maintain its relevance and support innovation, the legislative and regulatory framework must be technologically neutral as tomorrow's technology may be striä y

evaluation and operating in a regulatory environment. Banks benefit by discovering new and innovative products and solutions that their customers demand and expect. Our recommendations will further the policy objectives of innovation, modernization, and competition in banking and financial services in Canada that Finance has identified as central to this Review. Our recommendations also support Finance's objectives of improving the protection of bank customers, and safeguarding a stable and resilient financial services sector.

We have focused our commentary below on the following key areas highlighted in the second consultation paper:

- Fintech business powers and collaboration**
- Exploring the merits of open banking**
- Cyber risk**
- Competitiveness of small and mid-sized banks**
- Improving the protection of bank consumers**
- Corporate governance**

We have also attached an appendix that will address some of our more technical recommendations, as well as other policy measures raised in t

Reflecting this additional definition, it is apparent that fintech is increasingly intrinsic to and intertwined with the provision of financial services and the business of banking more broadly. Given these developments, we believe that it is critically important for government policy to revisit the historical technology constraints in the current legislative and regulatory framework for banks. The framework needs greater clarity regarding the nature of fintech activities in which banks may engage. Additionally, the removal of barriers that limit fintech access to bank capital and fintech collaboration with banks, is desired by both banks and non-bank fintech entities. We are facing a defining moment for the future of financial institutions and the framework should ensure that banks are positioned to participate in fintech fully in this era of rapid technological evolution.

2. Open Banking

As noted above, Canadian banks are strong proponents of a competitive and innovative financial services sector that utilizes rapidly advancing technology to better serve customers

challenges posed by cyber crime. The financial sector relies on other critical infrastructure sectors, most notably telecommunications and energy (electric power), to deliver services to Canadians. We are reminded of cyber security risks on a regular basis through media reports on cyber attacks that affect millions. As a result, it is imperative to ensure consistent oversight across critical infrastructure sectors to help safeguard the integrity of the financial system. Consistency of global cyber standards is equally critical for banks, and we support Finance's pursuit of greater international cooperation on cyber security in the financial sector.

With its highly-educated workforce and the federal government's commitment to the Innovation Agenda, Canada is well-positioned to become a global leader in groundbreaking cyber security technology. Canadian innovation in this area should be encouraged at all levels of government and the public/private sector. Expanding the ability of banks to invest in, and partner with, domestic and international companies that provide novel solutions to cyber security problems would help to drive growth and innovation, and to protect Canadians and the Canadian economy from cyber crime.

4. Competitiveness of Small to Mid-Sized Banks

We are pleased to see the consultation paper highlight the important contributions of small and mid-sized banks to long-term economic growth in Canada, as well as their role in enhancing innovation and competition in financial services. We agree that these objectives need to be balanced against a well-managed regulatory and legislative framework for oversight and risk. In our view, there are opportunities to recalibrate the balance between these policy objectives. Small and mid-sized banks that are not designated as domestic systemically important banks, referred to here as non D-SIBs can face disproportional impacts from additional regulatory and capital expectations which are not aligned with the risks these institutions could pose to the Canadian financial system.

Regulatory burden

It is important that Finance and OSFI are sensitive to important discrepancies in the resources and level of systemic risk among the various players within the Canadian banking sector. Growing regulatory requirements can have a disproportionately greater impact on the non D-SIBs given the scale of their operations. Although the consultation paper notes that small and mid-sized banks are regulated in a manner proportionate to their size, risk and complexity, there are opportunities to recalibrate the balance to be more aligned with an institution's level of risk. There are numerous areas where a re-examination would be beneficial including with respect to: accommodations

The consultation paper notes that the statutory minimum initial capital requirement for banks has been reduced from 10 million dollars to 5 million dollars. However, this provision has had limited impact as OSFI's *Guide for Incorporating Banks and Federally Regulated Trust and Loan Companies* requires additional capital requirements including meeting the requirements of OSFI's *Capital Adequacy Requirements Guideline*. As part of this consultation, the government should consider a revised framework which ensures that OSFI guidance supports Finance's objective of enhancing the contributions of non D-SIBs to the Canadian economy.

5. Improving the Protection of Bank Consumers

The banking industry has long supported a strong federal consumer protection framework. Fragmentation of a national banking system leads to consumer confusion and impairs the ability of the federal government to inform and protect consumers. A consistent set of rules and regulations helps to foster innovation and competition in financial services by permitting banks to more quickly respond to customer demand by developing and enhancing products and services that are available and consistent in all provinces and territories.

As noted in the consultation paper, Canadian consumers already benefit from a strong consumer protection regime for financial services. However, the banking industry fully supported the federal framework proposed in Bill C-29, Budget Implementation Act, 2016 No. 2, as an important step to further improve upon that regime with clear, streamlined, and consistent regulations that would apply across the country. Bill C-29 set out a clear federal framework designed to both keep pace in meeting consumer needs and provide clarity to guide the operations of federally-regulated banks. We support moving forward with the measures proposed in 2016 as we believe that consolidating consumer protection and establishing a uniform set of standards under a single framework will:

- Improve the efficiency of financial services regulation;
- Ensure consistent policy across the country;
- Prevent consumer confusion;
- Maximize product availability;
- Enhance the capacity of the FCAC to fulfill its mandate to inform and protect consumers; and
- Ensure innovative products and services are available to all Canadians on the same basis.

The stability and efficiency of the Canadian banks is founded on a streamlined regulatory system with national laws applicable across the country and with a single regulator responsible for safety and soundness – OSFI – and a single regulator for consumer protection – the FCAC. We agree that Canadians benefit from a dedicated consumer protection regulator, the FCAC, and we support the consumer protection framework being placed under the oversight of a single regulator.

With respect to the sales practices reviews, we note that the FCAC and OSFI regularly conduct reviews of the banks' business practices and the banks fully cooperate with them on these reviews, and we support continued federal oversight over these matters.

6. Corporate Governance

Strong governance practices at institutions support innovation and competition by creating a climate where ingenuity and creativity can flourish, and where the results of those efforts are visible to shareholders and other institutional stakeholders. We are pleased to see that Finance's consultation paper highlights that federally regulated financial institutions are recognized leaders in establishing and applying strong corporate governance frameworks, and support in principle Finance's proposed measures to enhance corporate governance. We also agree with Finance that, while the same governance principles generally apply to all federally regulated financial institutions irrespective of size, the implementation of those principles may give rise to challenges for smaller institutions. We note Finance's recognition that publicly listed institutions already follow some of the proposed corporate governance practices where Finance is seeking stakeholder views. We strongly encourage Finance to harmonize the corporate governance aspects of the federal financial institutions statutes with existing rules applicable to publicly listed institutions, such as those of the Canadian Securities Administrators (CSA) and the Toronto Stock Exchange (TSX).

Promoting Diversity on Boards

The CBA strongly supports the existing "comply or explain" model established by the CSA to promote the participation of women on boards of directors and in senior management. Banks proactively support and foster diversity and inclusion in their workforces. Many CBA members have formal and informal diversity policies, programs and practices in place aimed at promoting diversity. As of 2017, Canada's six largest banks have, on average, 36 percent women on their boards of directors and h

Distributing Meeting Materials and Annual Statements

Consistent with the proposed changes to the *Canada Business Corporations Act* (CBCA) in Bill C-25, the use of the notice-and-access approach should be permitted for all federally regulated financial institutions. The BA should be amended to expressly provide for notice-and-access that would permit communications to be sent to shareholders by making them available on the bank's website and through the System for Electronic

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We are supportive of this proposal since a materiality threshold would address any potential prudential concerns while providing banks and other federally regulated financial institutions (FRFIs) with greater flexibility in how they manage their businesses.

Eliminating Superintendent approval where a FRFI acquires control of a limited partnership investment fund (that is not a mutual fund entity or closed-end fund) only because it controls the general partner of that partnership. This potential change would recognize that limited partners, and not general

We are supportive of this proposal for the reason stated by Finance.

Requiring Superintendent approval for the acquisition of control of a factoring or financial leasing entity,

Frequently Traded and Easily Valued Assets

Finance is seeking views on whether to narrow the scope of large asset transactions excluded from the requirement to obtain Superintendent approval. Generally speaking, we are against narrowing the exemption from Superintendent approval. We are concerned that this would hamper the banks' ability to execute transactions that are required to meet their obligations and objectives (e.g. for liquidity). In addition, broadening the requirement for Superintendent approval from "large asset transactions" to include "transactions involving significant financial risk" would be quite a material change, and it is furthermore unclear how these transactions would be defined. In order to opine fully, we would need to be provided with more detail on the proposal.

As such, we would be interested in discussing with the government any potential change in the scope of the exemption for frequently traded and easily valued assets. The industry is not clear how the exemption would be modified and would want to ensure there are no unintended consequences. For example, the industry would expect that normal trading activity (security sales, repo, and stock borrow/lend activity) with the same counterparty over a 12-month period would not trigger review by the Superintendent.

In addition, we would ask that any increases in regulatory burden related to accessing capital market transactions be carefully considered, especially as they relate to small institutions. In this instance, we have concerns that a narrowing of the scope for transaction exemptions could disproportionately affect small institutions. Even using a '10 percent of assets' definition translates to a lower absolute threshold for smaller institutions. Despite this lower threshold, smaller institutions may be expected to deliver transaction volumes commensurate with evolving market expectations, and those expectations will not necessarily vary by institution size. As a result, smaller institutions will face regulatory hurdles which large institutions will not, for similar transactions. We are concerned that this would complicate the timing of market access and lead to inefficiencies in transaction execution for smaller institutions.

CDIC Claims in Liquidation

Finance is seeking views on whether to change the *Canada Deposit Insurance Corporation Act* to clarify that a