Intelligence MEMOS

From: Nicholas Le Pan

To: All Canadian financial regulators

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Re: **GETTING CANADA READY FOR ITS SYSTEMIC RISK AUDIT**

When the IMF last reviewed Canada's financial system in 2014 it recommended we do better in managing the federal provincial coordination aspects of systemic risk oversight, and improve systemic risk management in the capital markets area. The IMF will be back soon for an update assessment. So, the question is, how are we doing?

In today's C.D. Howe Commentary I argue that more needs to be done and that Canadians should expect a high level of preparedness from federal and provincial authorities. Then, problems arising in one part of the financial system don't cause ripple effects endangering the system as a whole. Just because we did well last time is no reason to not want excellent preparation so we can do well next time.

Since the last IMF review the federal government and participating provinces have fleshed out the Capital Markets Regulatory Authority and released the proposed federal Capital Markets Stability Act. There appears to be room for it to make a significant contribution, particularly in regular analysis of systemic capital markets risk. But there is very little clarity and transparency about how that system will work in practice. For that new authority to make a meaningful contribution to systemic risk oversight I argue it should:

- Develop and publish the framework it intends to use to analyze systemic risk in capital markets.
- Commit to regularly publishing its analysis of systemic capital market risk.
- Ensure clear authority is given to a senior position in the Authority with a clear mandate for systemic risk work.
- Play a lead role in putting in place arrangements for sharing of market data necessary for financial stability analysis—which is now managed in silos.

Also, the Bank of Canada clarified several years ago that major domestically systemically important financial institutions like the Desjardins system and the B.C. Credit Union Central will only be eligible for emergency liquidity assistance in a crisis if pre-arrangements with provinces to cover any losses are in place. But important provinces have not made progress in entering into necessary arrangements. Those entities are important because of their position in their respective provinces and because they also link into the national financial system. When a crisis starts is not the time to try to negotiate these arrangements.

The authorities have also not been clear about how federal-provincial coordination is supposed to work. It is not necessary or desirable to give one organization overall responsibility. But clarity of the responsibility and accountability of existing ad hoc federal-provincial coordination mechanisms for crisis management, would focus minds and clarify accountability and promote cooperation.

It also appears that identified weaknesses in certain provinces' safety and soundness regulation have not kept pace. Analysis is hampered by a lack of transparency by a number of provinces in what they are doing. However, while it appears that Quebec has been active in upgrading regulation and supervision, B.C. and Alberta have been slow to respond to issues they themselves identified in their own review of their regulatory framework, or that provincial auditors general identified. In B.C. the regulatory agency is severely and chronically understaffed, while there is little transparency in Alberta about its systemic risk oversight of Alberta Treasury Branches, which has almost 15 per cent of the provincial consumer market.

None of this has to be an overwhelming, expensive task—and the effort and resources expended in advance are worth the savings in avoiding the next potential crisis.

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