

MEETING OF THE FINANCIAL SERVICES COMMITTEE

BRUSSELS, 19 JUNE 2018

JOINT REPORT

The inaugural meeting of the Financial Services Committee meeting established under CETA took place in Brussels on 19 June 2018. The parties discussed financial sector developments as well as regulatory and supervisory issues relating to banking and capital markets. They also discussed issues pertaining to financial stability as well as cybersecurity, consumer and data protection and sustainable finance.

Session 1 - Financial Sector Developments and Regulatory Priorities

1(a) Financial System Review of Canada

Canada summarized the June 2018 Financial System Review published by the Bank of Canada, which notes elevated household indebtedness, housing market imbalances and the potential for disruptive cyber attacks as key vulnerabilities to the Canadian financial system. While there are some signs of easing, household vulnerabilities remain elevated and are expected to persist. With respect to cyber risk, domestic and international collaboration will continue to be important, particularly in the area of recovery plans that can be used to quickly restore financial system functioning and prevent a loss of confidence in the event of a cyber attack.

1(b) Canada's 2019 Financial Legislation Review

Canada provided an overview of its current five-year review of the federal financial sector framework. Finance Canada is currently considering stakeholder input on a series of policy issues covering four themes: 1) supporting a competitive and innovative financial sector; 2) improving the protection of bank consumers; 3) modernizing the regulatory framework; and 4) safeguarding a stable and resilient sector. The European Commission provided an overview of its 2015 Call for Evidence on the European Union regulatory framework for financial services, which assessed whether rules adopted since the financial crisis were working as intended.

Session 2 - Banking and Financial Stability

2(a) Implementation of Basel III

The European Commission provided an overview of its implementation of the Basel III framework. It explained how the negotiations regarding its November 2016 package of legislative proposals on banking were evolving. This package contains among others, the new rules on the leverage ratio, on market risk and on the net stable funding ratio. The Commission outlined the next steps in the implementation of the final elements of the Basel III reform. In Canada, the Office of the Superintendent of Financial Institutions is consulting on the proposed scope and timing of domestic implementation of the final Basel III reforms and is seeking feedback from stakeholders on specific issues.

2(b) Resolution Planning

Canada gave a presentation on its resolution planning efforts, which include its 2016 bail-in regime and 2017 by-law making the Canada Deposit Insurance Corporation the authority with respect to the development, submission and maintenance of resolution plans by domestic systemically important banks (D-SIBs). The European Commission echoed Canada's views on the importance of international preparedness and coordination and outlined the Single Resolution Board's work to increase the depth of the initial plans already in place and gradually build up the Single Resolution Fund to reach a target level of 1% of covered deposits by the end of 2023.

2(c) Stress Testing

Canada discussed its biannual stress testing process led by the Office of the Superintendent of Financial Institutions and the Bank of Canada's planned top-down approach, which proposes testing a variety of stress scenarios to examine a range of factors including cost of funding impacts and spill over effects across the financial system. The European Commission summarized the enhanced rigor of the European Banking Authority's 2018 testing process, the results of which are expected to be published in November.

2(d) G-SIB Methodology

The parties discussed two issues that were raised during the Basel Committee's April 2018 review of the framework on Global Systemically Important Banks (G-SIB): (i) the cap on the substitutability category score and (ii) treating the Banking Union as a single geographic area.

Lunch – International developments

Over lunch, the parties informally discussed developments in ongoing financial services trade negotiations and in multilateral institutions, like the G7, G20 and the Financial Stability Board.

Session 3 - Fintech, Payments and Consumers

3(a) EU Fintech Action Plan

The European Commission provided Canadian authorities with an overview of the main actions included in its March 2018 action plan, including regulatory and supervisory aspects and how to best support new technologies. Canadian authorities provided an update on recent developments, notably legislative amendments to include crypto-currencies under anti-money laundering requirements and securities law regulatory work on initial coin offerings. On crypto-assets, the European Commission explained that when tokens could be qualified as securities, relevant legislation was applied. On Initial Coin Offerings, the current focus is on improving disclosure to ensure sufficient transparency towards investors. In addition, the parties aim to support innovation through different tools including specific funding mechanisms and enabling partnerships between incumbents and Fintech companies.

3(b) ICT Security and Governance Requirements for Financial Institutions

The European Commission explained that cybersecurity is a horizontal policy priority and provided an overview of the organisation of its cybersecurity-related work. The Commission stressed the importance of international coordination, in particular within the G7 and G20. Canadian authorities emphasised the importance of promoting information sharing, continuing to work jointly with G7 partners and engaging with the financial sector on issues such as threat-led penetration testing, third-party risks and cross-sector coordination. In 2018, Canada announced significant investments in cybersecurity – over \$500 million over five years – to launch a comprehensive National Cyber Security Strategy.

3(c) Supporting an Innovative Retail Payments System

Canada provided an overview of the process to modernize its payment systems to facilitate real time payments, enhance security measures and foster innovation and competition. As part of this process, Finance Canada is undertaking public consultations on the 2015 governance changes to the *Canadian Payments Act* and is seeking views on Payments Canada's current membership structure in light of the growth of non-financial institution service providers in the payments ecosystem. The European Commission highlighted its work towards implementing real-time payments under the second Payment Services Directive (PSD2).

3(d) Enhancing Consumer Protection in Banking

Canada presented the findings of the Financial Consumer Agency of Canada's (FCAC) Domestic Bank Retail Sales Practices Review and its recommendations for strengthening financial consumer protection. Proposed legislative amendments that would strengthen the FCAC's tools and mandate and continue to advance consumers' rights and interests when dealing with their banks were also outlined. The European Commission discussed its product-specific approach to consumer protection and noted increasing attention to consumer issues now that the implementation of post-financial crisis measures is largely complete.

3(e) Data and Impact on Financial Sector

The parties discussed open banking and its potential impacts on issues such as competition, consumer protection and privacy. Canada outlined its review of the merits of open banking in order to assess whether it would deliver positive results for Canadians with the highest regard for consumer privacy, data security and financial stability. The European Commission noted the competitive advantages of facilitating the portability of financial services and the challenges of ensuring consumers are properly informed.

Session 4 – Capital Markets Developments

4(a) Review of the EU Prudential Framework for Investment Firms

The European Commission presented its proposal to review the prudential framework for investment firms. It aims at tailoring the framework in order to make the prudential rules more proportionate and risk sensitive. Special attention is given to the regulatory and supervisory treatment for systemic investment firms, who share trading activities with credit institutions and compete directly with them. Under the proposal, these firms would need to hold a banking license when their activities would reach a certain threshold that would qualify them as systemic. Systemic investment firms located in the Euro Area which would be requalified as credit institutions would become subject to supervision of the Single Supervisory Mechanism.

The Commission also explained the changes introduced to the equivalence framework for third country investment firms provided in the EU's Markets in Financial Instruments Directive and Regulation. In that context, the objective of the Commission is to ensure that a proper assessment of the content of the third country's legislation under which that provision of service is provided is made, taking into account the possible systemic nature of the flow of services coming from that third country.

4(b) European Commission Proposal on Covered Bonds

The European Commission presented its March 2018 proposal for a legislative framework on covered bonds, which has the dual purpose of ensuring that covered bonds can develop across the EU and addressing prudential concerns about the preferential treatment granted by the current EU legislation. It explained that a third country regime would be considered after the legislative framework has come into force and has been transposed in national law. Canada highlighted the strengths of its covered bond regulatory and supervisory regime and requested timely consideration of equivalency.

4(c) Overview of Capital Markets Regulation in Canada

Canada provided an overview of its capital markets regulatory framework, which is under the shared jurisdiction of the federal Parliament and provincial and territorial legislatures. The presentation also included a description of the cooperative capital markets regulatory system initiative between the federal government and participating provinces and territories.

The European Commission enquired about Canadian financial services operators' interest in recognition of Canadian benchmarks in the EU as at the end of the transitional period foreseen by the European Benchmark Regulation (No 2016/1011) it will no longer be possible to use them in the EU, unless an equivalence decision is adopted by the Commission or such benchmarks are endorsed or their administrators recognised by an EU national competent authority. Canada advised that provincial and territorial securities regulators are working to establish a Canadian regulatory regime for financial benchmarks in time for the EU equivalency deadline.

The parties discussed initiatives with regard to alternative risk free rates.

Session 5 – Other Regulatory and Policy Developments

5(a) Sustainable Finance

The European Commission presented the EU strategy on sustainable finance. It explained how the strategy took into account the recommendations of the FSB's Task Force on Climate-related Financial Disclosures, how the European Supervisory Authorities will take into account sustainability in their mandate, and how in practice pension funds will be expected to disclose the way they take into account sustainability in their investment decisions. Canada noted its establishment of an Expert Panel on Sustainable Finance to consult with financial market participants on the opportunities and challenges relating to sustainable and climate-related risk disclosure in Canada, which will complete its work and provide recommendations to the federal government in the coming months.

5(b) FSB Review of Processes

The parties underlined their continued support for the role of the FSB and welcomed the review of the FSB's processes, procedural guidelines and transparency as a timely opportunity to support the overall effectiveness of the FSB.

Conclusions

Both parties agreed on the importance of strengthening regulatory cooperation and the work of multilateral institutions, including efforts to improve their processes. It was thought that discussions within the CETA Financial Services Committee could usefully contribute to these objectives. The scope and depth of the discussions in the inaugural meeting demonstrated the usefulness of the Committee as a forum for exchanging views on issues of direct bilateral interest. Some of the topics mentioned for possible further follow-up were stress-testing, cybersecurity, payment services, consumer protection and covered bonds.