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## Overcapitalization Part I: A Note on CIBC and a Perspective on Canadian Banks, OSFI, and Basel I

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### Abstract

Overcapitalization is defined here as a bank having capital adequacy ratios higher than required by regulators. As well, it can also be a strategy adopted by regulators for the institutions that they regulate. With Basel I, between 1996 and 2007, the Canadian regulator, the Office of the Superintendent of Financial Institutions (OSFI), adopted Tier 1 and Total Capital ratios which required Canadian banks to be overcapitalized by 3 percent and 2 percent, respectively, above the minimum ratios specified by the Basel Accord. In addition, Canadian banks adopted internal Tier 1 and Total Capital ratio targets that were higher than OSFI's minima, generally by 1.5 percent. These conservative strategies provided stability to the financial system and enabled Canadian Imperial Bank of Commerce (CIBC) to recover from an Enron legal settlement in 2005 without breaching the minimum standards. CIBC used securitization, purchase of residential mortgage insurance, and increased quarterly earnings to return to its internal capital ratio targets within one fiscal quarter. OSFI and Canadian banks continued to use overcapitalization as a strategy through Basel II and into Basel III.

**Keywords:** Basel Accord, Canada, financial regulation, overcapitalization

**JEL Classification:** G21

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