July 2001

Expansion of List of Securities Eligible as Collateral for use in Bank of Canada Standing Liquidity Facility

Under its Standing Liquidity Facility (SLF), the Bank of Canada is prepared to provide liquidity on a daily basis to financial institutions that participate directly in the payment systems operated by the Canadian Payments Association - the Automated Clearing Settlement System (ACSS) and the Large Value Transfer System (LVTS). Liquidity loans made under this facility must be fully collateralized. Currently the Bank accepts as collateral Canadian dollar securities issued or guaranteed by the Government of Canada or by a provincial government, National Housing Act mortgage-backed securities, and Special Deposit Accounts held at the Bank of Canada. Once appropriate operational arrangements are in place, the securities that will be eligible for use as collateral will be expanded to include Canadian dollar Government of Canada stripped bonds and coupons, bankers' acceptances, commercial paper and corporate debt. The attached appendix provides the complete list of securities that are or will soon be eligible as collateral under the SLF.

The use of this broader range of assets as collateral will be subject to the following conditions:

(i) private sector debt securities used as collateral must meet a minimum credit rating as indicated in the appendix;

(ii) debt securities used as collateral will be limited to those that can be pledged using the Debt Clearing Service operated by The Canadian Depository for Securities Ltd., or that can be physically delivered to the Bank in certificated form;

(iii) the Bank will apply concentration limits that will lead to a diversification of the private sector securities used as collateral by any one pledgor; and,

(iv) debt securities issued by the pledgor of collateral (or any related party) cannot be used as collateral by the pledgor.

The Bank expects to have the necessary operational arrangements in place to accept the broader range of assets as collateral by November 1, 2001. Prior to that date, the Bank will make available the terms and conditions regarding the use of various securities as collateral, including the margins that will be applied.

In taking this decision, the Bank recognizes that broadening the range of collateral eligible to secure standing liquidity facility loans from the Bank will be beneficial to direct LVTS and ACSS participants and their customers. It should reduce the cost of collateral used to support liquidity borrowing related to ACSS and LVTS activities, and to support the use of intra-day credit in the LVTS. The expansion of eligible collateral should also help to deal with any concerns regarding the supply of government securities for collateral purposes.

Finally, the Bank has identified some legal, operational and structural risks associated with asset-backed securities (ABS), other than those guaranteed by CMHC, which are not present in the case of conventional debt securities. The Bank is in the process of examining these risks and possible means of addressing them. Until they are satisfactorily addressed, ABS (other than those guaranteed by CMHC) will not be eligible as collateral under the SLF.

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Appendix
List of securities eligible as collateral under Standing Liquidity Facilities

Currently, the following can be used as collateral for borrowings under the Bank of Canada's Standing Liquidity Facility:

- Canadian dollar securities issued or guaranteed by the Government of Canada
- Canadian dollar securities issued or guaranteed by a provincial government
- NHA mortgage-backed securities (minimum pool size of $75 million)
- Special Deposit Accounts held at the Bank of Canada

This list will be expanded to include the following Canadian dollar securities once operational arrangements are in place:

- Government of Canada stripped coupons and residuals
- Bankers' acceptances
    - minimum issuer credit rating of R1 (low) by the Dominion Bond Rating Service (DBRS) or equivalent Standard and Poor's or Moody's Investors Service
- Commercial Paper (maximum term 364 days)
    - minimum issuer credit rating of R1 (low) by DBRS or equivalent Standard and Poor's or Moody's Investors Service
- Corporate debt (term of one year and longer)
    - minimum issuer credit rating of A by DBRS or equivalent Standard and Poor's Moody's Investors Service