

CDIC's 2019 Annual Public Meeting

T+0: CDIC's Audacious Goal

Payments Canada Summit, Toronto, Ontario

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Remarks by:

Robert Sanderson, Chair of the Board of Directors

Peter Routledge, President and CEO

Chantal Richer, Vice-President, Corporate Affairs, General Counsel and Corporate Secretary

Angela Roberge, Director, Resolution Preparedness for Depositor Solutions

Gina Byrne, Managing Director, Resolution Planning

John Rossi, Policy and Research Advisor

CHECK AGAINST DELIVERY

Bob Sanderson

Good afternoon,

I am Bob Sanderson, and since 2016 I have had the honour of serving as the Chair of CDIC's Board of Directors.

On behalf of the Board, I'd like to thank Payments Canada for this opportunity to partner for our Annual Public Meeting. Payments are a critical part of CDIC's activities, and it is interesting to see the future of the industry unfold here.

CDIC's Board is unique in many respects. It comprises five *ex officio* members, who are senior figures in the Government of Canada, such as the Governor of the Bank of Canada and the Superintendent of Financial Institutions. These public sector members are matched with six private sector members, including me.

The year 2018-19 was a year of significant change at CDIC.

First, five new private sector directors were appointed to our Board of Directors, and I am delighted by their depth of experience, talent and ambition. There have already been some very lively discussions, and we carried out a full review of our Governance and committee structure to keep pace with our evolving risk environment.

And second, Michele Bourque, who had served as President and CEO of CDIC since 2010, retired last year. I am pleased to introduce you today our new CEO, Peter Routledge, who brings a wealth of financial sector expertise to this role, both from the private and public sectors.

Peter will lead a panel presentation by senior CDIC staff of the corporation's key priorities and recent accomplishments. Following the presentation, there will be time for questions from people here in the room and on social media.

And with that, I'm pleased to hand things over to Peter Routledge.

Peter Routledge – Part 1

Thank you, Bob, for the kind introduction.

And welcome to CDIC's Annual Public Meeting.

I'm very proud to lead an organization that manages \$800 billion in credit risk in the form of deposits at 84 member institutions.

As Canada's resolution authority, we are responsible for handling the failure of any of our members, from the smallest to the largest. Our members include banks, federally regulated credit unions as well as loan and trust companies and associations governed by the *Cooperative Credit Associations Act* that take deposits.

I joined CDIC at a very interesting and important time given the global and domestic economic context in which we operate.

I'm not sure it feels this way, but we're now more than 10 years out from the global financial crisis. And while it has indeed been a decade, I tend not to think of it as 10 years since the last crisis. Instead, I think we are 10 years closer to the next one.

Are we ready? Are you ready? Is Canada ready?

At CDIC, our position is that the financial system requires us to be ready for a failure tomorrow. Or next week. Or next decade.

We don't make predictions about when it will occur, so we assume it's right around the corner.

Let's look at the fundamentals, not to sound alarmist.

Looking at the bigger picture, the financial system in Canada is safer than 10 years ago. The volume of insured deposits has vaulted to close to \$800 billion. Better tools to identify troubled institutions and address them, better capital and liquidity buffers, and more detailed resolution planning mean we are better prepared than ever.

As well, there is a bail-in framework in place that shifts the burden of risk from taxpayers and depositors to shareholders and certain creditors who are aware of – and accept – the risk of loss. So investors can price the risk, in advance of a failure, in the free market and they agree to recapitalize the bank should that unwelcome day ever arrive.

And so, as the industry continues to grow, our objective is not to create failure-proof financial institutions. Not that you could ever build, I might point out, a failure-proof institution within a financial system designed to manage risk.

Rather, in talking to CDIC members – some of whom are here today – my message is that we need to work together to strengthen our mutual readiness for resolution in the event of a failure.

T+0

For example, we know that Canadians need access to their savings and financial services at all time. Digital payments and settlement are growing faster every day.

That's why CDIC will become far more ambitious in reimbursement readiness – within five years, we aim to build a payout capability able to reimburse depositors on the same day if a member institution should fail – T+0. This means investing more in technology and business process redesign. My colleague Angela Roberge will speak more about this.

Brokered trusts

We also need to ensure the billions that Canadians save in the form of trust deposits can be quickly and accurately reimbursed in the event of a failure.

Changes to the rules regarding trust deposits that come into force in 2021 mean we must work closely with financial stakeholders, including nominee brokers and member institutions, to strengthen disclosure of beneficiary information and to clarify CDIC's coverage rules for trust deposits. John Rossi will discuss this important area in more detail.

Resolution authority

Of course, reimbursement is not necessary if a bank's operations are never interrupted.

The overall objective of CDIC's resolution-planning process for Canada's largest banks is to ensure that these large, complex institutions are considered resolvable in a manner that protects deposits, maintains the flow of essential financial services, protects our economy, and minimizes risk to taxpayers.

A key element of this role is the development of resolution plans that set out a strategic and operational plan that could be implemented if recovery actions fail.

CDIC aims to ensure that all of Canada's largest banks are fully resolvable by March 31, 2020. I'll ask Gina Byrne to provide an update on this key objective.

Awareness

And of course, none of these efforts on behalf of depositors would be effective if Canadians did not know about it. People can only benefit from deposit protection and the stability it conveys to the financial system if they are aware, so my colleague Chantal Richer will discuss CDIC's public awareness program.

So I will start by asking Angela to tell you about our reimbursement goals, which I think many of you in the payments sector will find very interesting.

Thank you.

Angela Roberge

Thank you, Peter.

Being a leader in how we reimburse depositors if their bank fails is at the heart of our journey to achieve a T+0 payout target. It puts Canadians first. Not unlike Payments Canada, we are undertaking a multi-faceted modernization effort – and as Peter indicated, a huge piece of that effort will be technology and the business processes. However, underpinning these are other parts of our ecosystem to support this journey – the building blocks, if you will, like legislation, payment infrastructure and our stakeholders. My colleagues will touch on a number of these.

So let me tell you where we are and where we are headed.

We are currently able to reimburse most deposits within just a few business days of failure. We do so by getting data extracts from the failed bank, loading cleaned data into our bespoke insurance calculation engines, producing payment files and sending a letter and cheque in the mail to the depositor. Or for very large dollar amounts, we may also send a wire transfer. While the approach works, you can see that there are a lot of steps (and I have only given you the simplified version), few payment methods, and a heavy reliance on physical mail delivery. Further a key dependency in this approach, or any payout approach for that matter, is having the data and information in order to execute on a payout. Without having good quality data, we are unable to move to the next step to calculate insurance and prepare the payment.

In the age of the consumer, information immediacy, faster payments and big data, we are evolving so that we can have line of sight to the right data, at the right time. We don't need to be leading edge but we do need a solution that is scalable and future-proof to meet changing demands. And we need to empower depositors so that they feel in control during a time of uncertainty. For example, giving them the opportunity to select a preferred payment method, direct that payment, manage their contact information and view reimbursement details.

Right now we are at the discovery phase in our journey – we have looked at solutions from other depositor insurers and are consulting with our stakeholders. But that is not to say we are standing still and waiting until 5 years from now to go-live. We are advancing our capabilities through improved data standards with our member institutions; leveraging cloud-based service providers for increased scalability of our systems, and trialing new customer relationship management applications to improve the depositor experience. Each of these elements will support our T+0 vision. And, as you can imagine, a key objective to this vision will be to establish processes, complemented by technology, that allows us to get assurance that the deposit data will be “payout ready” at the time of failure. We are going to be exploring different options to achieve this, while recognizing that there are a number of factors that will need to be considered including:

- Getting visibility at the quality of the data **prior** to the bank failure, to allow sufficient time for the institution to rectify any anomalies
- The burden or effort on member institutions, trustees, and brokers required to produce the data for us, and
- Security and safeguarding of that sensitive data

More developments will continue as we further intelligence gather and select the right partners to help advance our vision. Whether that will be a large systems integration firm to develop a solution that uses APIs to plug in certain capabilities or mid-sized firms with specialized technologies, it is too soon to tell. However, there will be a lot of decisions to make. But privacy and data security will be factored into every one of them. We want to ensure that Canadians’ trust in us is well-placed and that they can have access to their savings when they need them most, in a secure but also convenient manner.

John Rossi

Thank you Angela,

The Government has made a number of important changes to the deposit insurance framework.

These changes, which will take effect in two phases, include:

- Changes that modernize the scope of deposit insurance to better reflect products currently offered in the market by, for example expanding deposit insurance coverage to include eligible deposits in foreign currency & deposits with terms greater than 5 yrs.

These changes will take effect in April next year.

- The other changes, which include creating two new separate deposit insurance categories for Registered Education Savings Plans and Registered Disability Savings Plans and strengthening the rules for deposits held in trust and for nominee brokered deposits will take effect in April of 2021.

The changes to rules for trust deposits are particularly relevant for CDIC's aspiration to reimburse deposits on the same day in a failure.

I suspect that many of the people here have placed deposits with CDIC member institutions through a broker either directly with the brokerage firm or through their financial advisors.

You may not know that when a GIC or other deposit product is placed by a brokerage firm on a client's behalf with a CDIC member institution, the broker is typically acting as a nominee for that client.

And under the CDIC Act, these deposits are considered to be held in trust, and therefore the nominee broker is considered to be the trustee of the deposits and their client is the beneficiary.

This is a critical thing to understand from the perspective of deposit insurance because for a nominee brokered deposit to benefit from the full protection of CDIC deposit insurance, nominee brokers must take steps to meet several requirements, including transmitting to our member institutions essential information about their client beneficiaries. In turn, those member institutions receiving this information must record it, keep it current and be able to transmit it to CDIC in the event of a failure.

Let me explain why this is important. If a member institution fails, CDIC uses the deposit information held at the failed member institution to determine what amounts are to be reimbursed to depositors. For deposits held in trust, including nominee brokered deposits, this would include the beneficiary information available on the records of the member institutions.

Needless to say, it is critical that brokers, as trustees, correctly transmit this information to the member institution **and** keep it current and up-to-date, in order to allow CDIC to make prompt and accurate reimbursement of these deposits.

Some nominee brokers are better than others in this regard. And those who have invested in the data systems and business processes to ensure that CDIC members have the right information about their depositors – will have a higher-quality product than their competitors from the perspective of deposit insurance protection.

Unfortunately, this is not the case for many brokered deposits right now. There are many brokers who are not providing our member institutions with the information about their client-beneficiaries that CDIC requires to calculate coverage accurately.

For example, many brokers are providing account number instead of client identifiers which does not allow us to correctly aggregate deposits for broker beneficiaries.

This can impact the amounts that CDIC can reimburse brokers for their clients.

New Framework:

And this is precisely why the Government introduced the new changes to our Act focusing on nominee brokered deposits.

Let me provide some perspective:

Currently, nominee brokered deposits represent about \$80 billion or 32% of total deposit liabilities held as CDIC's small and medium-size members.

And we have approximately fourteen of our 84 members for whom nominee brokered deposits represent 40% or more of their total deposit funding.

This represents an exposure risk to CDIC that cannot be ignored, and a clear stability risk if we cannot payout these deposits quickly and accurately. The changes made to the CDIC Act affecting nominee brokered deposits that will be coming into force in 2021 will help ensure that CDIC can quickly and accurately calculate coverage for these deposits if we are faced with the situation of having to liquidate one of these institutions and reimburse depositors.

It does so by setting out clearly in the law, the information that needs to flow between brokers, our member institutions and to CDIC to ensure that we can protect these deposits and reimburse brokers accurately on behalf of their clients.

The new rules clarify the responsibilities that brokers and member institutions have for ensuring that the deposits they place for the clients are well protected by CDIC.

This includes hardwiring into the law as a requirement of coverage, that brokers disclose unique client IDs each time they place a deposit for a client and be able to provide CDIC with the names and addresses of their clients, post-failure.

This is complemented by requirements on our member institutions to correctly record this information and transmit it to CDIC when required.

Implementing the new CDIC Act requirements will help ensure that broker clients who place their funds in deposits get the full extent of protection under the CDIC Act.

CDIC is taking a proactive role in the implementation process and has established, in cooperation with key industry associations, an industry Brokered Deposit Advisory Group.

This Advisory Group will play a critical role in finding solutions to the inevitable challenges that brokers and CDIC members will face while implementing new requirements.

And we are looking forward to working with all of our brokered deposit stakeholders over the coming months towards helping ensure that these new requirements are properly implemented and complied with for the benefit of depositors in Canada and the financial system more generally.

Gina Byrne

Thanks John,

As Peter mentioned earlier, Canada was fortunate to avoid the worst effects of the global financial crisis – no banks failed here.

However, the crisis highlighted certain weaknesses in our financial system, including our readiness to handle the failure of very large banks. And this led to a transformation of CDIC's mandate.

For our first 40 years or so, CDIC handled the failure of smaller institutions using a somewhat common suite of tools: payout and liquidation, and the provision of financial support to aid the sale of a troubled member.

However, at that time we did not possess the legal tools necessary to resolve the failure of one of Canada's largest banks.

Following the 2008 crisis, CDIC was designated the resolution authority for these banks, known as Domestic Systemically Important Banks, or D-SIBs. This became official when our Act was amended in 2017.

The resolution of a large systemically important bank in Canada, while a remote possibility, would be an unprecedented, and high consequence event. An important component of CDIC's preparedness for such an event is the development and maintenance of resolution plans for our D-SIB member institutions. These plans set out a strategy and operational plan that could be implemented, in the event that their recovery actions fail.

CDIC considers it a priority to ensure that banks undertake the necessary work to create credible resolution plans. Planning for the resolution of a D-SIB is a challenging undertaking and we believe that the banks are best positioned to develop their own resolution plans based on their expertise, capabilities, and knowledge of their business.

As Canada's resolution authority, CDIC is responsible for reviewing these plans to ensure they are realistic and practical. CDIC's assessment of these plans is a core component of our approach to engage, guide and support the D-SIBs during the process.

In assessing the resolution plans we are seeking to promote a set of outcomes:

- We want reasonable clarity on the risks posed by the failure of the material aspects of a D-SIB's operation.
- We want D-SIBs to demonstrate that their operations and resources are structured in a fashion which promotes Canadian financial stability and the protection of Canadian depositors.
- We want the resolution strategies put forward by D-SIBs to reinforce confidence in the Canadian intervention and resolution regime.
- We want D-SIBs to present a meaningful set of divestiture and wind-down options.
- Any reliance on public sector stabilization measures to aid a D-SIB's resolution should be temporary and limited in scope.

In June 2017, the federal government made amendments to the CDIC Act that provided CDIC with a by-law making authority to incent banks to develop credible and feasible resolution plans.

Since then, CDIC has undertaken work to develop a new Resolution Planning By-law, which is expected to be brought into force later this Spring.

The By-law will provide a solid foundation on which CDIC will continue its work to ensure the D-SIBs become fully resolvable by our target date of 2020.

This is important work, and we are pleased by the level of engagement and collaboration that Canada's D-SIBs have showed so far.

That said, resolution planning is not – and cannot be – a one-and-done exercise.

We expect – indeed the By-law expects – that these plans will evolve and improve as time goes on. Harm reduction requires effective and on-going planning, and we will remain diligent in working with our members.

The cost of not having credible plans to resolve systemic banks, and the lack of options to take action in a manner that protected the financial system and the economy from damage, contributed to the extensive losses incurred during the financial crisis and its aftermath. We are fully aware that banks are incurring costs to develop these resolution plans and anticipate as banks become more resolvable and their plans mature, the cost of planning can be expected to decline in relative terms.

Our Resolution planning activities are not limited to DSIBs. CDIC also develops plans for the failure of medium-size institutions whose failure, while not systemic, should nevertheless be handled in a manner that poses as little disruption to depositors and the financial system as possible.

CDIC is committed to maintaining a safe and resilient financial system, and remains an active participant in strengthening the resolution framework both here in Canada and on the global stage.

And now I will call on Chantal Richer to talk about CDIC's public awareness activities.

Thank you.

Chantal Richer

Thank you Gina.

As you may know, one of the purposes of holding an Annual Public Meeting is to ensure Canadians know about what we do and how we do it.

It is part of a range of public awareness activities that CDIC undertakes as part of its mandate to protect depositors and support financial stability.

For example, many of you may have seen our colourful purple ads on TV, online, on social media platforms and in public transit zones.

And you may ask yourself why we advertise something that is free and automatic for depositors? This is a fair question, and one we get all the time.

We advertise because we have conducted behavioural research that clearly demonstrates we can significantly reduce the risk of a bank run in Canada by making depositors aware their money is protected by CDIC.

A summary of this research is available on our website and the correlation between awareness and the reduction of risk of bank runs is quite strong. If Canadian depositors know that their money is safe, they won't be inclined to panic in the event of a bank failure.

The corollary is also true, with enormous potential costs. If depositors are not aware of this protection, they are more likely to behave as if there is no deposit insurance and run. And in the context of a bank in trouble, this can quickly snowball.

This is what occurred in the UK in 2007, when Northern Rock Bank suffered the first bank run in that country in close to 150 years. When depositors heard the bank was in trouble, they lined up at branches and withdrew all their funds and the bank had to be bailed out by the UK government for close to \$80 billion Canadian.

The prime minister, Gordon Brown, described it later as his worst moment in Downing Street, and he, along with many others, will never forget the image of pensioners and savers, armed with flasks of tea and deckchairs, queuing for days outside the bank's branches.

Among the key reasons was that depositors were not aware of the deposit insurance scheme at the time.

We are constantly exploring new ways to ensure Canadians know about us so they know they are protected. It is much better to advertise in non-crisis periods, when people are more receptive to our message, than in periods of crisis when people are under stress.

Our own survey research suggests that Canadians would be up to 65% more likely to buy financial products that display our purple lock logo, just as the Energy Star logo or the Intel logo help guide the buying decisions of appliance and computer shoppers.

This is also why our CDIC logo is featured on bank websites, ATMs, screens in branches and on mobile apps – so Canadians can find out what is covered and what is not.

With on-line banking and social media – where information including misinformation can spread like wildfire - and people can transfer money with the press of a button, it becomes even more important that people know their money is safe with CDIC members. This dovetails with our T+0 goal. When CDIC can assure depositors they would have access to their funds the same day a member institution failed, it improves confidence, promotes stability in the financial system and reduces the risk of bank runs.

Peter Routledge – Part 2

Thank you Chantal.

As you have heard, CDIC is making key investments in the quality of its product.

If your bank runs into financial distress, we will be here to protect your savings.

Over the 50 plus years of our existence, we have handled 43 failures that touched over 2 million Canadians. And throughout that time not a single person has lost a single dollar that was protected by CDIC.

When they think of CDIC, many Canadians tend to think about receiving a cheque in the mail. This is how CDIC resolved all failures in its earliest years and is usually what the public thinks of as “insurance.”

And we still do this, much faster than in the past, but we have other tools that may be less disruptive for depositors, which we refer to as “non-payout resolutions.”

These tools operate less like insurance and more like deposit protection.

Under the right circumstances, CDIC can provide financial assistance to its members, including loans, guarantees, deposits, or loss-sharing agreements or by acquiring shares. CDIC can provide this assistance on a stand-alone basis, to assist in a private transaction, or in combination with any of its other resolution tools.

That means a failing institution may remain open for depositors, who can continue banking with no interruptions.

Likewise, when there is a willing buyer, CDIC can take control of a failing bank for a short period of time to complete its sale, merger or restructuring. The sale would ensure that insured deposits are protected. With the approval of the government, a forced sale would be used when shareholder consent of the transaction is not expected or the time to obtain consent would take too long.

If there is no private sector solution on the horizon, we can also create a bridge bank to “bridge” the gap between when an institution fails and when a buyer or private-sector solution can be found. CDIC can use this tool to transfer all or part of the failing bank’s business to a bridge bank, which is temporarily owned by CDIC.

As CEO of CDIC, I **have** to promote financial stability, and I’m thus attracted to the capacity of certain resolutions to help us do exactly that.

Pursuing some targeted resolutions – which are always and everywhere de-stabilizing – helps us overcome this conflict in executing our financial stability mandate.

For example, non-payout resolutions – a method advanced impressively by the FDIC since 2008 – have characteristics that align well with our financial stability objectives here in Canada.

This is something we must consider very carefully.

However, as Canadians look at the business news, and think about their futures and the security of their money, they should rest assured CDIC will be there to protect their savings at all our member institutions. If you want to know more, look for our purple logo wherever you save.

And now my colleagues and I will be pleased to answer any questions you may have.

Thank you.