Canadian Government Tables Bail-In Legislation

April 19, 2016

Bill C-15 includes provisions that would implement the long awaited bail-in legislation, i.e., the power to convert eligible liabilities of certain banks into common shares.

On April 20, 2016, the Government of Canada tabled Bill C-15 entitled *An Act to implement certain provisions of the budget tabled in Parliament on March 22, 2016 and other measures* (hereinafter "Bill C-15").

Significantly, Bill C-15 includes provisions that would implement the long awaited bail-in legislation, i.e., the power to convert eligible liabilities of certain banks into common shares.

In addition, among other things, Bill C-15 also proposes to amend the sunset provisions of certain Acts governing federally regulated financial institutions ("FRFIs") to extend by two years, namely, from March 29, 2017 to March 29, 2019, the period during which those institutions may carry on business. This extension will facilitate the next federal review of legislation governing FRFIs. Bill C-15 also proposes to amend the *Bank Act* to facilitate the continuance of local cooperative credit societies as federal credit unions, and implements several announcements contained in prior budgets with respect to the *Taxpayer Protection and Bank Recapitalization Regime.*

The focus of this BLG Bulletin will be the proposed bail-in powers. Set out below is some background information followed by a summary of the proposed amendments.

Background

Following the global financial crisis, the Financial Stability Board adopted a document entitled *Key Attributes of Effective Resolution Regimes for Financial Institutions* ("Key Attributes") in October 2011 (updated in October 2014). The objective of the Key Attributes is to put in place a special resolution regime for systemically important banks in order to reduce the risk of failure for these financial institutions and provide governmental authorities with the means to restore a bank to viability in the event that it should fail, without disrupting the financial system or economy and without using taxpayer money.

The Key Attributes recommended the adoption by its members of several tools to be used by resolution authorities to prevent another bail-out of a failing bank. In Canada, the resolution authority for banks is the Canada Deposit Insurance Corporation ("CDIC").

Several of the powers recommended in the Key Attributes are already held by CDIC. For example, CDIC's toolkit already includes the powers to ask the Cabinet of the Government of Canada (i) to order the transfer of the shares and subordinated debt of a bank to CDIC, (ii) to order the appointment of CDIC as receiver of a bank and (iii) to order the Minister of Finance to incorporate a bridge institution which will assume the failing bank's deposit liabilities.

However, conspicuously missing from CDIC's toolkit was the power to bail-in a domestic systemically important bank, i.e. to convert eligible liabilities of a bank into common shares.

In recent budgets, the Government of Canada announced its intention of implementing a bail-in regime for Canadian banks. In addition, the Government completed a consultation on this issue in the fall of 2014.

Principal Provisions of Bill C-15

Bill C-15 proposes to amend the *Canada Deposit Insurance Corporation Act* by adding the bail-in powers to CDIC's toolkit. However, the bail-in powers are only applicable to domestic systemically important banks ("D-SIBS"), while the other powers of CDIC noted above are available with respect to all financial institutions that are members of CDIC.

Bill C-15 also proposes to amend the *Bank Act* to provide that D-SIBS shall be those designated as such by the Superintendent of Financial Institutions.1 On March 26, 2013, the Superintendent of Financial Institutions identified Canada's D-SIBS as Bank of Montréal, The Bank of Nova Scotia, Canadian Imperial Bank of Commerce, National Bank of Canada, Royal Bank of Canada, and The Toronto-Dominion Bank.

The proposed bail-in powers would be triggered in the event that a report from the Superintendent of Financial Institutions to CDIC provided that a bank has ceased or is about to cease to be viable and that it cannot be restored to viability by the exercise of the Superintendent's powers under the *Bank Act*, even assuming the full conversion of the bank's non-viability contingent capital, although Bill C-15 is silent on this condition. Upon receipt of such a report, CDIC can request that the Minister of Finance recommend to the Cabinet that a conversion or winding-up order be made.

A conversion order may only be made if the Cabinet has also ordered that the shares and subordinated debt of the bank be vested in CDIC or has appointed CDIC as receiver of the bank.2 From the moment a vesting order is made or a receiver is appointed, all shareholders, subordinated debtholders, secured creditors and contractual counterparties of the bank are prevented from exercising their voting and other rights in any manner that could hinder the rights and powers of CDIC. In addition, a stay of proceedings protects the bank.3

The conversion order made by the Cabinet grants CDIC the power to convert or cause the bank to convert the bank's shares and liabilities into common shares of the bank. Bill C-15 does not mention which liabilities of the bank will be eligible for conversion into common shares. Such eligible liabilities will be detailed in regulations adopted by the Cabinet, together with the conversion formula to be applied for the conversion.4

The 2015 federal budget provided that deposit liabilities should be excluded from the conversion powers, and that such conversion powers should only apply to unsecured debt that is tradable and transferable, with an original term to maturity of 400 days or more. The 2015 federal budget also provided that the conversion power would only apply to liabilities issued or renegotiated after the implementation date set by the Government. Bill C-15 now specifies that the Cabinet of the Government of Canada may subject shares and liabilities to the conversion power if they were issued before the day on which the bail-in power is implemented, if such shares and liabilities are amended or their term is extended in the case of liabilities.5

Shareholders or debtholders that see their interest being converted are entitled to receive compensation.6 The compensation mechanism will be implemented by the Government in regulations. The compensation mechanism will ensure that the "no creditor worse off" principle is respected. In essence, this principle requires that no shareholder or debtholder be in a financial situation worse after conversion than the one they would have been in had the bank been wound-up. CDIC will be responsible for paying the compensation.

Contact Us

If you would like to know more about Bill C-15, have any questions regarding Bill C-15 and how it affects your business or would like any assistance in commenting on the proposed legislation, please do not hesitate to call or write any member of the Financial Services Regulatory Group.

1 Sections 156 and 159 Bill C-15 amending Section 2 and adding Section 484.1 of the *Bank Act*.

2 Section 131(3) Bill C-15 adding subsection 39.13(1.2) to the *Canada Deposit Insurance Corporation Act*.

3 Section 131(9) Bill C-15 amending subsection 39.13(4.1) of the *Canada Deposit Insurance Corporation Act*.

4 Section 139(3) Bill C-15 amending subsection 39.2(2.3) of the *Canada Deposit Insurance Corporation Act*.

5 Section 139 (4) Bill C-15 adding subsections 39.2(10) and 39.2(11) to the *Canada Deposit Insurance Corporation Act*.

6 Section 139(6) Bill C-15 amending subsection 39.2(9) of the *Canada Deposit Insurance Corporation Act* and Section 142 Bill C-15 amending sections 39.23 to 39.37 of the *Canada Deposit Insurance Corporation Act*.

By

Stephen J. Redican, Olivier Tardif, Jeffrey S. Graham

Expertise

Banking & Financial Services, Financial Services

BLG | Canada's Law Firm

As the largest, truly full-service Canadian law firm, Borden Ladner Gervais LLP (BLG) delivers practical legal advice for domestic and international clients across more practices and industries than any Canadian firm. With over 725 lawyers, intellectual property agents and other professionals, BLG serves the legal needs of businesses and institutions across Canada and beyond – from M&A and capital markets, to disputes, financing, and trademark & patent registration.

blg.com

BLG Offices

Calgary

Centennial Place, East Tower
520 3rd Avenue S.W.
Calgary, AB, Canada
T2P 0R3

T 403.232.9500
F 403.266.1395

Ottawa

World Exchange Plaza
100 Queen Street
Ottawa, ON, Canada
K1P 1J9

T 613.237.5160
F 613.230.8842

Vancouver

1200 Waterfront Centre
200 Burrard Street
Vancouver, BC, Canada
V7X 1T2

T 604.687.5744
F 604.687.1415

Montréal

1000 De La Gauchetière Street West
Suite 900
Montréal, QC, Canada
H3B 5H4

T 514.954.2555
F 514.879.9015

Toronto

Bay Adelaide Centre, East Tower
22 Adelaide Street West
Toronto, ON, Canada
M5H 4E3

T 416.367.6000
F 416.367.6749