Department of Finance Launches Second Round of Consultations on Reform of Federal Financial Institution Statutes

August 16, 2017

The Canadian Department of Finance ("Department") has released a paper entitled Potential Policy Measures to Support a Strong and Growing Economy: Positioning Canada's Financial Sector for the Future ("Paper"). The Paper launches the second stage of the renewal of Canada's federal financial institutions statutes. The Department is consulting on potential policy measures that could lead to consideration of legislation in Parliament prior to the statutory sunset date of March 29, 2019, or inform the Department's longer-term approaches to the financial sector.

Background

The Department notes that it began the first stage of the renewal process with the release of a consultation paper on August 26, 2016. The first paper set out the landscape of Canada's financial sector and identified key trends that may influence future directions. The Department indicates that it heard from a diverse range of stakeholders and the Paper takes into account its comments and recommendations.

The Department notes that the Paper seeks views on whether and how to implement potential policy measures, as well as on policy directions for future work under the following four themes: supporting a competitive and innovative sector; improving the protection of bank consumers; modernizing the framework; and safeguarding a stable and resilient sector. In addition, the Department indicates that it will undertake targeted stakeholder consultations on separate technical and consequential changes that could be made to the federal financial institutions statutes to ensure they remain up to date and sound.

The Department seeks comments on the Paper by September 29, 2017. We summarize the themes discussed in the Paper below.

Supporting a Competitive and Innovative Sector

The Paper notes that the Government of Canada has clearly defined a growth agenda to build an inclusive economy and support the middle class. The Department notes that

a competitive and innovative financial sector has an important role to play in driving this agenda.

The Department indicates that it is seeking input on near-term measures that are stated to be as follows: clarifying the FinTech business powers of financial institutions; facilitating FinTech collaboration by removing obstacles to collaboration between FinTechs and financial institutions; and streamlining the bank entry and exit framework. The Department notes that views related to the current outsourcing framework applicable to federally regulated financial institutions should be directed to the Office of the Superintendent of Financial Institutions ("OSFI").

In addition, the Department intends to examine the merits of open banking — a framework under which consumers have the right to share their own banking information with other financial service providers — and will seek the views of stakeholders.

In an effort to improve regulatory transparency and coordination, the Department notes that the Government of Canada and federal regulatory agencies are committed to working with provincial and territorial regulatory authorities to better coordinate and share information, a key concern of many FinTech companies.

The Department also signals that over the longer term, it will consider the current balance of economic growth and risk management and whether refinements are needed to better position the sector to be competitive and innovative. In this regard, the Department notes that it intends to analyze the contribution that small and mid-sized banks can make to increasing capital formation and efficient credit allocation, which are important financial functions that can stimulate the Canadian economy.

Improving the Protection of Bank Consumers

The Department notes that in 2016 it proposed measures to strengthen the protection of bank consumers. The measures covered five areas: access to basic banking services, business practices, information disclosure, complaints handling, and governance and public accountability. In the Paper, the Department notes that certain related initiatives are underway. The Financial Consumer Agency of Canada ("FCAC") is, at the request of the Minister of Finance, examining best practices in financial consumer protection across Canada. The Department notes that the FCAC is also reviewing bank sales practices to assess whether sales targets and incentives are contributing to poor outcomes for consumers.

In addition, OSFI is reviewing domestic retail sales practices at domestic systemically important banks, and is focusing on risk culture, the governance of sales practices, and how banks manage the potential reputational risk inherent in sales activities. The Department indicates that these reviews will help inform potential policy measures to strengthen the framework and improve protections for bank consumers, building upon the measures proposed in 2016.

Modernizing the Framework

The Department notes that to accommodate the changing needs of institutions — and enable them to adapt to an evolving business environment — flexibility has been

incrementally incorporated into the federal financial sector framework over time. In this regard, the Department notes that it is considering whether to permit federally regulated life and health insurers to have additional investment powers in infrastructure.

The Department notes that it is also considering whether to align the federal statutes — which are tailored to reflect the unique nature of financial institutions — with the proposed changes to the *Canada Business Corporations Act* across a number of areas. For example, the Department is seeking views on whether to implement a "comply or explain" model to promote the participation of women on boards of directors and in senior management of federally regulated financial institutions. The Department is considering whether to change the federal financial institutions statutes so as to establish annual elections (two years for smaller institutions) mandate individual director elections, and introduce majority voting in uncontested elections. Further, the Department is considering the merits of allowing federally regulated financial institutions to choose to adopt the notice and access system established by provincial-territorial securities regulators. In addition, the Department is seeking views on whether to strengthen corporate transparency by prohibiting bearer shares and bearer share warrants under the federal financial institutions statutes. It is also seeking views on whether to maintain or repeal the *Cooperative Credit Association Act*.

Another issue on which the Department is seeking input is whether prudentially regulated non-bank deposit-taking institutions should be given flexibility to use the terms "bank" or "banking" to describe their activities and services in appropriate circumstances. As a result of the inclusion of this issue in the Paper, OSFI has issued a notice suspending the compliance expectations set out in its June 30, 2017 cover note to Advisory 2017-01 — Restrictions on the use of the words "bank", "banker" and "banking".

Safeguarding a Stable and Resilient Sector

The Department indicates that it continues to be interested in measures to safeguard the stability and resiliency of Canada's financial sector. In this regard, it is considering measures regarding the ability of Canada's property and casualty insurance sector to cope with a low-probability, high-impact earthquake. The Paper notes that Department is considering how to limit the system-wide risks an extreme earthquake could pose to federal property and casualty insurers, and will be consulting with provinces, territories, and stakeholders. It also sets out work being undertaken by the Department in the areas of life insurance resolution, cyber risk, and climate risk disclosure. In addition, the Paper notes that the FCAC intends to improve consumer education products related to catastrophic risk and insurance to develop consumer awareness of insurance products and consumer rights and responsibilities, and will seek out opportunities to collaborate with provincial and territorial governments.

Technical Issues

An annex to the Paper sets out for comment potential policy measures of a more targeted nature to the federal financial sector framework. Specifically, the Department is seeking feedback on the following issues: OSFI information publication requirements; reforms of the unclaimed balance requirements of the Bank of Canada; regulation of nuclear insurance; record keeping requirements of foreign insurers, three-party structured settlement agreements; Ministerial approvals of significant interests;

electronic meetings; advanced voting; proposals of members of federal credit unions; access to federal credit union membership lists by members; the related party regime; permitted credit exposures; the substantial investments regime; large asset transactions and the Canada Deposit Insurance Corporation's claims in liquidation.

Further Comments

The agenda for reform briefly described above is both ambitious and wide-ranging. The interest of the Department in supporting the Government of Canada's innovation agenda is welcomed and urgent. FinTech is an increasingly important global area of change and Canada is well positioned to be a leader in the development and implementation of Fintech for the benefit of Canadian consumers, the Canadian financial system and the Canadian economy as a whole. Undoubtedly, in the upcoming consultations regarding the Paper, the Department will hear from many stakeholders interested in FinTech, both regulated entities and FinTech companies. The examination of the merits of open banking is a discussion of considerable importance to many FinTech companies.

The fate of the changes to the federal consumer protection framework will depend on both the important work being done by the FCAC and OSFI. It will also undoubtedly be influenced by political considerations to the extent that the outcome of such work and policy recommendations lead to efforts to in some way supplant provincial jurisdiction. This is an area where coordinated discussions between the Government of Canada and the governments of the provinces would seem sensible and helpful.

Implementation of many of the issues that are on the modernization agenda of the Department will be welcomed. The efforts at modernization are fully consistent with the Department's efforts to ensure that the regulatory structure is efficient and up-to-date. The focus on the stability and resilience of the sector is a continuing theme of policy makers and regulators that was a consequence of the 2007-2008 global financial crisis. It is perhaps worthy of note that legislators and regulators in the United States are looking at ways to reduce the heightened regulatory burden that has been imposed as a consequence of the 2007-2008 global financial crisis. It is not clear that the Department is proposing any similar review of what has been implemented over the past decade.

Finally, the Paper does not refer to the other recent Department paper regarding reform of the retail payments system. This presumably reflects the fact that the payments reform process is on a separate timetable, likely to conclude prior to the reforms contemplated by the Paper.

Contact Us

If you would like to know more about the Paper, have any questions regarding the proposals contained in the Paper and how they affect your business or would like any assistance in commenting on the Paper, please do not hesitate to contact the authors or any member of BLG's Financial Services Regulatory Group. Comments can be submitted to the Department up to September 29, 2017.

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