

# Bridge bank backgrounder



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## Bridge bank context

When a member institution is non-viable in the opinion of the Superintendent of Financial Institutions, CDIC may establish a temporary bridge bank. In such cases, CDIC must transfer all insured deposits to the bridge bank to contribute to its viability and preserve financial stability. It may also transfer uninsured deposits and other assets and liabilities of the failing institution. Any assets and liabilities it chooses not to transfer, including “bad” assets that are not critical and certain liabilities such as subordinated debt, are left behind for liquidation in the failed institution.

The key objectives of a bridge bank are to maintain critical services and continue operations that are important for financial stability. This minimizes disruptions to the financial system that might otherwise occur if those functions were subject to wind-up and liquidation procedures.

## Bridge bank steps

- The Superintendent of Financial Institutions concludes that a member institution is not viable and reports this to CDIC’s board.
- CDIC’s board reviews the various options and recommends the best resolution approach for the failing bank to the Minister of Finance.
- The Minister of Finance recommends a resolution approach to the Governor in Council (GIC), i.e., the federal Cabinet.
- The GIC makes an order authorizing the resolution approach.

When the decision is made to establish a bridge bank, the GIC appoints CDIC as the failed institution’s receiver. In its order establishing the bank, the GIC specifies when the deposit liabilities will be assumed by the bridge bank.

In pursuing this course of action, CDIC looks not only at financial stability and confidence in the financial system, but also factors like execution risks, costs, and exposure to and size of the loss. It also considers whether:

- the CDIC board, the Minister of Finance and the GIC deem it undesirable to allow the member to be closed;
- it is important to ensure continuity of service;
- the institution has value that a bridge bank can preserve or enhance; and
- the institution has failed on short notice.

The bridge bank spans the time between when the institution failed and when a sale of the bridge bank or its assets can be completed. Unlike with a forced sale tool, a bridge bank may be used when there are no immediate private sector acquirers.

The bridge bank model is especially suited for member institutions that deteriorate rapidly with little notice and where a potential buyer does not emerge and there are financial stability concerns. It stabilizes the situation for depositors and transfers all creditors to the bridge bank.

## Bridge bank setup

This is how bridge bank setup usually unfolds:

- CDIC is appointed as receiver of the failed institution.
- It asks the Minister to incorporate a bridge bank.
- The letters patent incorporating the bridge bank are made on a Friday night after the close of the Large Value Transfer System clearing cycle.

The bridge bank—a new legal entity wholly owned by CDIC—is authorized by the Superintendent to commence and carry on business immediately on Friday.

As the receiver of the failed institution, CDIC decides which assets and liabilities should be passed on to the bridge bank. This would include all insured deposits at a minimum. All creditors passed on to the bridge bank receive full and uninterrupted access to their funds.

The idea is for the bridge bank to be the “good bank,” leaving the stub of the failing member institution as a “bad bank.” All assets left behind in the “bad bank” are then liquidated in a court-supervised process, with creditors receiving their share of any money recovered as the assets are sold off.

CDIC may decide to transfer only those assets and liabilities necessary to preserve essential services or may transfer all assets and liabilities to keep the institution whole.

Once CDIC has substantially transferred the assets and liabilities to a bridge bank, it applies for a winding-up order of the failed institution under the *Winding-up and Restructuring Act*.

CDIC provides any financial assistance the bridge bank needs to discharge its obligations. To do this, CDIC can draw from its investment portfolio and exercise its borrowing authority under the *CDIC Act*. Additional borrowings, if needed, can be authorized by Parliament.

CDIC has authority over the bridge bank's board of directors. If it so chooses, it may remove and replace the failing institution's board and senior management when the bridge bank is set up.

A bridge bank will be run much like any bank, by a board of directors and an executive team chosen for their ability to lead the bridge bank through restructuring and back to the private sector. Executives and directors may be drawn from the bank itself or its own succession planning, as well as from CDIC's stand-by executive roster, consisting of highly experienced financial sector leaders who stand ready to take on a challenging role and support the stability of the financial system in Canada.

The GIC may exempt the bridge bank from application of any provision of the *Bank Act* or certain other statutes.

The bridge bank should not be viewed as a "competitor" to other banks. The goal is to return the bridge bank to the private sector as soon as possible through one or more transactions (e.g., sale to a third party or amalgamation with another bank). The pricing of loans and deposits at the bridge bank and various fees are expected to be roughly equivalent to industry norms.

## Bridge bank duration

Bridge banks are intended to be in existence for up to two years, but the GIC may grant up to three one-year extensions, for a total of five years. This period is an opportunity to "clean up" the institution and market it to prospective buyers, and for buyers to conduct due diligence. Once it expires, the bank ceases to be designated as a bridge bank.

## Stays

When a bridge bank is ordered set up, the *CDIC Act* imposes a general stay of proceedings that overrides contractual rights under Canadian law, similar to the protections afforded to receivers and trustees in bankruptcy under insolvency legislation. The stay is to allow sufficient time to set up the bank and stabilize the situation. Generally speaking, all legal proceedings and general contract termination and enforcement rights are temporarily stayed in a bridge bank scenario, subject to certain exceptions for eligible financial contracts (or EFCs) and the obligations of Payments Canada members.

## Exit options

- a) Share sale/recapitalization: bridge bank shares are sold to a third party, which injects additional capital, subject to Ministerial approval and ownership concentration issues.
- b) Purchase and assumption: bridge bank assets and liabilities are transferred to and assumed by one or more purchasers.
- c) Amalgamation: the bridge bank is amalgamated with another institution subject to Ministerial approval and ownership concentration issues.