Consultation on CDIC Differential Premiums By-law

Sector Brief

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Summary

On January 18, 2025, the Canada Deposit Insurance Corporation (CDIC) launched a 30-day consultation on its *Differential Premiums By-law (By-law)* through the Canada Gazette.

The proposed updates would implement the most recent strategic review (2021–2023), where CDIC's Board of Directors concluded that the following changes should be made to the Differential Premium System (DPS):

- increasing the number of premium categories from four to five;
- updating the policy for the classification of new member institutions;
- increasing the frequency of CDIC's risk assessment from an annual to a semi-annual classification for the purpose of determining each member institution's annual premium; and
- improving the risk sensitivity of the differential premium scorecard by making changes to the qualitative and quantitative criteria.

Following a 90-day consultation in July 2022, CDIC published the results of its review in July 2023. Please see CCUA's summary attached.

The change to increase premium categories would take effect on April 1, 2025; however, the first semi-annual classification would come into force on April 29, 2026. Accordingly, the first fall return must be submitted to CDIC by October 31, 2026. The first annual premium determined under the new semi-annual classification framework would be for the premium year that begins on May 1, 2027.

The new member classification may be of particular interest to PCUs contemplating – or in the process of pursuing – federal continuance or a merger with an FCU. CCUA is confirming the details of this measure with CDIC and it may be a point of advocacy in CCUA's submission.

Please provide your comments to mpaulgaard@ccua.com by Wednesday, February 5th to meet the Department's deadline of February 17, 2025.

Key Topics

i) Increasing Premium Categories from Four to Five

CDIC proposes to increase the number of categories from four to five. This is in line with its proposal and feedback received during the 2022 consultation. The stated intent of the additional category (i.e. ≥ 90) is to improve differentiation and reduce cross-subsidization of risk. Under the four-category matrix, CDIC found that a large and increasing majority of members have been classified in the top premium category (i.e., ≥ 80). For example, in 2021 and 2022, 90% and 92% of members fell in this category respectively.

Score	Premium Category
≥ 90 [1]	1
≥ 80 but < 90	2
≥ 65 but < 80	3
≥ 50 but < 65	4
< 50	5

ii) New Member Policy

Per the proposed By-law, new member institutions are institutions that have been operating as members for less than two full premium years. The proposed By-law would require new member institutions to be classified in Premium Category 2 (i.e., ≥ 80 but < 90), subject to certain exceptions. The consultation states that the classification in Premium Category 2 is because a new member institution has an unproven track record as a CDIC member against its status as a federally regulated, deposit-taking institution.

The proposed By-law includes a transitional provision that would allow member institutions that become new member institutions before the proposed By-law comes into force to be grandfathered in Premium Category 1 until they are no longer considered new.

If OSFI assigns that institution a stage of intervention, however, the new member institution must be classified in Premium Category 3 (i.e., ≥ 65 but < 80) for its annual premium.

However, it appears that the CDIC has made two changes, which may prove challenging for credit unions. First, following the 2022 DPS consultation, CDIC recommended an exemption to the new member policy, which would enable new institutions to opt out of the new member policy after the first year, provided they provide three years of historical data (p. 8). If the data is unavailable, they will continue to be subject to the new member policy for the second year. In 2023, the above exemption was of particular interest to PCUs contemplating federal continuance and those credit unions already on their continuance journey. It appears that this exemption may have been omitted from the proposed By-law. CCUA is confirming this with CDIC. As a result, this matter may be a point of advocacy.

Second, the By-law appears to add an additional challenge for FRFIs who amalgamate with non-FRFIs. A member institution formed by an amalgamation must—if all its amalgamating member institutions would be new if they were still operating—be classified in premium category 2. CCUA is again confirming this provision with CDIC, and it may also be a point of advocacy.

iii) Semi-annual classification

The proposed By-law would increase the frequency of CDIC's classification of each member institution from an annual classification to a semi-annual classification. The stated intent is to ensure that intra-year changes in a member institution's risk profile are appropriately captured and that they incentivize member institutions to promptly address any identified issues to reduce their overall annual premiums.

Under the proposed By-law, each member institution would be classified into a premium category as of January 15 of each year, based on information submitted October 31st the previous year, and as of July 15 of each year, based on information provided by April 30 of the

[1] New category.

same year. CDIC would be required to notify member institutions of their classification by January 15 and July 15. For each classification, CDIC must determine the sum of the member institution's quantitative and qualitative scores.

In its 2022 consultation paper, CDIC proposed that premiums be issued on a quarterly basis. However, most feedback suggested that quarterly DPS reporting could add burden for relatively little benefit, and that it would present disproportionate burden to smaller institutions. Quarterly financial data may also be more volatile. As a result, the frequency changed to twice annually.

iv) Qualitative scores

For both the January 15 and July 15 classifications, the qualitative score would be determined by an examiner's rating, which is assigned by the Office of the Superintendent of Financial Institutions (OSFI), and a new Risk and Resolvability Score (RRS) that would be assigned by CDIC. The RRS would replace the CDIC component of the qualitative criteria under section 30 of the current By-law.

The five-point scale of the examiner's rating would be replaced by an eight-point scale with an associated maximum of 25 points instead of 35 points. This change is consistent with OSFI's *Supervisory Framework*, which provides for Overall Risk Ratings based on an eight-point scale.

The maximum of 5 points associated with the CDIC component would be replaced by a maximum of 15 points that could be assigned by CDIC for the RRS. The RRS takes the following into consideration: CDIC's internal risk assessment of member institutions; compliance with sections 2 to 4 of the *Canada Deposit Insurance Corporation Data and System Requirements By-law*, and in the case of a D-SIB, the compliance of their resolution plan with the *Canada Deposit Insurance Corporation Resolution Planning By-law*.

v) Quantitative criteria

To strengthen risk differentiation among member institutions, the proposed By-law would make a number of changes to the quantitative criteria and their corresponding scoring thresholds. These changes include

- the removal of the Stress-Tested Net Income and Efficiency Ratio metrics, given that they are closely correlated to other metrics;
- the introduction of five new metrics to capture a member institution's liquidity and funding risk. For domestic systemically important banks (D-SIBs), these include the Liquidity Coverage Ratio and the Net Stable Funding Ratio. For other member institutions, the new metrics are the following: the High Quality Liquid Assets to Short-Term Funding Ratio, the Stable Funding Ratio, and the Brokered Deposit Ratio; and
- the introduction of separate quantitative criteria for D-SIBs and Category I, II, and III small and medium-sized deposit-taking institutions. This change is consistent with OSFI's *Small and Medium-Sized Deposit-Taking Institutions (SMSBs) Capital and Liquidity Requirements – Guideline* (2023*Assessing the annual premium*

vi) Scorecard Changes

Under the proposed By-law, for each classification, CDIC must determine the sum of the quantitative and qualitative scores described above to classify the member institution into one of the five premium categories and assign to that member institution a corresponding premium rate. Next, CDIC must determine the average of the member institution's two premium rates, based on its January 15 and July 15 classifications, and apply the following formula to assess the member institution's annual premium:[2]

A × B × (C + D) ÷ 2, where

A is 1/3 of 1% of the member institution's volume of insured deposits;

B is the volume of insured deposits as of April 30 in the immediately preceding premium year;

C is the premium rate that corresponds to the member institution's premium category as of its January 15 classification; and

D is the premium rate that corresponds to the member institution's premium category as of its July 15 classification.

Conclusion

The forms for the fall and spring returns will be published in the Differential Premiums Manual (Manual) on CDIC's website. CDIC will update the Manual before the first fall return submission deadline of October 31, 2026.

Please provide your feedback to mpaulgaard@ccua.com by Wednesday, February 5, 2025.

[2] The proposed twice-per-year formula is similar to the current annual formula, which is as follows: A × B × C, where:
- A is the legislated maximum premium rate (33bps of a member's volume of insured deposits),
- B is the volume of insured deposits (i.e. current assessment base), as at April 30,
- C is the risk-based rate determined pursuant to the Differential Premiums By-law assessment.