Canada Deposit Insurance Corporation

CDIC

Protection for Your Clients

CE Module

OBJECTIVE

Could you imagine the dismay of depositors when they learn that the financial institution they placed their money into has just failed and that some of their investment products are not protected?

To avoid any unpleasant surprise and ensuing hardship, the following online self-study program has been developed to assist financial advisors to better understand deposit insurance and the role CDIC plays in protecting depositors in the event of a financial institution's failure. To many consumers, protection of their savings is a key element in their decision as to how to invest their money. This course provides useful information on deposit insurance, in particular what is and what is not insured, with a view to enable advisors in the course of their business to better advise clients on the financial protection available to them.

CE CREDITS

- For details on course credits available, please go to www.cdic.advisorce.com

INSTRUCTIONS

This course is a simple 8-page "read and learn" program. The examination component is composed of 15 multiple-choice questions. The questions are based on material found in the course, many of which are word-for-word.

An informed client is a better client!

On June 4, 1996, about 2,600 Canadians discovered that their savings were not immediately available from their financial institution. They had entrusted a total of $42 million in deposits to Calgary-based Security Home Mortgage Corporation, which had now closed its doors for good. The news must have momentarily sent a shiver of fear through each one of this financial institution's clients. Fortunately, this failed financial institution was a member of the Canada Deposit Insurance Corporation (CDIC) and, in this instance, ***all but $10,000 of the deposits was insured***. Within a span of three weeks, CDIC made payment of all insured deposits.

Since its creation in 1967, CDIC has stepped in to help depositors following the failure of 43 member institutions like Security Home. In fact, during the past four decades, it has protected more than two million people holding about $26 billion in insured deposits at these failed institutions. Yet many investors are unaware of the tremendous benefits of CDIC insurance when a member institution fails. By communicating these benefits to your clients, you can reassure them that all or a portion of their life savings will be protected even if the financial institution that holds their eligible deposits becomes insolvent.

What is CDIC?

CDIC is a federal Crown corporation. It provides insurance to depositors against the loss, in whole or in part, of deposits made at member institutions, namely banks, trust companies, loan companies and deposit-taking associations to which the Cooperative Credit Associations Act applies, in the event of their failure. It's important to note that credit unions and caisses populaires are members of provincial, not federal, deposit insurance organizations in their respective provinces, and are therefore not part of CDIC's mandate.

CDIC does not receive federal tax dollars to finance its operations and any necessary payments to depositors. Instead, its funding comes directly from the premiums paid by member institutions. However, it is accountable to Canada's Parliament through the Minister of Finance. The Corporation's actions are governed by the Canada Deposit Insurance Corporation Act, which describes CDIC's objectives and powers. CDIC is also empowered to pass its own by-laws dealing with various matters.

CDIC is an internationally recognized deposit insurer and many countries have been eager to learn from CDIC's experience as they adopt their own deposit insurance to protect small depositors and maintain confidence in institutions that accept deposits.

A complete list of CDIC member institutions is available at www.cdic.ca

How does deposit insurance work?

When investors place money in eligible deposits they are automatically insured to a maximum basic coverage limit of $100,000, including principal and interest. This amount was raised from $60,000 in the 2005 federal budget. In addition, separate coverage of up to $100,000, including principal and interest, is available for each of the following: eligible deposits held in joint accounts, in trust, in Registered Retirement Savings Plans (RRSPs), and in Registered Retirement Income Funds (RRIFs).

Eligible deposits must be:

- in Canadian currency, payable in Canada;
- repayable no later than five years from the date of deposit; and
- placed at a financial institution that is a CDIC member.

Deposits that are not insurable include foreign currency deposits (such as accounts in U.S. dollars) and term deposits that mature more than five years after the date of deposit. Mutual funds, stocks, notes, bonds and certain debentures issued by corporations (including member institutions), Treasury bills and bonds issued by governments and investments in mortgages are not deposits.

Basic Coverage

Basic coverage applies to a depositor's eligible savings and chequing accounts. It also covers eligible term deposits, including Guaranteed Investment Certificates (GICs), as well as money orders, drafts and certified cheques.

EXAMPLE

Your client has the following deposits at a CDIC member institution:

- Canadian dollar savings account worth $15,000, including interest earned
- Five-year GICs worth $20,000, including interest earned
- U.S. dollar savings account worth $10,000
- Mutual fund investments worth $15,000

Only the Canadian dollar savings account and five-year GICs are eligible for deposit insurance, so your client will receive $35,000 if the institution fails.

Joint Deposits

Deposits that your clients hold jointly with someone else are eligible for separate coverage as long as the member institution's records state that the deposits are jointly owned and identify the name and address of each joint owner. Joint owners are collectively (not separately) eligible for a maximum of $100,000 in coverage.

EXAMPLE

Your client has the following joint deposits at a CDIC member institution:

- Eligible deposits worth $75,000 held with a spouse
- Eligible deposits worth $75,000 held with a spouse and a child
- Eligible deposits worth $125,000 held with two business partners

The $75,000 held by your client with a spouse is eligible for separate deposit insurance. So is the $75,000 held with the spouse and a child. In addition, $100,000 of the $125,000 held with the two business partners is protected. A total of $250,000 of your client's joint deposits will be reimbursed if the institution fails.

Deposits Held in Trust

Trust deposits with the same trustee(s) and beneficiary(ies) may be eligible for separate coverage of up to $100,000 provided that the member institution's records state that the deposits are held in trust, identify the name and address of the trustee(s) and beneficiary(ies), and, if there is more than one beneficiary, disclose the amount or percentage of each beneficiary's interest in the trust. (However, CDIC can decline to cover a trust deposit if the trust was set up primarily to obtain or increase deposit insurance coverage.)

EXAMPLE

Your client has the following trust deposits at a CDIC member institution:

- Eligible deposits worth $150,000 held in trust for three children, each of whom has a one-third interest in the trust

The full $150,000 is insurable in favour of the trustee of the trust because each beneficiary's share ($50,000) is less than the $100,000 maximum coverage available in respect of each beneficiary.

Deposits Held in RRSPs

Eligible deposits held in RRSPs, such as term deposits, are eligible for separate coverage of up to $100,000. Multiple RRSP accounts held by one annuitant are collectively (not separately) eligible for a maximum of $100,000 in coverage. In the case of a spousal RRSP, eligibility is calculated based on the total RRSP deposits of the annuitant, namely the spouse, and not of the contributor.

EXAMPLE

Your client and your client's spouse have the following RRSP deposits at a CDIC member institution:

- Five-year GICs that your client contributed to his/her RRSP worth $95,000 at maturity
- Mutual funds that your client contributed to his/her RRSP worth $225,000
- Three-year GICs worth $80,000 at maturity that your client's spouse contributed to his/her own RRSP
- Three-year GICs worth $35,000 at maturity that your client contributed to his/her spouse's RRSP

Your client's mutual fund investments are not protected by CDIC, as mutual funds are not deposits; however, the GIC deposits worth $95,000 (including interest) in your client's RRSP are insurable. Your client's spouse's RRSP deposits would be added together (as the spouse is the annuitant of both the deposits contributed by your client to the spousal RRSP and those contributed by the spouse to his/her own RRSP) to determine eligibility ($80,000 + $35,000 = $115,000); the maximum total of $100,000 will be reimbursed if the institution fails, leaving $15,000 unprotected by deposit insurance.

Visit www.cdic.ca for more information

You and your clients can find valuable additional information about CDIC and deposit insurance at www.cdic.ca, including a Deposit Insurance Calculator, an up-to-date list of CDIC member institutions, a news archive and a variety of online publications. The website also features links to other organizations that may be of interest to advisors and their clients, including Canadian supervisory organizations for financial institutions, provincial deposit insurance corporations, other consumer financial agencies and international organizations.

Deposits Held in RRIFs

Eligible deposits held within RRIFs, such as term deposits, are eligible for separate coverage of up to $100,000. This insurance is in addition to coverage for a depositor's eligible RRSP savings at the same member institution.

EXAMPLE

Your client has the following RRIF deposits at a CDIC member institution:

- Savings account worth $8,000
- Sixty-day term deposits worth $20,000 at maturity
- One-year term deposits worth $50,000 at maturity
- Mutual funds worth $22,000

Your client's mutual fund investments are not protected by CDIC, as mutual funds are not deposits. The remaining deposits, valued at $78,000 on maturity, are insurable and will be reimbursed if the institution fails.

If your client has detailed questions on deposit insurance, you can invite them to contact CDIC's toll-free information line at 1-800-461-2342, or you can call CDIC on their behalf to get further details about deposit insurance.

What happens when two institutions merge?

Your clients' deposit insurance coverage may be affected when two member institutions merge. The *Canada Deposit Insurance Corporation Act* defines an amalgamation as either:

- the merger of two or more CDIC member institutions into one, which continues business as a single member institution; or
- the acquisition of deposits from a CDIC member institution by another member institution.

Common ownership of two member institutions, as long as each retains its separate identity and CDIC membership and no deposits are assumed by the other, is not considered an amalgamation. Neither is a merger or transfer of deposits between a member institution and a non-member.

Following an amalgamation, eligible demand deposits (e.g., savings and chequing accounts) made before the merger continue to be insured separately until clients withdraw money from their accounts. Eligible term deposits (e.g., GICs) made before the merger continue to be insured separately until they mature or are redeemed. Eligible deposits made after the merger are only insured if the combined total of all deposits, including the remaining balance of the deposits that existed at the time of the amalgamation, does not exceed $100,000.

EXAMPLE 1

Your client has the following eligible deposits at the time of amalgamation:

- At member institution A, a total of $50,000
- At member institution B, a total of $75,000

After the amalgamation, the full $125,000 will continue to be insured — but that amount will decrease as your client withdraws money or term deposits mature until the insured deposits at the merged institution reach the $100,000 maximum. New deposits will not be insured until the total amount of insured deposits that existed at the time of the amalgamation drops below $100,000.

EXAMPLE 2

Your client has the following eligible deposits at the time of amalgamation:

- At member institution A, a total of $25,000
- At member institution B, a total of $45,000

If your client deposits an additional $40,000 in the amalgamated institution, he or she will only be insured up to the $100,000 maximum. A portion of the new deposit – $10,000 – will not be insured.

What happens when an institution fails?

As soon as possible after the failure of a member institution, CDIC sets up a dedicated toll-free number that depositors can call for information and to request an advance payment out of their insured balance if there is some urgent need. CDIC also sends out letters to depositors explaining how they will receive their reimbursement. Your clients do not have to file a claim to receive this money. Depositors usually receive their payment within two months, either by cheque in the mail or by direct deposit into a new account in their name set up by CDIC at another member institution.

In the case of RRSPs and RRIFs, CDIC makes sure it has approval from the Canada Revenue Agency to place the insured funds in new registered plans with a new member institution without triggering the tax consequences of collapsing a registered plan. Payments are deposited into a savings account within an RRSP or RRIF so that you and your clients can decide how to reinvest the money.

The amount of each insurance payment is based on the member institution's records, but is calculated independently by CDIC. In very rare cases, your clients may be asked to provide proof of their deposits, but on the whole CDIC relies on an audit of the failed institution's books to satisfy itself that the records are complete and reliable.

To speed up the calculation and distribution process, which can be quite complex, CDIC has invested in sophisticated information systems. CDIC also sometimes arranges to examine the books, records and accounts of a member institution in trouble if it believes that preparing to make payments will serve depositors' best interests. An external accounting firm audits the payout process to verify its integrity.

Working to prevent institution failures

CDIC's mandate is both to provide deposit insurance and to contribute to the stability of Canada's financial system. Member institutions operate within a regulatory environment that is designed to promote sound and prudent practices and, where possible, prevent the failure of institutions.

As part of its own risk management strategy, CDIC gathers and analyzes financial and other information that its members publish or file with their regulator. It also looks closely at reports published by rating agencies. There is a regular exchange of data among CDIC, the Office of the Superintendent of Financial Institutions (OSFI), the Department of Finance and the Bank of Canada that helps all of these organizations stay up to date on the status of CDIC member institutions.

When a potential problem is identified, CDIC and OSFI or the relevant provincial regulator may intervene. CDIC may, for example, ask the member institution to provide additional information, such as financial statements, deposit records, descriptions of deposit systems, details about assets and liabilities, a business plan and other reports, documents and information about the member institution, its subsidiaries and its affiliates.

If an analysis of this additional information leaves CDIC with unanswered questions and continued concerns — often the case when there are serious liquidity or solvency problems — CDIC may conduct a "special examination" of the member institution. The scope of that examination is determined by CDIC together with OSFI or the relevant provincial regulator.

If CDIC is concerned about the solvency or viability of a member institution, it may take various actions, including implementing action plans concerning the amalgamation or sale of the institution or accepting an appointment as liquidator, receiver or inspector of the institution or a subsidiary of the institution. However, CDIC's focus is on prevention — developing solutions and working out problems before an institution sinks beyond the point of no return.

That said, every member institution is examined at least once a year by OSFI or, in the case of provincial members, a person CDIC designates. If CDIC believes that a member institution is in breach of any CDIC by-laws, or is in breach of any condition of CDIC's policy of deposit insurance, and the institution fails to demonstrate satisfactory progress in remedying the situation, CDIC may terminate the institution's deposit insurance policy. The Canada Deposit Insurance Corporation Act governs the process and timing of the termination. Deposits cannot be accepted after termination, so this will ultimately lead to the failure of the member institution.

A brief history of institution failures

Most of the failed institutions with deposits insured by CDIC collapsed in the 1980s and early 1990s. The first, Commonwealth Trust Company, failed just three years after CDIC was formed, in 1970, and was closely followed by Security Trust Company Limited in 1972. But the years when CDIC had to step in most frequently were 1983 and 1985, each of which saw seven institutions fail. Security Home's collapse in 1996 was the last member institution failure at the time of writing.

Talking to clients about CDIC

Making an effort to communicate some basic information about CDIC to your clients will give them more confidence in their financial institutions and in you, their advisor. Most importantly, they need to understand which savings are covered by deposit insurance and which are not. Deposits in Canadian currency, payable in Canada, with no more than a five-year term and placed at a CDIC member institution are protected up to a maximum of $100,000. On the other hand, investments such as mutual funds, stocks and bonds, are not deposits, and so are not covered.

In an unpredictable world, CDIC deposit insurance can provide a measure of security to nervous clients who want to protect all or part of their savings from the possibility that a financial institution will fail — as 43 have since 1967. Ultimately, the objective is not to promote only insured financial products, but to help investors make informed decisions and understand that they have an option that covers a significant sum of money when they place funds in eligible deposits at member institutions, and that separate coverage may protect assets in joint accounts, trust accounts, RRSPs and RRIFs. Then they can rest assured that, if not all, at least a portion of their hard-earned savings will be underwritten by a federal Crown corporation with a long record of fulfilling its commitments to Canadian depositors.

Depositors can check with their member institution to find out which eligible deposits the institution offers.

After carefully reading this material, visit our CE website at www.cdic.advisorce.com to answer each question. Detailed instructions appear for registrants online

Q&A

Question and Answer

1. Which of the following statements is true?
a) All deposits at Canadian financial institutions are insured by CDIC.
b) Most deposits at Canadian financial institutions are insured by CDIC and the rest are insured by the federal government.
c) CDIC only insures eligible deposits at member institutions.
d) CDIC does not insure deposits.

2. How many member institutions have failed since CDIC was created in 1967?
a) 23
b) 33
c) 43
d) 53

3. Which years saw the largest number of member institution failures (seven failures in each year)?
a) 1967 and 1970
b) 1983 and 1985
c) 1998 and 1999
d) 2000 and 2001

4. To be eligible for CDIC deposit insurance, a deposit must be:
a) In Canadian currency, payable in Canada.
b) Repayable no later than five years from the date of deposit.
c) Placed at a financial institution that is a CDIC member.
d) All of the above.

5. Which of the following portfolios will be entirely protected by CDIC deposit insurance?
a) $50,000 in three-year GICs in a non-registered account and $25,000 in mutual funds in an RRSP.
b) $50,000 in three-year GICs in a non-registered account and $100,000 in five-year GICs in an RRSP.
c) $50,000 in three-year GICs in a non-registered account, $50,000 in a joint savings account, and $125,000 in five-year GICs in an RRSP.
d) $50,000 in a Canadian dollar savings account and $50,000 in a U.S. dollar savings account.

6. Which of the following portfolios will NOT be entirely protected by CDIC deposit insurance?
a) $150,000 in eligible deposits in a joint account owned by three individuals.
b) $100,000 in eligible deposits in a non-registered account and $75,000 in eligible deposits in a joint account.
c) $25,000 in eligible deposits in a RRIF.
d) $50,000 in eligible deposits in an in-trust account.

7. The following may be eligible for separate coverage, above and beyond a client's basic coverage maximum of $100,000:
a) Eligible deposits in an in-trust account.
b) Eligible deposits in a second Canadian dollar savings account.
c) Eligible deposits in a U.S. dollar savings account.
d) A client is not entitled to any separate coverage beyond the $100,000 maximum.

8. Your client has contributed $50,000 to three-year GICs in a spousal RRSP. The amount that is insured by CDIC depends on:
a) The other eligible deposits in your client's RRSP.
b) The other eligible deposits in the spouse's RRSP.
c) The eligible deposits in your client's savings account.
d) None of the above.

9. When two member institutions amalgamate, your client has $50,000 in eligible deposits at institution A, and $75,000 in eligible deposits at institution B. After the merger:
a) $100,000 of your client's deposits will continue to be insured.
b) Half of your client's deposits will continue to be insured, so a total of $62,500 will be covered.
c) The full $125,000 will continue to be insured, but new deposits will not be insured until the total amount of the insured deposits that existed at the time of the merger, drops below $100,000.
d) None of the deposits will continue to be insured; your client will have to build up a new insurable amount with new deposits.

10. Which of the following Canadian dollar investments, held within a RRIF, is NOT eligible for CDIC deposit insurance?
a) Savings account worth $8,000.
b) Sixty-day term deposits worth $20,000 at maturity.
c) One-year GICs worth $50,000 at maturity.
d) Mutual funds worth $22,000.

11. What is the maximum term a GIC may have to qualify for deposit insurance?
a) One year
b) Three years
c) Five years
d) Ten years

12. If your client has $50,000 in eligible deposits in her name and $100,000 in eligible deposits held jointly with her spouse, how much is insured?
a) $50,000
b) $60,000
c) $100,000
d) $150,000

13. Three of the following are not eligible for CDIC deposit insurance. Which one is eligible?
a) Canadian dollar chequing account.
b) U.S. dollar savings account.
c) 10-year GIC.
d) Corporate bonds.

14. Your client holds an account in trust for his two children, each of whom has a one-half interest in the trust. What proportion of the trust's $150,000 eligible deposits is insured?
a) 100%
b) 75%
c) 66.6%
d) 50%

15. CDIC insures deposits at all but one of the following types of financial institution. Which one of the following is covered by provincial deposit insurance plans, not CDIC?
a) Banks
b) Trust companies
c) Loan companies
d) Credit unions/caisses populaire

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