

Mapping the Future: Five-year review of the *Credit Unions Act*

Financial Institutions Division
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FINANCIAL AND
CONSUMER SERVICES
COMMISSION

regulation • education • protection

FUTURE





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Honourable Cathy Rogers
Minister of Finance
Chancery Place
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Madame Minister,

I am pleased to submit to you the 2018 Report on the Review of the Provisions and Operation of the *Credit Unions Act* which has been prepared by the Financial and Consumer Services Commission pursuant to section 290.1 of the *Act*.

Yours truly,

Peter Klohn
Chair

Section 290.1 of the *Credit Unions Act* stipulates the following:

290.1(1) A review of the provisions and the operation of this Act shall be completed by the Commission every five years after 31 October 2008.

290.1(1.1) When the Commission has completed a review, it shall prepare a report on the review and shall file it with the Minister.

290.1(2) When the Minister receives a report under this section, the Minister shall

- a) if the Legislature is in session when the report is completed, lay the report before the Legislative Assembly, or
- b) if the Legislature is not in session when the report is completed, lay the report before the Legislative Assembly within 15 days after the commencement of the next session.

INTERPRETATION

In this document:

“2013 Report” means the first five-year review report filed in the Legislature on 20 November 2013.

“Credit union” means a credit union incorporated or continued under the New Brunswick *Credit Unions Act*.

“Atlantic Central” is a trade association for credit unions in Atlantic Canada.

“FCNB” means the Financial and Consumer Services Commission.

“NBCUDIC” means the New Brunswick Credit Union Deposit Insurance Corporation.

“Risk Management Agency” or “RMA” means the Brunswick Credit Union Stabilization Board Limited.

“Superintendent” means the Superintendent of Credit Unions, Financial and Consumer Services Commission.

BACKGROUND

The *Credit Unions Act* (the *Act*) governs the business activities of credit unions. The purpose of credit unions is to provide a comprehensive range of financial services that meets the needs of their members. These include receiving deposits from and operating chequing services for their members and making loans to their members. As of 1 July 2018, 10 credit unions operate in New Brunswick, serving 66,000 members. Total assets exceed \$1.0 billion. The Canadian credit union and *caisses populaires* system assets total about \$495 billion.

As New Brunswick's only provincially incorporated and regulated financial institutions, the 10 credit unions serve an integral part of the province's financial and business infrastructure needed to promote and contribute to the provincial economy.

Each credit union is a member of Atlantic Central. Atlantic Central is a trade association that manages the regulatory liquidity of member credit unions as well as providing them other services. It is regulated by the Province of Nova Scotia and its members also include credit unions in Nova Scotia, Prince Edward Island and Newfoundland and Labrador.

Each credit union is subject to the authority of RMA. RMA maintains a fund to provide financial assistance to member credit unions for the purposes of stabilization, and conducts regular inspections of credit unions.

The *Act* also provides an additional layer of protection for credit union members through the NBCUDIC. This Crown Corporation administers a deposit insurance fund that insures eligible deposits up to \$250,000. It also can assist the Risk Management Agency in providing financial assistance to credit unions.

On 1 July 2013, the provincial government established FCNB as a self-funded, independent Crown Corporation. FCNB, through the Superintendent as the statutory regulator, provides oversight of RMA and the credit union system.

Significant systemic changes have occurred to provincial credit unions since the 2013 Report. The current credit union regulatory structure was designed to meet the needs of the two separate systems operating in the province: the credit union system and the *caisses populaires* system. On 1 July 2016, the *caisses populaires* system, consisting of 15 *caisses populaires*, a federation, and a stabilization board, amalgamated and transferred to federal jurisdiction. When the *caisses populaires* system transferred to federal jurisdiction, it represented \$3.6 billion in assets, or 78 per cent of assets of the provincial credit union/*caisses populaires* system. The transfer left behind a regulatory structure disproportionate to the size of the remaining 10 credit unions, with \$1 billion in assets, having to bear the full cost of regulation.

The regulatory cost at the current level presents an impediment to the credit unions' competitiveness. FCNB presented a proposal to the credit unions for a regulatory model that is streamlined, efficient and affordable. The government of New Brunswick has directed FCNB to pursue this proposal.

The stakeholders consulted for this report identified four themes: (1) competitiveness and long-term sustainability; (2) depositor protection; (3) modernization; and (4) having a responsive and efficient regulator.

PROCESS

FCNB sought input from stakeholders regarding the development of a legislative proposal for the implementation of the restructured and streamlined regulatory framework. In August 2017, FCNB released a concept paper entitled "*Restructuring the Credit Union Regulatory Framework*", which sought input from stakeholders to make the model work. At the same time, FCNB sought input from stakeholders as part of the five-year statutory review of the *Credit Unions Act*. This consultation targeted feedback from Atlantic Central, RMA and NBCUDIC. In October 2017, FCNB sought input from the Credit Unions Managers Association (CUMA). FCNB received written submissions from each of these stakeholders.

In January 2018, FCNB held an in-person meeting with all four stakeholders to discuss their written comments and obtain clarification, if needed. This report brings together the content of the stakeholders' written submissions and follow-up discussions from the in-person meeting.

MAJOR THEMES ARISING FROM CONSULTATIONS

1. Competitiveness and Long-Term Sustainability

The current regulatory structure includes two deposit protection funds and three organizations performing oversight activities. This structure is unique in Canada, and is disproportionate to the size of New Brunswick's 10 credit unions.

The stakeholders confirmed the need to create regulatory and operational efficiencies, including the need for the regulatory bodies to be responsive to changes in the financial services industry, and to generally reduce duplicative oversight entities and other duplication within the regulatory framework, where possible, to reduce costs.

Some stakeholders proposed changes to help credit unions remain competitive, such as creating a framework for subsidiaries to permit credit unions to pursue other sources of income. The current *Act* is silent on how to create and operate subsidiaries. Other suggestions included permitting credit unions to use a business name separate from its legal name to operate. The use of a business name would level the playing field with branding and marketing practices of financial institutions, such as banks. Stakeholders also identified certain operational decisions that should not require the regulator's approval, for example, the establishment and relocation of branches. This requirement restricted a credit union's ability to perform minor renovations, upgrades or expansions without regulatory approval.

2. Deposit Protection

Similar to the findings in the 2013 Report, certain stakeholders submitted suggestions to enhance the governance of existing organizations or calling for the restructuring of the deposit insurance system. As noted above, the current regulatory structure includes two deposit protection funds: the stabilization fund administered by RMA, which provides financial assistance to member credit unions, and the deposit insurance fund administered by NBCUDIC, which provides deposit insurance protection to members of credit unions. The suggestions sought to reduce the duplication in the roles and responsibilities of RMA and NBCUDIC to achieve efficiencies without negatively impacting depositor protection.

Now that a federal credit union is operating in New Brunswick, it is possible that other federal or extra-provincial credit unions will follow. One stakeholder raised the issue of depositor protection, and specifically the need to ensure that the scope of deposit protection is easy for depositors to understand. Depositors need to be aware that the deposit protection provided by NBCUDIC is only for the benefit of New Brunswick credit unions and their depositors.

One stakeholder expressed the need to provide protection to depositors and credit unions in the event of a financial crisis. The failure of a credit union would not only impact depositors; it would also destabilize the credit union system in general. In response to the financial crisis of 2008, the international financial industry has developed a new approach that aims to protect customers, the financial system and public finances. This is known as “resolution.” One stakeholder suggested the Act adopt a resolution approach to ensure NBCUDIC has the tools to respond appropriately during a crisis. This could be accomplished by issuing debentures to raise capital from credit unions while reducing government dependency; by managing cash flow in the event of a large payout to depositors; or by providing for various types of loans or grants by the government on behalf of NBCUDIC.

Stakeholders also suggested improvements to capital management to provide credit unions the means to expand and grow in a sustainable fashion. Some suggestions included minimum capital requirements for any new credit unions, greater capital requirements for existing credit unions engaged in higher risk activities, and having credit union board approved capital management plans.

3. Modernization

The *Act* came into effect in January 1994. The *Act* has since been amended to address specific issues, such as the creation of Atlantic Central on 1 January 2011, the creation of FCNB on 1 July 2013 and the transfer of the *caisses populaires* system to federal jurisdiction on 1 July 2016. Although there were other minor updates to the *Act*, none have appropriately addressed technological advances, changes in privacy legislation, changes in international accounting reporting standards, member participation and changes in responsible governance practices.

During this five-year statutory review, all four stakeholders identified areas where the *Act* could be modernized to help credit unions improve their business operations and promote sustainability of the credit union system. Stakeholders suggested that the *Act* could be updated to address changes in technology, which would:

- Help credit unions provide services to their members through electronic means.
- Allow for electronic reporting, disclosure and other communications between the credit unions and the regulator.
- Permit voting by credit union members in numerous forms, including by mail ballot, in-branch ballot, or electronic voting.

Stakeholders also indicated their membership places a high priority on the privacy of their personal information, and it was vital to protect this information. The *Act* requires credit unions to maintain a membership registry and to make this registry available to other members in the event a member meeting needs to be called. Since this *Act* came into effect in 1994, privacy legislation has evolved and personal information is now protected. The requirement to maintain a membership registry was making it difficult for credit unions to compete with other financial institutions not required to maintain such a registry.

One stakeholder suggested reducing the age (from 19 to 18) for members to vote in credit union elections, which would enable credit unions to more fully engage their youth members. It would also harmonize with similar age requirements in credit union legislation in Nova Scotia and Prince Edward Island.

Stakeholders commented on difficulties in finding qualified individuals (who are members) to act as a director for a credit union, particularly since the *Act* has a nine-year limit on consecutive director terms. To address this challenge, an idea to permit a portion of non-member directors was suggested in subsequent stakeholder meetings, which would expand the pool of qualified directors.

Stakeholders also identified other areas that could be modernized to maintain competitiveness with other financial institutions, including:

- Creating a framework to manage inactive member accounts and other unclaimed balances.
- Stopping the use of beneficiary cards, which are no longer used in other Atlantic provinces, causing confusion.
- Requiring training for directors of credit union to ensure qualified leadership.
- Updating the definition of “residential property” to be consistent with other credit union legislation and Canada Mortgage and House Corporation (CMHC) definitions.
- Removing reporting requirements that duplicate requirements under money laundering legislation.

4. Provide for a responsive and efficient regulator

All four stakeholders were consulted on a regulatory model that would be more efficient and responsive to the credit union changing environment. Their input during the consultation process included, among other suggestions:

- Removing the member requirement to approve a patronage refund and keep this responsibility with the directors, who have a fiduciary duty to members.
- Attracting qualified individuals to act as directors on credit union boards.
- Strengthening the audit committee responsibilities of a credit union to ensure effective accountability and governance.

At a subsequent meeting with stakeholders to discuss their comments, FCNB clarified its current approach with rule-making as a means of keeping the regulatory framework timely and relevant. Stakeholders would be provided with further opportunities to submit comments on any proposed rules related to the *Credit Unions Act*.

EPILOGUE

The review of the *Credit Unions Act* every five years as required by section 290.1 is an opportunity to consider the *Act* in its entirety in a proactive context. The consultations that formed the basis for this report are helpful to identify appropriate policies and priorities for consideration.