# STANDARDS OF SOUND BUSINESS PRACTICE

# MANDATE

Credit Union Deposit Guarantee Corporation (the Corporation) is the deposit guarantor for Saskatchewan credit unions and the primary regulator for credit unions and Credit Union Central of Saskatchewan (SaskCentral), together, Provincially Regulated Financial Institutions or "PRFIs", as directed in provincial legislation – *The Credit Union Act, 1998* and *The Credit Union Central of Saskatchewan Act, 2016*. The Corporation instills confidence in the province's credit union system with a mandate of:

- guaranteeing the repayment of deposits in Saskatchewan credit unions
- establishing regulatory standards and ensuring PRFIs are performing to those standards
- promoting responsible governance by PRFIs, and contributing to the strength and stability of the credit union system
- directing PRFIs to take remedial action on material deficiencies and any issue that may put depositors' funds at risk
- maintaining and managing a guarantee fund in a sound and prudent manner

# VISION

To instill public confidence in the Saskatchewan credit union system.

# VALUES

Values guide individual and organizational behaviour. The Corporation's values are reflected in its Code of Conduct which provides a common frame of reference for staff, management, and the board in fulfilling the Corporation's mandate and strategic focus.

**Co-operation:**
As part of the co-operative financial services system, we respect co-operative principles and support credit unions and SaskCentral in enhancing their strength and development by working together.

**Honesty & Integrity:**
We perform our duties conscientiously with the highest level of honesty and professional integrity.

**Fairness:**
We approach issues and decisions with common sense, sound judgement, fairness, and consistency.

**Responsible Regulation:**
We act to protect the rights and interests of Saskatchewan depositors. We strike an appropriate regulatory balance that effectively protects depositors without unduly impairing credit unions' ability to compete in the market.

**Leadership:**
We use our knowledge of the credit union system and the financial services industry to anticipate future trends and proactively respond to our environment. We demonstrate leadership provincially and nationally by advocating positive change that contributes to the strength and stability of PRFIs.

**Teamwork & Respect:**
We work as a team to achieve goals and progress towards our common vision. We recognize that people are the key to success. We consistently treat people with dignity, respect, fairness, and the highest standards of ethics. We demonstrate co-operation when working with others, encouraging questions that generate innovative ideas and creative solutions.

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This reference guide has been published for use by provincially incorporated Saskatchewan credit unions. It outlines the Standards of Sound Business Practice, set by Credit Union Deposit Guarantee Corporation, in consultation with the Registrar of Credit Unions, under *The Credit Union Act, 1998*.


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Regulatory Guidance Documents, the Supervisory Framework and assessment criteria for reviewing credit unions are available on the Corporation’s credit union intranet. Information pertaining to the Corporation’s roles and responsibilities, deposit guarantee fund, and the legislative framework for Saskatchewan credit unions is available on both the Corporation’s credit union intranet and public website.

Changes to the Standards of Sound Business Practice will be communicated when they take effect.


January 1, 2024

# I. GENERAL INFORMATION

## 1. INTRODUCTION

*The Credit Union Act, 1998* (the Act) empowers Credit Union Deposit Guarantee Corporation (the Corporation), in consultation with the Registrar of Credit Unions, to establish Standards of Sound Business Practice (the Standards). The objectives of the Standards are to:

- establish principles and minimum requirements for corporate governance and the control environment that contribute to the sound and prudent operations of credit unions and the protection of deposits
- prescribe limits and restrictions for credit unions in the context of sound business practices to manage and control exposure to risk

The Standards may be supplemented, expanded upon, and brought into effect by the other components that comprise the Corporation's regulatory framework. These components include, but are not limited to, regulatory guidelines, directives, filing instructions, and bulletins (collectively, Regulatory Guidance Documents).[1] The Standards and the Regulatory Guidance Documents must be adhered to by Saskatchewan credit unions. Additionally, the Act and other provincial and federal legislation create legal requirements and obligations that credit unions must comply with. The Corporation's supervisory processes are a component of the regulatory framework. The supervisory processes are used to assess the safety and soundness of credit unions and proactively respond to credit unions demonstrating elevated risk.

While the Corporation establishes prudential requirements for credit unions, boards of directors (boards) of credit unions are ultimately responsible for the sound and prudent operation of their organizations. Boards and senior management are required to establish strong risk management cultures guided by sound risk management practices that support and provide appropriate standards and incentives for professional, prudent behaviour. As such, the Standards emphasize the careful and practical judgement that would be exercised by a reasonable person in the financial services industry, having regard to:

- the objectives of the credit union
- all the risks to which the credit union is exposed
- the amount and nature of the credit union's liquidity and capital
- the regulatory compliance obligations of the credit union

The effective date of these Standards is January 1, 2024. New or revised principles, requirements, limits, and restrictions contained in these Standards are not retroactive.

[1]Regulatory Guidance Documents can be found on the Corporation's credit union intranet at https://cudgcsk.sharepoint.com/sites/CUIntranet.

## 2. NON-COMPLIANCE

Where the Corporation determines a credit union is not in compliance with the Standards or Regulatory Guidance Documents, the Corporation may take any necessary action. Necessary action may include, but is not limited to:

- reducing or restricting the credit union's authorities and limits
- subjecting the credit union to preventive intervention
- issuing a compliance order
- placing the credit union under supervision or administration
- issuing an amalgamation order

## 3. EXCEPTION APPROVALS

Requests by a credit union for exceptions to, or a waiver of, the requirements under the Standards and/or Regulatory Guidance Documents must be accompanied by a detailed business case analysis including:

- policy recommendations
- financial projections
- any additional information that may be required by the Corporation

Exception approvals will be granted in exceptional circumstances only.

## II. STANDARDS OF SOUND BUSINESS PRACTICE

The Standards of Sound Business Practice set out the principles and minimum requirements related to credit union operations and business practices. The Standards are to be applied in conjunction with other elements of the regulatory framework, including:

- The Act and *The Credit Union Regulations, 1999* (the Regulations), which specify requirements respecting credit union operations and business practices.
- The Standards of Sound Business Practice – Capital Adequacy Requirements (Capital Standards), which set out the principles and minimum requirements for the quantity and quality of capital that credit unions are required to hold and how it is calculated.
- The Standards of Sound Business Practice – Liquidity Adequacy Requirements (Liquidity Standards), which set out the principles and minimum requirements for the quantity and quality of liquid assets that credit unions are required to hold.
- Regulatory Guidance Documents.

# 1. CORPORATE GOVERNANCE

Corporate governance involves a set of relationships between a credit union's board, senior management, members, and other stakeholders. An effective corporate governance framework provides:

- the structure through which the objectives of the credit union are set
- the means of attaining those objectives
- the means of monitoring performance

Effective corporate governance practices are essential to achieving and maintaining the trust and confidence of credit union members, the public, and other stakeholders.

## Key Principles and Requirements

### Board of Directors

- Credit unions are expected to have effective and appropriate corporate governance policies and procedures in place.
- The board has overall responsibility for the credit union and should obtain reasonable assurance that the credit union, including subsidiary operations, is in control.[2] This includes approving, overseeing, periodically reviewing, and assessing the implementation and effectiveness of the credit union's:
  - corporate governance framework
  - corporate mission, principles, and values
  - code of conduct and market code
  - strategic objectives and business strategy
  - control environment, including risk strategy, enterprise risk management framework, risk appetite, and risk tolerance levels
  - corporate policies for risk, risk management, and compliance
  - internal controls system
  - compensation system
- The board is responsible for providing oversight of senior management and for monitoring performance against business objectives, strategies, and plans. In addition, the board is responsible for the appointment, performance review, and compensation of the CEO and where appropriate, other members of senior management, including the heads of oversight functions.
- The board must define appropriate governance practices for its own work and have in place the means to ensure that such practices are followed and periodically reviewed for ongoing improvement.
- The board is expected to act independently of senior management and seek independent counsel as required.
- The board must ensure that the credit union's disclosures are adequately transparent to enable depositors and other key stakeholders to assess key areas of governance and risk, the soundness of its activities, and the soundness of its operations.

[2] The concept of "in control" refers to the ability to demonstrate that operations are subject to effective corporate governance, managed in accordance with appropriate, effective and prudent strategic management, capital management, and risk management processes, and supported by a sound control environment.

- Board members are expected to be and remain qualified, including through training, for their positions. They need to clearly understand their role in corporate governance and be able to exercise sound and objective judgement about the credit union's affairs.
- Credit unions must have an adequate number and appropriate composition of board members. Boards are expected to identify and nominate qualified candidates and ensure succession plans are in place.

### Senior Management

- Under the direction of the board, senior management is responsible for managing, monitoring, and controlling credit union operations, including subsidiary operations. This includes implementing and maintaining an appropriate enterprise risk management framework and an effective system of internal controls.
- Senior management is responsible for implementing and maintaining policies, processes, and systems for managing risk in all of the credit union's material products, activities, processes, and systems consistent with the organization's board-approved risk appetite and tolerance.
- Senior management is responsible for ensuring that all of the credit union's activities are consistent with the organization's board-approved principles and values, risk strategy, strategic objectives, business strategy, corporate policies, code of conduct, and market code.
- Senior management must establish management structures that promote accountability and transparency.
- Senior management must have the necessary experience, competencies, and integrity to manage all aspects of the business and individuals under their supervision.
- Senior management is responsible to facilitate board oversight of the credit union.

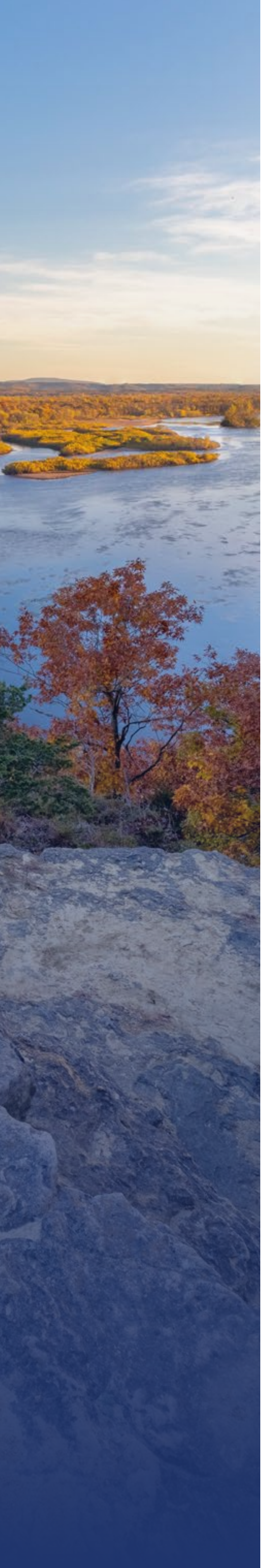
## 2. CONTROL ENVIRONMENT

Credit unions must ensure that they prudently manage the risks inherent in their operations to adequately safeguard members' deposits through an appropriate control environment that includes:

- financial management
- audit
- compliance
- risk management

### Key Principles and Requirements

- Credit unions must ensure that financial management, audit, compliance, and risk management:
  - are coordinated with one another
  - are consistent with the strategic plan
  - cover all areas of the organization
- Credit unions must ensure that all areas of the control environment are resourced appropriately and have sufficient independence, authority, and status within the organization.
- Financial management, audit, compliance and risk management are expected to reflect the nature, scope, complexity, and risk profile of the credit union.



## 2.1 FINANCIAL MANAGEMENT

Financial management involves the assessment and monitoring of financial and operational risks and results. This supports sound and prudent business decisions. Credit unions must have an effective financial management framework which includes, but is not limited to:

- capital and profitability management
- liquidity risk management
- investment and derivative risk management
- interest rate risk management
- credit risk management
- foreign exchange risk management

Credit unions should view financial management as a crucial element to ensure safety of deposits, soundness of operations, and achievement of strategic objectives.

### Key Principles and Requirements

- Credit unions are required to adopt investment, lending, and other financial policies and procedures that a reasonable and prudent person would apply in order to avoid undue risk and obtain a reasonable return.
- Credit unions are required to set financial targets and limits that are within the organization’s board-approved risk appetite and risk tolerance.
- Credit unions are required to have processes to identify, measure, monitor, control, and report on all key financial risks in an accurate and timely manner.
- Credit unions must adhere to the financial limits and restrictions (Capital Standards) periodically set by the Corporation.
- Credit unions are expected to have effective and appropriate internal capital adequacy assessment processes (ICAAP) in place.
- Credit unions are expected to perform forward-looking stress testing to assess significant components of the financial management framework, including assumptions.
- Credit unions must have contingency plans in place for early appropriate action on exceptions to financial limits and exposures and deteriorating financial results.

## 2.2 AUDIT

Credit unions must perform audits to determine the validity and reliability of financial information and to provide an assessment of the quality and effectiveness of the credit union’s control functions. An effective audit function is a key component of sound corporate governance.

The audit function must encompass three distinct areas:

- audit committee oversight
- internal audit
- external audit

### Key Principles and Requirements

- Credit unions are expected to have effective and appropriate audit policies and procedures in place.
- Credit unions must have an audit committee which is responsible for overseeing the credit union's audit function. This includes:
    - ensuring appropriate interaction and coordination between the internal and external audit functions
    - ensuring the scope of the audit plans are appropriate and include key areas of concern
    - ensuring any deficiencies are reported to the board
- Individuals responsible for the audit function must have access to the audit committee and board, including in-camera meetings.
- The internal audit function is required to independently and objectively evaluate the quality and effectiveness of the credit union's internal control, risk management, and governance processes.
- The internal audit program must be risk-based and include all relevant activities, regulatory matters, regulatory financial and statistical reporting, business functions, and decisions of the credit union and all subsidiary organizations. Internal audit must also complement and assess operational management, financial management, risk management, and compliance functions.
- The board is responsible to engage an external auditor to review and provide an unbiased and independent opinion on:
    - the financial statements prepared by senior management
    - the credit union's overall financial condition
- The audit committee is required to formally review the performance of the internal and external auditor.

## 2.3 COMPLIANCE

Compliance is the process of adhering to applicable requirements. It goes beyond what is legally binding and embraces broader standards of integrity and ethical conduct. The compliance function assists senior management in effectively managing the compliance risks faced by the credit union.

Compliance risk is the risk of legal or regulatory sanctions, financial loss, or a loss to reputation that a credit union may suffer as a result of its failure to comply with applicable laws, regulations, Standards, Regulatory Guidance Documents, credit union bylaws, codes of conduct, and market code.

### Key Principles and Requirements

- Credit unions are expected to have effective and appropriate policies and procedures in place to manage compliance risks.
- The board and senior management are expected to promote the values of honesty and integrity throughout the credit union. Compliance should be viewed as an essential means to this end and integral to the culture of the organization.
- Credit unions must establish and communicate compliance policy, ensure it is adhered to, and ensure senior management and the board receives regular and timely reports on the status of the credit union's compliance.
- Credit unions are expected to establish a compliance function and ensure its objectivity to support board oversight.
- Compliance risk is to be managed within a risk-based program that sets out planned activities including:
    - implementation and review of specific policies and procedures
    - compliance risk assessment
    - compliance testing
    - training of board and staff
- Senior management must ensure that appropriate action is taken if breaches are identified, and immediately report any material non-compliance to the board.

## 2.4 RISK MANAGEMENT

Risk is inherent in all aspects of a credit union's operations. Effective management of risk is fundamental to sound and prudent operations.

Risk management encompasses the process of:

- identifying risks to which the credit union is exposed
- measuring exposures to identified risks
- ensuring that an effective risk-monitoring program is in place
- monitoring risk exposures on an ongoing basis
- controlling and mitigating risk exposures
- reporting to the board and senior management on the credit union's risk exposures

Risks include, but are not limited to:

- credit risk
- market risk
- liquidity risk
- strategic risk
- operational risk
- legal and regulatory risk

Operational risk includes, but is not limited to human resource management risk, management information system risk, outsourcing risk, fiduciary risk, technology risk, and internal controls.

### Key Principles and Requirements

- Credit unions are expected to have effective and appropriate risk management policies and procedures in place.
- The board is expected to establish a “tone at the top” by setting professional standards and corporate values that promote integrity for all employees of the organization. This includes fostering a strong risk management culture that supports and provides appropriate standards and incentives for professional and responsible behaviour.
- Credit unions must have a strong control environment that uses:
  - policies, processes, and systems
  - appropriate internal controls
  - appropriate risk mitigation and/or risk transfer strategies, including insurance
- Credit unions are required to have a process to identify, measure, monitor, control, and report on all key risks to which the organization is exposed.
- Credit unions are required to perform forward-looking stress testing to complement and validate risk management approaches.
- Credit unions must have a comprehensive business continuity program.

## 3. LIMITS AND RESTRICTIONS

The following limits and restrictions are regulatory minimums. The Corporation expects credit unions to establish limits for key financial indicators that:

- support prudent operations
- are appropriate for the credit union’s risk profile, risk appetite, and risk tolerance
- are aligned with the credit union’s stress testing program and ICAAP
- are stricter than regulatory minimums

### 3.1 CAPITAL AND PROFITABILITY MANAGEMENT

Limits and restrictions pertaining to capital and profitability management can be found in the Capital Standards.

### 3.2 LIQUIDITY

Limits and restrictions pertaining to liquidity, including investment and derivative management, and foreign exchange risk management, can be found in the Liquidity Standards.

## 3.3 CREDIT MANAGEMENT

- A loan[3] made by a credit union on residential property cannot exceed 80% of fair market value unless the loan:
  - is insured by Canada Mortgage and Housing Corporation or another insurance company authorized to carry on the business of mortgage insurance in Canada and licensed in the province of Saskatchewan
  - is secured by a specific charge on additional properties or securities; or
  - is guaranteed by a government agency
- The loan-to-value ratio for non-conforming residential mortgages[4] cannot exceed 65% of the value of the mortgaged property.
- The maximum loan-to-value ratio for the non-amortizing home equity line of credit component of a residential mortgage cannot exceed 65% of the value of the mortgaged property.
- Pursuant to section 2(1) (c) of the Regulations, credit unions may only provide financial leases to credit union customers.
- Upon acquisition of real or personal property through realization on a debt owed to the credit union, the credit union shall:
  - dispose of the property as soon as is practicable after the acquisition
  - use the property for its own use, subject to the limit on ownership of real property and equipment for the credit union's own use prescribed by the Corporation; or
  - hold the property as an investment, subject to consultation with the Corporation
- Loans made by a credit union are subject to the following limits which are based on the financial position of the credit union as indicated by its most recent audited financial statement:

| Loan | Limit |
| --- | --- |
| Aggregate loans per a single counterparty or group of connected counterparties<br><br>Note: Government guaranteed[5] or cash or equivalent secured loans[6] are excluded from this limit | Lesser of 25% of Eligible Capital<br>-or-<br>5% of assets |
| Aggregate loans per individual local government body[7] | 10% of credit union assets |

[3]Loan is defined as the acceptance, endorsement or other guarantee, financial lease, conditional sales contract, overdraft, letter of credit, repurchase agreement, or any other similar arrangements for obtaining funds or credit. Overdraft is defined as any withdrawal or payment from an account in excess of the amount on deposit that is not covered by an authorized line of credit, or funds in another account for which the credit union has written authority to transfer. This definition excludes amounts that are posted to the member's account solely for administrative purposes and are reserved by the next outgoing clearing.

[4]Non-conforming residential mortgages can include, in general, non-income qualifying loans, loans to those with low credit scores or high debt serviceability ratios, mortgages where attributes of the property cause the loan to carry credit risk (e.g., illiquid properties) or any loan that has clear deficiencies relative to a conforming residential mortgage.

[5]Government guaranteed loan is a loan defined under federal or provincial programs or acts. This includes the: *National Housing Act (Canada)* residential and commercial mortgages; *Canada Small Business Financing Act (Canada)*; or *Canadian Agricultural Loans Act (Canada)*.

[6]Cash or equivalent secured loan is defined as a loan secured by assignable:

- credit union deposit;
- term certificate (credit union and other financial institution);
- irrevocable letters of credit issued by Schedule 1 Canadian Chartered Banks;
- provincial or federal government guaranteed bond;
- or deferred grain ticket based on a credit union's policy and credit risk tolerance.

[7]Local government body includes municipalities, school boards, hospitals, universities, and social service programs that receive regular government financial support.

Credit unions are required to assess the common risk that a single counterparty or group of connected counterparties may present across multiple accounts and products. This includes but is not limited to; all types of loans, lines of credit (including home equity lines of credit), mortgages, reverse mortgages, overdrafts and other guarantees.

The existence of common risk is to be determined on a case-by-case basis, with reference to the material facts of the situation and with sound judgment. The presence of either of the following conditions indicates the presence of common risk:

1. **Control relationship:** if one of the counterparties has direct or indirect control over the other(s), or if both counterparties are directly or indirectly controlled by a common person or entity.
2. **Economic interdependence:** if one counterparty were to experience financial difficulties, particularly funding or repayment difficulties, it would likely lead to funding or repayment difficulties of another counterparty.

Where two or more counterparties constitute a common risk, the counterparties should form a group of connected counterparties. The exposures to each of the counterparties in the group of connected counterparties should be aggregated and treated as an exposure to a single counterparty.

Credit unions should have sound and robust policies and processes for assessing and identifying control relationships and economic interdependences for determining the existence of common risk. Credit unions should first determine the existence of control relationships, and then assess economic interdependence between counterparties.

## 3.4 RELATED PARTY TRANSACTIONS

Related party transactions entered into by a credit union are subject to the following limits which are based on the financial position of the credit union as indicated by its most recent audited financial statement.

| Related Party Transaction | Limit |
| --- | --- |
| Aggregate of all related party transactions | 20% of credit union assets |

This limit is pursuant to subsection 174(4) of the Act and includes loans and all other transactions with related parties.

## 3.5 SERVICE DELIVERY OUTLETS

Credit unions must provide the Corporation with 30 days written notice prior to opening a new service delivery outlet.

## 3.6 MARKET CODE

Proposed changes to a credit union’s market code must be presented to the Corporation and approved by the Registrar of Credit Unions prior to implementation.

## OPERATING PRINCIPLES

Our principles provide direction on how to carry out the Corporation's roles and responsibilities. They are what make us unique. These philosophical insights have contributed to the Corporation's notable success throughout its history and provide guidance in shaping the Corporation's future.

### Effective Regulation

As the primary prudential and solvency regulator, we support and encourage a successful credit union system by working with stakeholders to balance prudential regulation with market forces.

We recognize the need for PRFIs to evolve in the marketplace and we support a strong and prosperous credit union system by:

- focusing on the future of the financial services industry
- striving to implement industry best practices where it is reasonable to do so
- developing flexible and enabling approaches to effective and efficient regulation

Our role is to regulate, not to manage. Our actions demonstrate our preference to prescribe rather than restrict and demonstrate our respect for a credit union's right to determine its own destiny.

We believe that effective deposit protection is accomplished through investments in prevention including:

- analyzing PRFIs' performance on an ongoing basis to ensure early identification of potential risks
- communicating our expectations
- sponsoring and promoting programs that strengthen the knowledge and skills of credit union decision makers

### Authority, Responsibility, Accountability

#### Authority

We clearly communicate to all stakeholders our authority to take action to protect deposits. The Corporation has the authority to act to fulfill its deposit protection responsibilities in the best interests of PRFIs.

#### Responsibility

We exercise great care and judgement in carrying out the authority that has been granted to us.

We are responsible to act when others are either unwilling or unable to take action on matters concerning credit union and system solvency and the safety of deposits.

#### Accountability

We demonstrate accountability through fiscal responsibility.

We pursue economical business solutions to protect deposits and minimize costs to PRFIs.

Our operating methods demonstrate effective and efficient use of system resources.

### Objectivity and Independence

Our actions are free of influence, interest, or relationship that would impair professional judgement or objectivity.

We act independently and in the best interests of the Corporation to protect depositors' funds.

We carry out our responsibilities fairly and consistently, basing decisions on careful analysis of facts.

### Openness

We communicate openly with all stakeholders.

We respect our stakeholders' rights to privacy and confidentiality of information.

We value the opinions and ideas of our stakeholders and take care to ensure that we consult with them on matters that affect them.

### Collaborative Relationships

Through constructive relationships with our stakeholders, we create opportunities to enhance the overall quality and effectiveness of our results.

We believe that the best solutions are arrived at by working with others to build common understanding and to identify and achieve common goals.