



REGULATORY GUIDELINE

Background Checks on Directors and Senior Management

SYSTEM COMMUNICATION NUMBER
Guideline 2020-03

ISSUE DATE
MARCH 2020

TABLE OF CONTENTS

Introduction	1
I. Statement of Regulatory Principles.....	1
II. Application.....	1
III. Definitions	2
IV. Assessment Policy.....	2
V. Assessment Procedures	4
VI. Role of the Board of Directors.....	6
VII. Providing Information to the Corporation	6

INTRODUCTION

This regulatory Guideline is a Regulatory Guidance Document as contemplated by the Standards of Sound Business Practice (the Standards). It supplements and expands upon section 1, Corporate Governance, of the Standards and must be adhered to by Saskatchewan credit unions.

I. STATEMENT OF REGULATORY PRINCIPLES

This Guideline builds upon the following:

Regulatory System: The provincial regulatory framework is based on a tripartite division of responsibilities involving:

- the management and oversight processes of credit unions;
- the use of independent external reviewers (i.e. the external auditor); and
- monitoring and supervision by Credit Union Deposit Guarantee Corporation (the Corporation)

The primary responsibility for ensuring credit unions are soundly managed and directed rests with the board of directors and senior management of the institution. Accordingly, the suitability and integrity of senior management and members of the board of directors pose an important concern for the credit union and the Corporation, as the safety, soundness and reputation of the credit union can be negatively affected by the actions of these individuals.

Supervisory Approach: The Corporation relies on the credit union's own internal processes for assessing the initial and ongoing suitability and integrity of these individuals. Where warranted, the Corporation applies a risk-based approach to assessing the credit union's processes.

II. APPLICATION

This Guideline outlines a number of principles to assist credit unions in establishing policies and procedures regarding the conduct of assessments of its responsible persons and indicates areas that the Corporation may focus on in its supervisory practices. The Guideline recognizes that aspects of these assessments that address the suitability of a person, such as expertise, require assessment only upon initial appointment whereas regular assessments would focus on particulars that can change over time. Examples include, legal proceedings against an individual or changes in professional qualifications.

The Credit Union Act (1998) (the Act), prescribes minimum requirements with regard to the qualifications of directors, including the requirement for directors and employees to furnish the credit union with a security or fidelity bond¹. While it is recognized that credit unions may have various policies and procedures in place to meet these requirements as part of their own internal processes (e.g., hiring policies, code of conduct), this Guideline clarifies expectations and highlights practices considered necessary to minimize safety and soundness concerns. This includes reputational risk.

¹ Subsections 102(1) and 120(1) of the *Credit Union Act (1998)*.

This Guideline outlines prudent practices or standards that must be considered by the credit union in developing its own practices and procedures.

III. DEFINITIONS

Responsible Person

For the purposes of this Guideline, a responsible person is defined as:

- a) a director; and
- b) senior management, (i.e. any person who the credit union determines plays a significant role in the management of the institution. This could include the General Manager, Chief Executive Officer, Chief Financial Officer and any other officer who has a functional reporting line directly to the board of directors).

Credit Union Directors

Credit unions are unique among financial institutions in terms of the co-operative principles that underpin their formation and impact decision making. One of the unique attributes of credit unions is that directors are members of the institution who typically volunteer to stand for election and are not appointed strictly based on their qualifications or skillset. While the democratic nature of these institutions allows the membership to vote on board members, credit unions are expected to obtain reasonable assurance regarding the suitability and integrity of these individuals.

IV. ASSESSMENT POLICY

The Corporation expects credit unions to have a written policy regarding the performance of assessments of the suitability and integrity of its responsible persons. The assessment policy can be one consolidated document or a set of assessment policy and practice documents. For the purposes of this Guideline, this policy or set of documents will be referred to as the Assessment Policy.

Entities belonging to the credit union group² may have one umbrella Assessment Policy for the entire group.

The Corporation expects that the board of directors³ of the credit union will approve the Assessment Policy (and any material amendments thereto) of the credit union.

The Corporation expects that this Assessment Policy will consider the following matters in a way that prudently minimizes the risks that persons who are not suitable or do not possess the required integrity do not hold responsible person positions:

a) Identification of the Responsible Persons Subject to Assessments

The credit union is expected to identify as responsible persons, individuals who play a significant role in the management of the credit union. The Corporation expects that the board will approve the list of responsible persons subject to the assessments.

² In this Guideline, “the credit union group” refers to the credit union and its subsidiaries.

³ In this Guideline, the term “board of directors” includes a committee of the board.

Only one assessment is necessary in respect of responsible persons identified as being a responsible person for the credit union and any organization within the group. The board may choose not to apply the provisions of this Guideline to individuals in a subsidiary of the credit union where the management of the subsidiary is directed by responsible persons of the credit union.

b) Timing of the Assessments

The Corporation expects the Assessment Policy would require an assessment to be conducted before a person is appointed to a responsible person position unless it would be imprudent to delay the appointment. In such cases, the assessment would occur as soon as practicable and in any event within a number of days specified in the Assessment Policy. The initial assessment would address all aspects of the assessment including aspects that are not subject to change as well as those that can change over time.

After the initial appointment, updated assessments of each responsible person would be conducted at intervals specified in the Assessment Policy, which should be no longer than five years. Updated assessments can focus only on aspects that can change over time. Credit unions can rely on attestations from responsible persons to conduct update assessments. However, the credit union is expected to independently verify responsible persons' criminal records at least every seven years.

Assessments should be undertaken between intervals if the credit union acquires knowledge of material adverse information about a responsible person.

c) Key Practices

The Corporation expects that the Assessment Policy will indicate the key practices that will be followed by the credit union in implementing the principles of this Guideline, including the key practices relating to the credit union's decision-making process (discussed in greater detail below). For example, the Assessment Policy could set out when and how the Assessment Policy will be disclosed to responsible persons and candidates for responsible person positions. The Corporation also expects the Assessment Policy to set out practices that will be followed if the credit union concludes a responsible person is not suitable or does not possess the required integrity, such as when and how the decision will be escalated through the institution, how and when the responsible person will be notified of adverse information as well as the steps that will be taken to remove a responsible person. Credit unions should ensure their practices comply with all applicable legal requirements, including privacy and employment laws.

V. ASSESSMENT PROCEDURES

Credit unions are expected to have written internal procedures outlining how the Assessment Policy will be implemented.

Where Assessment Procedures similar to those described in this Guideline are already in place within the credit union to satisfy its internal policies (e.g., hiring or code of conduct) or to satisfy other regulatory requirements, the credit union can refer to the procedures used to meet the other requirements. The credit union will need to implement its own procedures taking into account its nature, size, complexity and risk profile.

The Assessment Procedures would consider the following matters:

a) **Persons or Groups that will Conduct Assessments**

Credit unions can assign the responsibility for conducting assessments of each responsible person to any person or group within the organization. The Corporation expects the Assessment Policy to be implemented by appropriately qualified individuals and that procedures exist to allow such individuals to escalate concerns about findings in respect of a responsible person or the conduct of assessments.

The credit union can assign responsibility for various facets of the assessments to different groups in the institution. The credit union can outsource some of the functions related to conducting assessments, but the Corporation expects that an appropriate person within the credit union will make the ultimate determination about whether a responsible person possesses the required suitability and integrity. Any outsourcing should comply with the Corporation's Outsourcing of Business Activities, Functions and Processes Guideline and all privacy laws, as applicable.

b) **Information that will be Obtained**

In its Assessment Procedures, the credit union is expected to identify the information it will obtain to assess the suitability and integrity of its responsible persons, upon initial appointment of the responsible persons to their positions and during subsequent update assessments.

When a responsible person is first appointed to his or her position, the credit union will obtain sufficient information to allow them to conclude that the responsible person possesses the suitability and integrity to perform properly the duties of the responsible person position. Such information could include:

- criminal records
- records of securities-related sanctions or disciplinary actions by a professional regulatory body
- evidence that the responsible person possesses the required education, skills, professional qualifications and experience
- attestation that the responsible person has not been held liable in a civil proceeding in connection with financial or business misconduct, fraud or mismanagement of an entity
- attestation that the responsible person has no conflicts of interests that could create a material risk that the individual will be unable to discharge the duties of the responsible person with integrity and in the best interests of the credit union

When conducting assessments at initial appointment, the credit union is expected to verify information using searches of databases and information made available by third parties when such independent sources are available. Credit unions should determine in which jurisdictions and how far back verifications should be conducted, based on the responsible person's history and circumstances. While attestations from responsible persons about certain aspects of the assessments, such as civil proceedings, are sufficient to meet the expectations of the Guideline, the Corporation encourages credit unions to conduct their own independent verifications if they have grounds to believe that an attestation is insufficient or inaccurate.

Subsequent to the initial appointment, the frequency at which verifications are updated would reflect the specific circumstances of the credit union and of each responsible person. Updates of assessments can focus only on particulars that can change over time, such as:

- criminal convictions, regulatory or civil proceedings against the responsible person
- changes in status in professional organizations
- new or changes in conflicts of interest

In update assessments, the credit union can rely on an attestation of the facts from responsible persons for all aspects of the assessment. In addition, credit unions are expected to independently verify a responsible person's criminal record at intervals specified in the Assessment Policy.

c) Decision-making Process

The credit union is expected to document the decision-making process they will follow when an adverse finding is made with respect to a responsible person. For example, the credit union can set its own threshold about the type of adverse information it would consider material and the type of information it would gather to follow-up on the adverse information, including mitigating factors or circumstances. The decision-making process can be tailored to the unique circumstances of the credit union.

An adverse finding would not necessarily render a person unsuitable to hold a responsible person position. Each finding should be considered in relation to all surrounding circumstances (e.g., seriousness of the incident or time elapsed since the incident). The Corporation expects credit unions to use judgement and to weigh the findings on each factor, including the materiality of the adverse information and the relevance of the factor to the responsible person's duties.

In the case of senior management, a responsible person may be found unsuitable for a particular responsible person position because of a lack of qualifications for that position or because of a conflict of interest related to the duties of that position. In that case, the responsible person may still be suitable for another responsible person position. Credit unions may also redefine the duties associated with a responsible person position.

Credit unions must determine whether a negative finding about a responsible person permanently disqualifies that person (e.g., absent legislative or other requirements to the contrary, whether a responsible person who has been suspended by a professional association can remain in the position after serving the suspension). However, where a responsible person is found to lack integrity because of negative findings related to the responsible person's character or honesty (e.g., conviction for offences relating to

money laundering or fraud), that responsible person will normally not be suitable for any responsible person position.

The Corporation expects that persons who do not possess the required suitability and integrity for a particular responsible person position will not be appointed to that position. The Corporation will engage with the credit union to address areas of question or concern and will look to gain insight into the actions taken by the credit union to resolve any situation that is deemed to be of material risk⁴.

VI. ROLE OF THE BOARD OF DIRECTORS

In keeping with the responsibilities attributed to the board in the Standards and the Corporation's Corporate Governance Guideline and Prudential Standard, particularly in regard to the board's duties with respect to overall risk management, it is expected that the board or a committee of the board will:

- approve the Assessment Policy and significant amendments thereto;
- where it is inappropriate for another person in the credit union to make the determination, determine whether a responsible person is suitable or possesses sufficient integrity and, if not, ensure such persons do not hold responsible person positions. If the responsible person is not removed, ensure adequate measures are taken to manage the risk arising from misconduct or mismanagement, such as redefining the responsibilities of the position or removing a conflict that applies to the duties of that position; and
- receive concerns elevated by senior management regarding the suitability and integrity of a responsible person or regarding the manner in which the Assessment Policy is implemented

VII. PROVIDING INFORMATION TO THE CORPORATION

The credit union is not required to provide its Assessment Policy or Assessment Procedures to the Corporation on a regular basis but it should be made available to the Corporation upon request. The Corporation expects that the information about assessments conducted in respect of each responsible person will be retained by the credit union for a reasonable length of time specified in the Assessment Policy and that such information will be readily available for examination by the Corporation upon request. As part of its regular supervisory practices, the Corporation may periodically, where warranted, verify the assessments conducted by the credit union in accordance with its risk-based supervisory approach.

The Corporation looks not only for evidence that the credit union has appropriate policies and processes in place but also for indicators that these policies and processes are understood, are being followed and that, as a result, they are effective.

⁴ The Corporation may remove directors and senior officers (section 444 of the Act). These powers apply independently of the credit union's powers and duties, regardless of whether the credit union is of the opinion that the responsible person meets the criteria of suitability and integrity.