



PRUDENTIAL STANDARDS

# Commercial Lending Criteria

SASKCENTRAL COMMUNICATION NUMBER  
Prudential Standard 2017-06

ISSUE DATE  
JANUARY 2017

## TABLE OF CONTENTS

Introduction .....	1
Commercial Lending .....	1
Approval Process.....	2
Role of The Corporation .....	2
Criteria .....	3

## INTRODUCTION

Pursuant to Part XIII of *The Credit Union Central of Saskatchewan Act, 2016* (the Act), Credit Union Deposit Guarantee Corporation (the Corporation) may make Prudential Standards that apply to SaskCentral. The Prudential Standard (Standard) contained herein must be adhered to by SaskCentral.

This Standard outlines the approach the Corporation uses in permitting SaskCentral to hold commercial loans in excess of 5 per cent of the total assets of SaskCentral.

## COMMERCIAL LENDING

The Act provides full commercial lending powers to SaskCentral, subject to certain conditions.<sup>1</sup> These conditions include a capital base of at least \$25 million and supervisory approval by the Corporation. If SaskCentral does not meet these conditions it is limited to commercial lending activities not exceeding 5 per cent of total assets as defined by the *Commercial Loan (Cooperative Credit Associations) Regulations* (Regulations). The Regulations define "total assets" to incorporate the assets of SaskCentral's prescribed subsidiaries.

Approval by the Corporation to engage in commercial lending will be granted only when certain established and defined criteria are met. The purpose of applying these criteria is to ensure that SaskCentral has the appropriate mechanisms in place to make, control and monitor a commercial loan portfolio subject to the prudent person approach.

The Act defines commercial lending for purposes of these expanded powers. The term "commercial loan" is defined to include not only loans in the conventional sense but also certain loan substitutes and investments in debt and equity securities of corporations and unincorporated entities. The definition does, however, exclude several classes of loans and investments that are not to be considered commercial loans. These include:

- deposits in, loans to, and investments in the debt obligations of a credit union, federal credit union or a cooperative corporation that is a member of SaskCentral;
- small loans - less than \$250,000 to natural persons (these are essentially consumer loans and will not be subject to portfolio limits under the Act);
- mortgage loans that are insured or meet certain requirements regarding loan-to-value ratios;
- certain deposits by SaskCentral with another financial institution;
- loans and investments in debt obligations directly or indirectly backed by the guarantee of a government or prescribed international agency;
- loans and investments in debt obligations either directly or indirectly backed by the guarantee of another financial institution or secured by deposits with any financial institution, including SaskCentral;
- investments in debt or equity securities that are widely distributed within the meaning of the Regulations; and
- investments in participating shares.

In defining a commercial loan, the Act defines "loan" with a modified meaning that incorporates close substitutes for loans, such as an acceptance, endorsement or other

---

<sup>1</sup> The legislative reference is Part X of the *Cooperative Credit Associations Act*, which applies pursuant to subsection 12-2 of the Act.

guarantee, a deposit, a financial lease, a conditional sales contract, a repurchase agreement and any other similar arrangement for obtaining funds or credit but does not include investments in securities.

## APPROVAL PROCESS

The Corporation expects SaskCentral to follow sound risk management practices in the context of commercial lending activities. Approval for expanding commercial lending beyond the limit of 5 per cent of total assets depends on SaskCentral demonstrating compliance not only with the criteria established with respect to commercial lending but with all provisions of the Act, Regulations (including capital adequacy tests), and Prudential Standards issued by the Corporation.

The approval process will encompass the following elements:

1. If SaskCentral wishes to exceed the 5 per cent limits, it is required to submit a request for approval.
2. Approvals will take two forms; general approval without predetermined limits and approval with predetermined limits.
3. To obtain approval for commercial lending without a predetermined limit, SaskCentral will need to have a strong capital position, a consistently sound record of credit management based on a significant volume of commercial lending business and, through a description of their commercial lending business plan, their credit risk management programs, their credit granting and monitoring processes, and matters related to the other criteria outlined below, exhibit a strong capacity to manage the risks associated with commercial lending.
4. If SaskCentral seeks to obtain approval beyond the 5 per cent limit but does not meet all of the conditions described in 3 but exhibits an adequate capacity to manage the risks associated with commercial lending using the criteria outlined below, it will be permitted to increase commercial lending activities gradually. When previously authorized limits are approached SaskCentral may apply for further increases in authorized limits or may seek approval to conduct commercial lending without predetermined limit if they meet all of the conditions described in 3.
5. Information contained in applications will be confirmed by reference to the Corporation's assessment of SaskCentral's condition and past performance obtained through its supervisory activities including monitoring, analysis and review processes.
6. Under normal circumstances previously authorized expanded commercial lending powers will not be withdrawn. The Corporation will use its supervisory processes to ensure that SaskCentral follows sound risk management practices as they relate to commercial lending.

## ROLE OF THE CORPORATION

As regulator, the Corporation will:

- consider requests from SaskCentral with respect to increasing the approved limits on commercial lending or removing such limits;
- establish, maintain and communicate the criteria used to consider such requests;
- upon review, provide written approvals where established criteria are met; and
- review, through supervisory processes, the commercial lending activities to ensure compliance with established criteria.

## **CRITERIA**

Each application for approval of expanded commercial lending authorities will be reviewed in light of the criteria outlined below.

### **Current Position**

A review of SaskCentral's current position with respect to:

- the existing authorized level of commercial lending activities;
- capital adequacy position; and
- compliance with the Act, Regulations and Prudential Standards.

### **Past Experience**

An analysis of past experience in credit management including:

- volume of commercial lending activity undertaken in the past five years;
- statistics on non-performing loans, provisions, write-offs, renegotiated reduced rate loans, arrears; and
- other asset quality indicators for both commercial and other loans.

### **Earnings Experience**

An analysis of annual earnings experience segmented by significant type of business activity for the previous five year period.

### **Expertise**

Background information and biographies of key managers including information on past experience and areas of specialization in commercial lending.

### **Business Plan**

A comprehensive business plan indicating the strategic direction of commercial lending activities, markets and market share targets, forecasts and budgets.

### **Risk Management**

A description of the credit risk identification and management program. This program should include the following essential elements:

- credit risk philosophy governing the extent to which SaskCentral is willing to assume credit risk;
- role of the board of directors and management;
- general areas of credit in which SaskCentral is prepared to extend credit, types of credit facilities, borrowers and geographic areas;
- levels of delegation of credit approval, and provisions or write-off authorities;
- portfolio concentration limits for the following:
  - a single counterparty;
  - a group of associated counterparties;
  - an industrial sector;
  - a geographic region;
  - one type of credit facility;
  - a class of security;

- (limits should be provided for both SaskCentral and, where appropriate, on a consolidated basis for SaskCentral and its subsidiaries).
- portfolio diversification policies.

### **Credit Granting, Documentation and Collection**

A description of the credit process including:

- evaluating credit proposals;
- credit documentation standards;
- credit collection processes.

### **Credit Monitoring**

A description of the credit monitoring and control practices including:

- portfolio characteristics analysis to track single and associated groups of counterparties, types of credit facilities, industries and geographic regions;
- credit rating systems which define risk rating criteria and rates SaskCentral's risks accordingly including the classification of credits as satisfactory, below standard or unsatisfactory;
- credit review process outlining the regular monitoring of borrowers and applicable procedures for re-evaluation and re-rating of credits;
- internal credit inspection and audit processes and procedures to ensure that credit processes are in compliance with SaskCentral's policies.