

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

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FINANCIAL AND
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Contents

Interpretation	4
Background	5
Process	7
Major Themes	8
1. Impact of the 2020 <i>Credit Unions Act</i>	8
2. Competitiveness and long-term sustainability	10
3. Preparing for the future	12
Epilogue	16

Honourable Ernie Steeves
Minister of Finance and Treasury Board
Chancery Place
P.O. Box 6000
Fredericton, NB
E3B 5H1

Minister Steeves,

I am pleased to submit to you the 2023 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 279 of the *Act*.

Yours truly,

Original signed by Peter Klohn

Peter Klohn,
Chair

Section 279 of the Credit Unions Act stipulates the following:

279(1) A comprehensive review of the provisions and operation of this *Act* shall be completed by the Commission on or before October 31, 2023, and on or before October 31 of every fifth year after 2023.

279(2) When the Commission has completed a review, it shall prepare and deliver to the Minister a report on the review.

279(3) If the Legislature is sitting when a report is received by the Minister under subsection (2), the Minister shall lay the report without delay before the Legislative Assembly.

279(4) If the Legislature is not sitting when a report is received by the Minister under subsection (2), the Minister shall lay the report before the Legislative Assembly within 15 days after the commencement of its next sitting.

Interpretation

In this document:

“2018 Report” means the five-year review report filed in the Legislature on October 29, 2018.

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

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

“Commission” or “FCNB” means the Financial and Consumer Services Commission.

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

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

“League Data” means the provider of technology services to New Brunswick credit unions. It is owned by a majority of provincially regulated credit unions across Atlantic Canada.

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 January 1, 2023, six credit unions operate in New Brunswick.

New Brunswick's credit unions are an integral part of the financial and business infrastructure. Credit unions promote and contribute to the provincial economy. Credit unions in New Brunswick serve close to 61,000 members and total assets are approximately \$1.47 billion. The Canadian credit union and *caisses populaires* system assets total about \$550 billion as of December 31, 2022.

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 include credit unions in New Brunswick, Nova Scotia, Prince Edward Island and Newfoundland and Labrador.

On July 1, 2013, the provincial government established FCNB as a self-funded, independent Crown corporation. FCNB's role, through the Superintendent as the statutory regulator, was to provide oversight of the credit union system. At that time, the credit union system consisted of two separate stabilization boards: one for the credit unions and one for the *caisses populaires*.

On July 1, 2016, the *caisse populaire* system transferred to the federal jurisdiction. This left New Brunswick with 10 provincially regulated credit unions with assets totalling approximately \$1.0 billion and a regulatory structure that was disproportionate to the size of the credit union system. There was a stabilization fund and a deposit insurance fund and three organizations performing oversight activities:

- FCNB, as the statutory regulator, oversaw the system;
- Brunswick Credit Union Stabilization Board, which operated under the name of the Risk Management Agency (RMA), oversaw the stabilization fund and front-line inspections; and
- NBCUDIC oversaw the deposit insurance fund.

In 2020, the regulatory framework overseeing credit unions was updated with the proclamation of the new *Credit Unions Act*. The new framework provided FCNB with oversight of all regulatory functions and oversight of the consolidated deposit protection and stabilization fund. NBCUDIC continued as a Crown corporation with responsibility for maintaining a deposit protection fund and the mandate to protect depositors from financial loss. The new framework eliminated duplication of regulatory functions and streamlined the credit union oversight responsibilities.

The resulting framework was more affordable and reduced the regulatory burden for credit unions. The reduced regulatory costs allow credit unions to maintain their competitiveness and long-term sustainability.

Under the new *Act*, the Superintendent is responsible for operational, administrative, and regulatory functions associated with the front-line regulation of the credit unions, including inspecting credit unions, developing sound business and financial policies and practices to be followed by credit unions, issuing directives and orders, and placing a credit union under supervision when necessary. The Superintendent decides when to provide financial assistance to a credit union for the purpose of maintaining the credit union as a going concern or for the purpose of liquidating a credit union, which may include paying deposit insurance to depositors. The Commission may direct NBCUDIC regarding the type of financial assistance to provide, and NBCUDIC will provide the financial assistance to the credit union.

The Commission's role is to provide oversight over regulatory policy and stewardship of the Deposit Protection Fund and includes the following:

- approval of the fund's investment policy;
- annual evaluation of the Deposit Protection Fund to determine if the Fund is impaired or is about to be impaired, and to inform the Minister of Finance of the impairment and of the corrective measures undertaken or required;
- determination of the amount of the levies to be paid annually by credit unions into the Fund;
- determination of the amount of an impairment levy to be paid by credit unions (if necessary);
- inform NBCUDIC regarding the provision of financial assistance to a credit union or to pay out deposit insurance to depositors.

NBCUDIC's role is to protect credit unions against financial losses and insolvency. NBCUDIC has various resolution powers, including the ability to provide financial assistance to credit unions and to pay for the Commission and the Corporation's regulatory expenses incurred to administer the regulatory regime. NBCUDIC is accountable for investing the Deposit Protection Fund in accordance with the investment policy approved by the Commission.

Together, the Superintendent, the Commission and NBCUDIC play critical roles in implementing a system that promotes the competitiveness, safety and soundness of credit unions while maintaining a fund sufficient to protect credit union members' insured deposits.

Process

FCNB sought input from stakeholders as part of the five-year statutory review of the *Act*. In May 2022, FCNB invited stakeholders to provide written submissions regarding potential improvements to the *Act*. This consultation targeted feedback from Atlantic Central, the Credit Unions Managers Association (CUMA), the Canadian Credit Union Association (CCUA), NBCUDIC and the credit unions.

On March 3, 2023, FCNB held a meeting with all 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 this meeting.

Major Themes

1. Impact of the 2020 *Credit Unions Act*

The timing of the five-year statutory review of the *Act* provided an opportunity for stakeholders to identify any concerns with the new regulatory framework and comment on whether the 2020 amendments to the *Act* addressed stakeholders' previous concerns.

The 2018 Report identified areas where the *Act* could be modernized to help credit unions improve their business operations, particularly with updates to address changes in technology that would:

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

The new regulatory framework addresses electronic participation in meetings of directors. Section 104 provides that meetings of directors may be by electronic means as long as the credit union's by-laws do not *prohibit* electronic participation. This provides a "default" to electronic participation for meetings of directors. However, for meetings of members, section 90 has the default as the traditional "in-person" or paper participation, unless the by-laws *allow* for electronic participation. One commenter suggested that the default for participation at meetings of members should be similar to the default for meeting of directors. The commenter suggested that members should be able to participate at meeting by electronic means unless the by-laws specified otherwise.

The commenter noted a proposed change to section 266 to facilitate electronic communications. The commenter suggested that the default method for notices required from the credit union should be updated to electronic means, such as by sending email (to the latest email address on record) and/or by posting on the internet (e.g., the credit union's website).

One stakeholder sought clarification regarding subsection 96(1) and paragraph 153(2)(g) regarding the terms of directors when a credit union has been amalgamated:

s.96 (1): A director named in the articles of incorporation of a credit union holds office from the issue of the certificate of incorporation until the first meeting of the members

153(2)(g) the articles of amalgamation shall be deemed to be the articles of incorporation of the amalgamated credit union and the certificate of amalgamation shall be deemed to be the certificate of incorporation of the amalgamated credit union

The stakeholder suggested the *Act* should be amended to clarify that, in the context of an amalgamation, the directors and the respective terms of those directors, are those named in the articles of amalgamation. Clarification of this issue would be helpful as there have been amalgamations within the credit union system, and there may be more in the future. However, this issue has been addressed by the Superintendent, and the amalgamation that prompted this concern has been completed.

There was another suggestion regarding section 216 of the *Act* which requires the Superintendent to inspect and examine the business and affairs of each credit union at least every 18 months. The stakeholder suggested the requirement to inspect or examine a credit union should be left to the discretion of the Superintendent, similar to the requirement in Nova Scotia.¹

1. See paragraph 157(e) of the Nova Scotia *Credit Union Act*.

One commenter suggested that paragraph 264(1)(b) of the *Act*, should be amended to require the Superintendent to consult with Atlantic Central with respect to any business and financial directives the Superintendent issues to credit unions. Currently, the Superintendent may issue financial directives in relation to sound business and financial policies and practices to be followed by credit unions. The Superintendent has typically consulted Atlantic Central, but is not required to do so.

2. Competitiveness and long-term sustainability

Residential property

Another issue raised by stakeholders is the definition of residential property. The 2018 Report suggested updating the definition of “residential property” to be consistent with other credit union legislation and the Canada Mortgage and Housing Corporation (CMHC) definition. Even with the changes to the *Act* and introduction of Rule CU-001 *General* (General Rule), commenters suggested this definition should be updated to remove the requirement that at least one of the four dwellings must be owner-occupied. This would harmonize with a similar definition in Nova Scotia.²

Construction mortgages

Commenters suggested another update to the General Rule. Section 8 lists situations when a credit union cannot issue a mortgage. This provision specifies that a credit union may provide a mortgage for the purposes of purchasing, renovation or improving the property or to refinance a mortgage on the property. However, while implied, it does not specifically permit a credit union to provide a mortgage for the purpose of constructing a home on the property. This exclusion limits a credit union’s ability to offer construction loans.

2. See the definition of “residential property” in Nova Scotia *Credit Union Regulations*.

Regulatory capital required to incorporate a new credit union

In the 2018 Report, stakeholders suggested minimum capital requirements should be added to the new regulatory framework. Subsection 8(2) of the *Act* requires that a credit union has a minimum of \$500,000 in capital to qualify for incorporation. Section 15 of the General Rule requires that credit unions maintain a regulatory capital above 5% of system assets. This means that a credit union as small as \$10M in assets could be incorporated ($\$10\text{M} \times 5\% = \$500,000$). A credit union with \$10M in assets is not large enough to be sustainable long term nor to provide adequate protection to member deposits and would, therefore, expose the Deposit Protection Fund to potential claims. Currently, small provincial credit unions with \$60M in assets are struggling with increasing costs while remaining competitive. A credit union with less than \$100M in assets would face long-term sustainability challenges.

The *Loan and Trust Companies Act* requires minimum capital of \$3M in the case of a loan company and \$5M in the case of a trust company before issuing a license or incorporation. While the *Act* has a minimum capital requirement of \$500,000 for new credit unions, this requirement is subject to further requirements after incorporation and any other information required by the Superintendent. The *Act* provides rule-making authority regarding regulatory capital requirements. FCNB may consider changes to the minimum capital requirements to incorporate a credit union in the future. These potential changes would aim to enhance a new credit union's ability to withstand financial shocks and to experience asset growth while remaining competitive.

3. Preparing for the future

Capital adequacy requirements

The *Act* contains provisions for credit unions to maintain a prudent capital ratio of 5% of system assets. This is commonly called the leverage ratio. In addition to the leverage ratio, risk weighted capital adequacy standards have been adopted as prudential standards internationally (Basel), federally (OSFI), and in all provincial jurisdictions except for Prince Edward Island and New Brunswick. Industry stakeholders previously proposed a one-year pilot project that would adopt a regulatory requirement to meet risk weighted capital adequacy standards. After completing the one-year pilot project, the Superintendent and credit unions agreed to adopt a 2023 risk weighted capital adequacy requirement as an additional metric to use in evaluating capital adequacy. The New Brunswick 2023 metrics are:

Risk Weighted Capital	Minimum	Capital Conservation Buffer	Risk Weighted Capital Requirement
Common Equity Tier 1	5%	3%	8%
Total T1 Capital	6%	3%	9%
Total Regulatory Capital	8%	2.5%	10.5%

The *Act*³ provides general requirements for credit unions to maintain capital, in order to remain up to date with prudential standards internationally and federally. One commenter suggested that the *Act* should be updated to reflect a calculation of regulatory capital based on risk weighted assets. FCNB may consider adding risk weighted capital standards and requirements to the General Rule in the future.

3. Section 64 of the [Act](#) states the following:

64(1) A credit union shall adopt a capital management plan that is approved by its board of directors and that meets the prescribed requirements.

64(2) A credit union shall, in addition to the allowance referred to in section 63, maintain a level of regulatory capital in accordance with the regulations.

64(3) Despite any other provision in this *Act* or the regulations, the Superintendent may issue an order that the credit union maintain additional levels of regulatory capital if the Superintendent is of the opinion that it is in the public interest to do so.

Cybersecurity

In response to the *Notice Regarding Cybersecurity Risk* issued by FCNB in October 2019, credit unions have improved their cybersecurity posture by:

- adopting the National Institute of Standards and Technology (NIST) framework to establish appropriate policies and standard operating procedures to manage cybersecurity risks;
- engaging League Data and CGI Canada (IT and business consulting services firm) to perform vulnerability assessments for all credit unions every two years;
- completing regular reviews of cybersecurity posture to identify gaps and implement appropriate risk mitigating strategies;
- establishing internal IT specialist roles within Brunswick and OMISTA credit unions; and
- engaging third-party IT and cybersecurity specialists to assist in improving cybersecurity posture.

While credit unions have voluntarily devoted a significant amount of effort and resources toward improving their cybersecurity posture, there are no regulatory requirements for credit unions in regard to cybersecurity. FCNB may consider requiring credit unions to have a cybersecurity management plan that would strengthen and formalize cybersecurity governance and risk management activities. This may be addressed in future amendments to the General Rule as the *Act* provides rule-making authority governing the requirements of sound business and financial policies and practices (paragraph 283(1)(j) of the *Act*).

Federal cybersecurity legislation

On June 14, 2022, the federal Minister for Public Safety introduced Bill C-26 *An Act respecting cyber security, amending the Telecommunications Act and making consequential amendments to other Acts*. This *Act* introduces a requirement for identified regulatory sector participants to formalize the process of establishing and documenting cybersecurity risks, policies and processes in a cohesive cybersecurity management plan. FCNB will continue to monitor this proposed legislation and may introduce similar requirements in the General Rule to formalize cybersecurity governance and risk management practices and activities, consistent with the federal requirements.

Open banking

In July 2022, the federal Department of Finance launched four open banking working groups (addressing accreditation, liability, privacy and security), each tasked with developing recommendations to inform Canada's open banking framework. Open banking is the practice of enabling different systems, devices, applications or products to connect and communicate in a coordinated and secure way. In the banking industry, this involves allowing third-party payment service and other financial service providers to access banking transactions and other data from banks and financial institutions.

One commenter noted that, while it was premature to speculate on the outcome of the discussion or the possible direction of the framework, it is possible that some amendments to the credit union regulatory framework may be required to enable credit unions to fully participate in open banking.

Administrative penalties issued by notice

Administrative penalties issued by notice have been identified as a means for the regulator to be more responsive and efficient to certain violations under financial and consumer services legislation. Although all Act or rule violations are serious and require attention, they may not always warrant the significant time and resources needed to pursue a full enforcement proceeding before the Tribunal. Despite this, not addressing these violations adequately can result in reputational harm for the regulator and cause these types of violations to proliferate. Administrative penalties issued by notice would provide FCNB with a compliance tool that could be used for minor violations and would serve as an immediate deterrent for future violations. Provisions regarding administrative penalties issued by notice were included in the *Financial Advisors and Financial Planners Title Protection Act* and similar provisions may be considered for the *Credit Unions Act* in the near future.

The regulatory framework

With the introduction of the new *Credit Unions Act* in 2020, the regulatory framework for credit unions was restructured to streamline responsibilities, eliminate duplication and reduce regulatory burden and costs for credit unions. While FCNB is an integrated regulator, responsible for administering the *Credit Unions Act* and prudential regulation of the credit union system, maintaining a fund for the purposes of deposit insurance and stabilization are the responsibility of NBCUDIC.

There have been notable changes in the regulatory framework overseeing credit unions in Ontario. In 2018, the Financial Services Regulatory Authority of Ontario (FSRA) assumed the regulatory duties of the Financial Services Commission of Ontario (FSCO) and the Deposit Insurance Corporation of Ontario (DICO). FSRA is responsible for the operation and prudent management of the Deposit Insurance Reserve Fund (DIRF). The DIRF is a separate reporting entity from FSRA's operations. The DIRF revenues, assets and investments are segregated from FSRA and the DIRF financial statements are audited. The DIRF Advisory Committee has the oversight responsibility to oversee management in its monitoring of the DIRF.

As the regulatory landscape continues to evolve, it is possible that further amendments to the regulatory framework for credit unions in New Brunswick may be considered.

Epilogue

The review of the *Credit Unions Act* every five years as required by section 279 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.