



Banc Ceannais na hÉireann
Central Bank of Ireland

Eurosystem

Section 35

Regulatory Requirements for Credit Unions

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Registry of Credit Unions

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Section 35 – Regulatory Requirements for Credit Unions

Introduction

The Central Bank Reform Act 2010 amends the limit for lending over five years set out in Section 35 of the Credit Union Act, 1997. **The amended lending limit is accompanied by regulatory requirements** (“requirements”) relating to liquidity; lending practices for rescheduled loans; provisioning for rescheduled loans; and systems, controls and reporting **that apply to all credit unions irrespective of the percentage of lending over five years.**

With effect from 1 October 2010, the Section 35 limit on lending over five years has been raised from 20 per cent to 30 per cent of total gross loans outstanding¹. The requirements and the transitional arrangements are set out in this document as follows:

- Section 1 sets out the requirements on liquidity;
- Section 2 sets out the requirements on lending practices for rescheduled loans;
- Section 3 sets out the requirements on provisioning for rescheduled loans;
- Section 4 sets out the requirements on systems, controls and reporting; and
- Section 5 deals with the transitional arrangements for certain requirements.

These requirements are effective from 1 November 2010. Credit unions may be subject to regulatory action by the Registry of Credit Unions (“the Registry”) for failing to comply with these requirements.

¹ The limit on lending over 10 years will remain at 10 per cent. The longer term lending limits will continue to apply to those credit unions that have been approved to avail of the longer term lending limits.

Glossary

Attached Savings

Attached savings are those savings which are attached to loans or otherwise pledged as security and are not withdrawable by members.

Gross Loan

Gross loan is the total outstanding loan amount remaining to be repaid by a member.

Liquid Assets

Liquid assets are cash and investments with less than three months to maturity, excluding the minimum reserve requirement.

Liquidity Ratio

Liquidity Ratio is liquid assets as a percentage of unattached savings.

Net Loan

Net loan is the outstanding loan amount remaining to be repaid by a member less any attached savings.

Rescheduled Loans

Rescheduled loans are those loans where the repayment conditions have been altered so that the duration of the loan is extended and the loan was in arrears at the time of reschedule, or the loan would have fallen into arrears if it had not been rescheduled because the terms of the original loan agreement would no longer be met.

Single or Lump Sum Repayment Loans

Single or lump sum repayment loans are those loans whose repayment takes the form of a single payment, or where the repayment schedule is less frequent than monthly.

Unattached Savings

Unattached savings are those savings which are not attached to loans or otherwise pledged as security and are withdrawable by members. Unattached savings include budget accounts with a positive balance.

1. Liquidity

Minimum Liquidity Requirements

- 1.1** A credit union must at all times keep a proportion of its total assets in liquid form so as to enable the credit union to meet its liabilities as they arise².
- 1.2** Credit unions are required to maintain a **minimum Liquidity Ratio of not less than 20 per cent**³ on an on-going basis⁴.
- 1.3** Notwithstanding this minimum liquidity requirement, it is the responsibility of the board of directors of each credit union to decide on the amount of liquid assets to hold in excess of the minimum, taking prudent account of the scale and complexity of the credit union's business, its funding requirements and prevailing market conditions.
- 1.4** Where it is considered appropriate, the Registry may set a ratio for a credit union, or a category of credit unions, that is higher than the minimum Liquidity Ratio.
- 1.5** Credit unions whose liquid assets are in excess of 20 per cent of unattached savings must continue to maintain liquid assets at such higher levels as are deemed prudent.
- 1.6** The board of directors of the credit union must inform the Registry immediately should the Liquidity Ratio fall below 20 per cent and take the appropriate measures to restore the Liquidity Ratio to the required level as soon as possible. The timeframe in which the ratio will return to compliance must be agreed with the Registry.

² Section 85(1) of the Credit Union Act, 1997.

³ See Section 5 for Transitional Arrangements.

⁴ Credit Union Act 1997 (Section 85) Rules 2010.

Section 35 – Regulatory Requirements for Credit Unions

1. Liquidity

Additional Liquidity Requirements for credit unions where lending over five years is above 20 per cent

1.7 Any credit union that wishes to increase its lending over five years above 20 per cent of total gross loans outstanding must hold additional liquidity. The additional liquidity requirements are set out in the table below and these requirements must be met **before** the credit union increases its lending over five years⁵.

Lending Over Five Years	Minimum Liquidity Ratio
>20% and <25%	at least 25%
≥25% and <29%	over 25%
≥29%	at least 30%

1.8 The board of directors of the credit union must inform the Registry immediately should the Liquidity Ratio fall below the required limits set out above. The credit union must cease making any further loans over five years until the Liquidity Ratio has returned to compliance and the credit union has received confirmation from the Registry that it is in order to do so.

⁵ See Section 5 for Transitional Arrangements.

2. Lending Practices for Rescheduled Loans

- 2.1** Loans must only be rescheduled in exceptional circumstances, at the request of the member and where relevant, with the agreement of the guarantor.
- 2.2** An application to reschedule a loan must be supported by appropriate fact finding and a new loan application. The application must be accompanied by evidence of the member's request to reschedule the loan and evidence of the change in the member's circumstances.
- 2.3** Loans must only be rescheduled with the agreement of the member and where relevant, the guarantor. A new credit agreement must be drawn up and the member must be made aware of any changes to the information contained in the original credit agreement, including changes to the cost of credit.
- 2.4** The new repayment schedule put in place for **all** rescheduled loans must not be less frequent than quarterly.
- 2.5** **In general, further credit must not be granted where a loan has been rescheduled.**
- 2.6** In exceptional circumstances the credit union may determine it prudent to grant additional credit to a member with a rescheduled loan that has performed in accordance with the new terms for a period of at least one year. The provision held against the existing rescheduled loan must remain.
- 2.7** Where a member's rescheduled loan has not performed in accordance with its terms for a period of at least one year, in limited circumstances if the credit union considers it necessary, small amounts of credit (maximum of €1,000 per member) may be granted to such members to cover exceptional expenses only. Any additional credit granted in these circumstances must be approved by the board and the rationale for extending such credit clearly documented. The maximum exposure limit for gross loans outstanding of this type at any one time is the higher of €5,000 or 0.5 per cent of the Total Regulatory Reserve⁶.

⁶ See 'Regulatory Reserve Ratio for Credit Unions – August 2009' available on www.centralbank.ie.

3. Provisioning for Rescheduled Loans

- 3.1** The responsibility for provisioning for bad and doubtful debts remains with the board of directors of each credit union. The requirements set out below are minimum requirements. Credit unions must ensure that the level of provisions held against rescheduled loans is adequate and that the financial accounts show a true and fair view. **Any amendment, alteration or change to a loan to avoid making bad debt provisions shall be considered a breach of these requirements and may result in regulatory action.**

Minimum provision required when a loan is rescheduled

- 3.2** When a loan is rescheduled a minimum provision, identifiable as a provision for rescheduled loans and capable of being inspected and audited, must be made against the loan. **This minimum provision⁷ must be the higher of 20 per cent of the net loan and any provision that existed at the time of reschedule.**
- 3.3** This minimum provision must be maintained until the **loan is repaid in full or written off.**
- 3.4** The financial impact of default associated with loans with atypical arrangements, for example single or lump sum repayment loans, can be significant. Accordingly, where such loans are rescheduled, an assessment must be made to determine whether a further provision should be made for the loan in addition to the minimum provisioning requirement set out in Requirement 3.2.

Provision required for rescheduled loans that perform in accordance with the new terms for at least one year

- 3.5** Notwithstanding Requirement 3.3, where the member has complied with the terms of the new loan agreement for a period of at least one year and the provision held against the rescheduled loan is greater than 20 per cent of the net loan then the credit union may, if it deems it to be appropriate, reduce the provision to 20 per cent of the net loan.

⁷ See Section 5 for Transitional Arrangements.

3. Provisioning for Rescheduled Loans

Provision required for rescheduled loans that fail to perform in accordance with the new terms

3.6 Additional provisions must be made for rescheduled loans that fail to perform in accordance with the new terms. The graduated provisioning requirement for such loans is set out in the table below. The **minimum provisioning requirement**⁸ is calculated based on the **combined weeks in arrears** which is *'the number of weeks the loan was in arrears at the time of reschedule plus the number of weeks the loan is in arrears since the loan was rescheduled'*.

Combined Weeks in Arrears⁹	Minimum Provision Required (% of Net Loan)
0 – 26 weeks	20%
27 – 39 weeks	40%
40 – 52 weeks	60%
53 weeks or over	100%

The Appendix contains two illustrative examples¹⁰ of the minimum provision required for rescheduled loans that do not perform in accordance with the new terms following reschedule.

Provision required for loans that are rescheduled more than once

3.7 Any loan that is **rescheduled more than once** must be provided for in full and the full provision must be maintained until the loan has been repaid in full or written off.

3.8 Notwithstanding Requirement 3.7, where a rescheduled loan that has been rescheduled more than once has performed in accordance with the new terms since the last reschedule for a period of not less than two years, it may be appropriate to review the level of provision held but this must not be less than the minimum requirement of 20 per cent.

⁸ See Section 5 for Transitional Arrangements.
⁹ Combined Weeks in Arrears should be calculated using the principal amount in arrears. Interest arrears should not be included.
¹⁰ These examples are for illustrative purposes only and are not intended to cover all circumstances.

3. Provisioning for Rescheduled Loans

- 3.9** A trial period of up to a maximum of three months may be agreed with the member and applied to a rescheduled loan at the time of the initial reschedule. The minimum provisioning requirement, in accordance with Requirement 3.2, must be held from the initial reschedule date. Any alteration of the repayment conditions at the end of the trial period is not considered a second reschedule.

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4. Systems, Controls and Reporting

- 4.1** Full details of all rescheduled loans must be entered in a **Register of Loan Amendments**. Rescheduled loans must be clearly designated and identifiable in the electronic loan records of the credit union and must be capable of being audited. It must be possible to generate detailed reports on all rescheduled loans from these records for inspection by the Registry.
- 4.2** Credit unions must monitor rescheduled loans on an ongoing basis to assess the performance of each rescheduled loan against the new loan agreement and must report on rescheduled loans to the board at each monthly board meeting.
- 4.3** Credit unions must ensure that they review their total loan portfolios, including rescheduled loans, on a quarterly basis to verify the adequacy of the provision for bad and doubtful debts, and that any resulting adjustments to the provision are incorporated into the monthly management accounts submitted to the board, and the Prudential Return submitted to the Registry.
- 4.4** A full review of the bad debt provisions, including the provisions held against rescheduled loans, must be undertaken as part of the year-end annual accounts preparation and audit process.
- 4.5** Credit unions must ensure they have the appropriate processes, procedures, systems, controls and reporting arrangements in place to monitor compliance with the Section 35 limits and these requirements.
- 4.6** Credit unions must submit a quarterly report on rescheduled loans to the Registry in the format required. The standard template report will be provided to each individual credit union. **The completed report must be received by the Registry no later than 21 days following the reporting period end in accordance with the timelines set out below.**

Reporting Period	Submission Deadline
31 December	21 January
31 March	21 April
30 June	21 July
30 September	21 October

5. Transitional Arrangements

Liquidity Requirements

- 5.1** Where a credit union does not have adequate liquid assets to meet the minimum Liquidity Requirements set out in Section 1 by 1 November 2010, the credit union must provide the Registry with a plan for achieving compliance with the minimum Liquidity Ratio within the shortest timeframe possible. This plan must be submitted no later than 30 November 2010.
- 5.2** Credit unions that are unable to meet the relevant minimum Liquidity Requirements as set out in Requirement 1.7 may be subject to certain restrictions in their business.
- 5.3** Where a credit union does not have the liquid assets to meet the minimum Liquidity Requirements set out in Section 1, the credit union must not make any further loans over five years until the required Liquidity Ratio is achieved.

Minimum provision required when a loan is rescheduled

- 5.4 Requirement 3.2:** Transitional arrangements apply until 30 September 2011 whereby credit unions must make a minimum provision for rescheduled loans that is the **higher of 15 per cent of the net loan and any provision that existed at the time of reschedule**. From 1 October 2011 the minimum provisioning requirement set out in Requirement 3.2 applies.

Provision required for rescheduled loans that fail to perform in accordance with the new terms

- 5.5 Requirement 3.6:** Transitional arrangements apply until 30 September 2011. These arrangements are set out in the table below. From 1 October 2011 the table set out in Requirement 3.6 applies.

Combined Weeks in Arrears	Minimum Provision Required (% of Net Loan)
0 – 18 weeks	15%
19 – 26 weeks	20%
27 – 39 weeks	40%
40 – 52 weeks	60%
53 weeks or over	100%

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Appendix – Illustrative examples of rescheduled loans that fail to perform in accordance with the new terms¹¹

Example 1 – Loan that is **not in arrears** is rescheduled and the loan subsequently fails to perform in accordance with the new terms.

A **minimum provision of 20%** is required **at the time of reschedule**. The table below shows the minimum provision required **over time** as the rescheduled loan **falls in arrears** and the position if the **arrears are subsequently repaid in full**.

Loan performance over time	Weeks in Arrears since Reschedule	Combined Weeks in Arrears	Minimum Provision Required
Loan is rescheduled (No arrears at the time of reschedule)	0	0	20%
Loan falls 10 weeks in arrears following reschedule	10	10	20%
Loan falls 27 weeks in arrears following reschedule	27	27	40%
Arrears repaid in full. Loan is 0 weeks in arrears following reschedule	0	0	20%

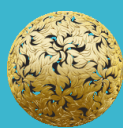
Example 2 – Loan that is **30 weeks in arrears** is rescheduled and the loan subsequently fails to perform in accordance with the new terms.

A **minimum provision of 40%** is required **at the time of reschedule**. The table below shows the minimum provision required **over time** as the rescheduled loan **falls in arrears** and the position if the **arrears are subsequently repaid in full**.

Loan performance over time	Weeks in Arrears since Reschedule	Combined Weeks in Arrears	Minimum Provision Required
Loan is rescheduled (30 weeks in arrears at the time of reschedule)	0	30	40%
Loan falls 10 weeks in arrears following reschedule	10	40	60%
Loan falls 27 weeks in arrears following reschedule	27	57	100%
Arrears repaid in full. Loan is 0 weeks in arrears following reschedule	0	30	40%

¹¹ These examples are for illustrative purposes only and are not intended to cover all circumstances.

T +353 1 224 4228 F +353 1 224 4209 www.centralbank.ie rcusupervision@centralbank.ie



Banc Ceannais na hÉireann
Central Bank of Ireland

Eurosystem

**Bosca OP 559, Sráid an Dáma, Baile Átha Cliath 2, Éire
PO. Box No 559, Dame Street, Dublin 2, Ireland**