World Council of Credit Unions

99 M Street, SE, Suite 300 Washington, DC 20003

www.woccu.org

COVID-19 GUIDE for CREDIT UNIONS - REGULATOR and OPERATIONAL RESPONSES

Andrew T. Price, Esq., BSACS, CUCE, CUERME

Vice President of Advocacy; aprice@woccu.org

Panya N. Monford, Esq.

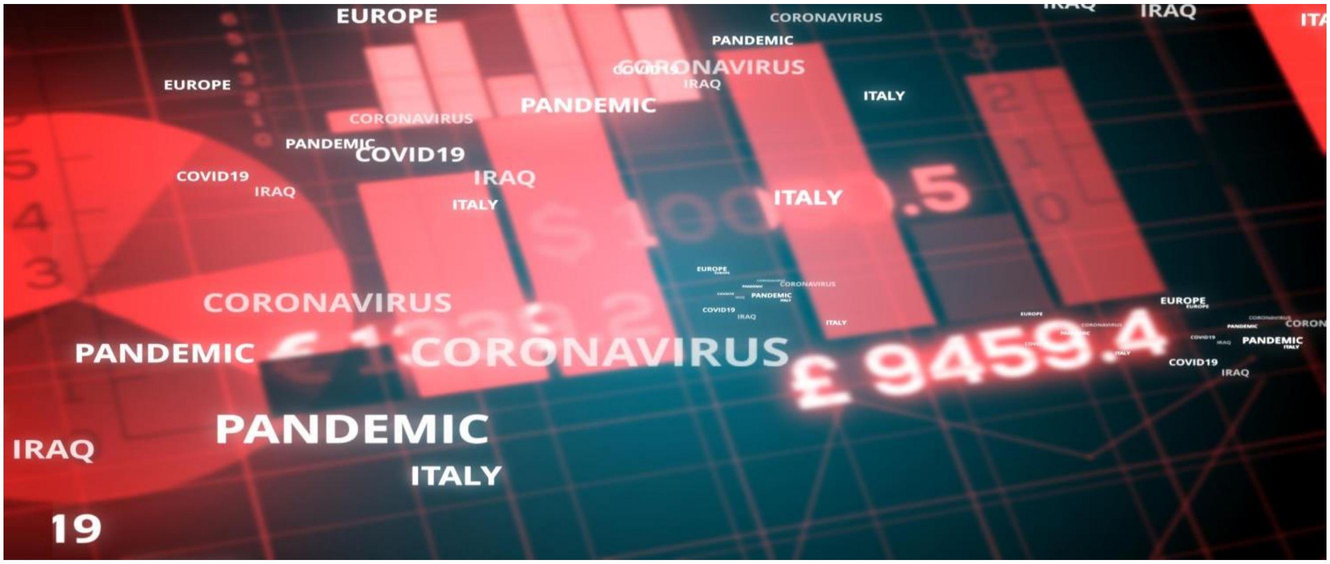
Advocacy Counsel; pmonford@woccu.org

TABLE OF CONTENTS

Introduction

In the wake of the COVID-19 Pandemic, International Standard Setting Bodies, prudential authorities and many national-level authorities have issued numerous responses designed to provide market trust and transparency, foster economic and financial stability, and assist credit unions in playing a significant role in addressing COVID-19 related issues.

This Guide is designed to illuminate the various responses taken by key regulatory authorities and how they might affect credit union regulatory frameworks at the national level. It will further discuss key credit union responses to the COVID-19 pandemic worldwide.



Credit Unions must be considered "essential" during the Covid-19 crisis.

Regulations:

How regulatory bodies respond to COVID-19 is critical to the survival of credit unions. Flexibility and a rapid response to the ever-changing financial landscape is imperative to support essential services for the most underserved in our communities.

Operations:

Financial resilience becomes an impossibility without flexibility of standards, and clear regulatory approval of such flexibility. Accounting, capital standards, IT requirements and lockdown orders all must be considered carefully during the crisis to allow effective operation of credit unions.

Regulatory Flexibility

With the understanding that COVID-19 represents a global health crisis, all regulatory bodies should provide sufficient flexibility to allow a credit union to adopt to the change in circumstances and adopt their operations to assist with the health crisis, cope with increased institutional stress and adjust for the upcoming likely global recession.

International standard setting bodies have signaled the need for this flexibility and national-level authorities are urged to follow suit.

The Financial Stability Board led the way by issuing a statement that includes the following:

> The FSB encourages authorities and financial institutions to make use of the flexibility within existing international standards to provide continued access to funding for market participants, and for businesses and households facing temporary difficulties from COVID-19, and to ensure that capital and liquidity resources in the financial system are available where they are needed. Many members of the FSB have already taken action to release available capital and liquidity buffers, in addition to actions to support market function and accommodate business continuity plans.

Resources: Financial Stability Board, *FSB coordinates financial sector work to buttress the economy in response to COVID-19* (March 2020), *available at* https://www.fsb.org/2020/03/fsb-coordinates-financial-sector-work-to-buttress-the-economy-in-response-to-covid-19/

Designation as Essential

Credit unions should be designated as "essential" during the COVID-19 crisis. Some jurisdictions do not currently include credit unions in the definition of essential, even though this classification has been extended to banks. Credit unions should be allowed to play a critical role in supporting people recently impacted by the pandemic, allowing them to provide pro-consumer financial services to help consumers weather the crisis. Exclusion from the definition of essential prohibits them from providing these necessary and often life-saving services.

The Financial Stability Institute of the Bank of International Settlements stated in FSI Brief No. 2, as follows:

> A key financial worker or a critical worker fulfils a role that is necessary for the bank to continue to provide essential financial services to consumers, or to ensure the continued functioning of payment systems and markets. In order for these individuals to be able to perform their roles, they might have to be exempted from some of the restrictions imposed by public authorities in response to the pandemic, such as access restrictions to workplaces.

Resources:

WOCCU Press Release on Designation as Essential: https://www.woccu.org/newsroom/releases/Credit_Unions_Must_Be_Considered_Essential_During_COVID-19_Crisis;

Financial Stability Institute of the Bank of International Settlements , FSI Briefs No. 2, *available at* https://www.bis.org/fsi/fsibriefs2.pdf

NCUA Letter to Credit Unions (20-CU-03): https://www.ncua.gov/regulation-supervision/letters-credit-unions-other-guidance/identification-essential-critical-infrastructure-workers-during-covid-19

Capital Standards

The Basel Committee on Banking Supervision has undertaken numerous measures in response to the COVID-19 pandemic.

First, numerous compliance dates within the Basel III Framework have been delayed as follows:

- The implementation date of the Basel III standards finalized in December 2017 has been deferred by one year to 1 January 2023. The accompanying transitional arrangements for the output floor have also been extended by one year to 1 January 2028.
- The implementation date of the revised market risk framework finalized in January 2019 has been deferred by one year to 1 January 2023.
- The implementation date of the revised Pillar 3 disclosure requirements finalized in December 2018 has been deferred by one year to 1 January 2023.

Next, the Basel Committee issued guidance on other issues affecting capital and accounting standards as follows:

1. **Expected credit loss accounting:** The Basel Committee notes that regarding the SICR assessment, relief measures to respond to the adverse economic impact of COVID-19, such as public guarantees or payment moratoriums, granted either by public authorities or by banks on a voluntary basis, should not automatically result in exposures moving from a 12-month ECL to a lifetime ECL measurement.
2. **Expected credit loss accounting transitional arrangements:** The Basel Committee is allowing for the implementation of several transitional arrangements, including applying exiting transitional arrangements even if those were not implemented initially. Additionally, a two-year period comprising of the years 2020 and 2021, is being allotted where jurisdictions may allow banks to add-back up to 100% of the transitional adjustment amount to CET1. The "add-back" amount must then be phased-out on a straight-line basis over the subsequent three years.

3. **Capital treatment of non-performing loans, loans subject to moratorium or past due:** The Basel Committee also provided treatment for a loan that might otherwise be considered troubled or in default, noting that jurisdictions can apply relief criterion for payment moratorium periods (public or granted by banks on a voluntary basis) relating to the COVID-19 outbreak such that they can be excluded by banks from the counting of days past due. Another criterion used is whether a bank considers that the borrower is unlikely to pay its credit obligations. The Committee has agreed that this assessment should be based on whether the borrower is unlikely to be able to repay the rescheduled payments.
4. **Non-centrally cleared derivatives:** The Committee and the International Organization of Securities Commissions have agreed to defer the final two implementation phases of the framework for margin requirements for non-centrally cleared derivatives by one year.

Finally, the Basel Committee has signaled flexibility to national-level regulators in its statements as follows:

> The Basel Committee notes that member jurisdictions are pursuing a range of regulatory and supervisory measures to alleviate the financial stability impact of COVID-19, including measures targeting the provision of lending by banks to the real economy and to facilitate banks' ability to absorb losses in an orderly manner. The Committee notes that supervisory authorities also have additional flexibility to undertake further measures if needed.

Guidance from The Financial Stability Institute provides the overall considerations for national level authorities suggesting deliberation of the following:

- In the wake of the COVID-19 pandemic, several prudential authorities and the Basel Committee introduced a series of measures to clarify how banks should consider various public and private debt relief programs—both in their ECL estimates and in their calculation of regulatory capital. These measures are intended to incentivize banks to continue supporting the real economy, while reducing pressure on banks' ECL provisions, earnings and regulatory capital.

- Supervisory initiatives that provide capital relief should be augmented by severe constraints on the payment of dividends, bonuses and share buybacks. These joint actions will simultaneously expand banks' lending capacity and enhance their ability to absorb losses.
- Prudential authorities face difficult trade-offs as they confront the most severe economic crisis in modern times. Encouraging the use of flexibility in applicable accounting standards while preserving market trust and transparency in the reported financial statements of banks will be key in fostering both economic and financial stability.

Resources:

Basel Committee on Banking Supervision, Press Release (March 20, 2020) *available at*: **https://www.bis.org/press/p200320.htm.**

Basel Committee on Banking Supervision, Press Release (March 27, 2020) *available at:* **https://www.bis.org/press/p200327.htm.**

Basel Committee on Banking Supervision, *Measures to Reflect the Impact of COVID-19* (April 2020) *available at:* **https://www.bis.org/bcbs/publ/d498.pdf.**

Financial Stability Institute, FSI Briefs No. 3, *Expected Loss Provisioning Under a Global Pandemic* (April 2020) *available at:* **https://www.bis.org/fsi/fsibriefs3.pdf.**

Accounting Standards

IFRS:

The IFRS Foundation published a document entitled "IFRS 9 and COVID-19, Accounting for expected credit losses applying IFRS 9 Financial Instruments in the light of current uncertainty resulting from the COVID-19 pandemic", which was created to address IFRS 9 application questions during this pandemic. The document outlines applicable accounting standards related to expected credit losses (ECL) that may arise during the COVID-19 pandemic.

Of note, the document outlines that extensions of payment holidays to all borrowers in particular classes of financial instruments should not automatically result in all those instruments being considered to have suffered an SICR. It also notes that it is likely difficult at this time to incorporate the specific effects of COVID-19 and government support measures on a reasonable and supportable basis into expected loss calculations but urges post-model overlays or adjustments to be considered at appropriate times.

The document suggests the use of "all reasonable and supportable information available" when determining ECL and lifetime losses. It further characterizes IFRS 9 as flexible, suggesting that during these times it may be necessary to adjust "approaches to forecasting and determining when lifetime losses should be recognized to reflect the current environment." The Foundation also recommends deferring to guidance provided by prudential and securities regulators, including guidance issued by the European Banking Authority, the European Central Bank, the European Securities and Market Authority, the Prudential Regulation Authority and the Malaysian Accounting Standards Board.

> ***WOCCU Comment on Practical Problems:*** While this guidance from the regulators is helpful to provide flexibility, numerous jurisdictions have reported difficulty in obtaining specific guidance on many practical issues such as how to treat moratoriums on payments, moratoriums on foreclosures, debt collection and moratoriums on evictions. Often, not enough specificity or flexibility is afforded to a credit union on provisioning for these circumstances when the lack

of payment is due to a government order. Regulators should provide clear guidance on these issues. Further, specificity on whether interest will continue to accrue, whether missed payments can be capitalized or need to be forgiven, should be addressed.

Resources:

1. IFRS, IFRS and Covid-19, IFRS 9 and Covid-19, Accounting for expected credit losses applying IFRS 9 Financial Instruments in the light of current uncertainty resulting from the covid-19 pandemic, (March 2020) *available at* https://cdn.ifrs.org/-/media/feature/supporting-implementation/ifrs-9/ifrs-9-ecl-and-coronavirus.pdf?la=en.
2. European Banking Authority, Final Report, *Guidance on Legislative and non-legislative moratoria on Loan Repayments in the Light of the Covid-19 Crisis* (April 2020) *available at* https://eba.europa.eu/sites/default/documents/files/document_library/Publications/Guidelines/2020/Guidelines%20on%20legislative%20and%20non-legislative%20moratoria%20on%20loan%20repayments%20applied%20in%20the%20light%20of%20the%20COVID-19%20crisis/882537/EBA-GL-2020-02%20Guidelines%20on%20payment%20moratoria.pdf.
3. European Central Bank, *Letter to All Significant Institutions, IFRS 9 in the Context of the Coronavirus (COVID-19) Pandemic*, (April 2020) *available at* https://www.bankingsupervision.europa.eu/press/letterstobanks/shared/pdf/2020/ssm.2020_letter_IFRS_9_in_the_context_of_the_coronavirus_COVID-19_pandemic.en.pdf.
4. Prudential Regulation Authority, Bank of England, *Letter to Chief Executive Officer, IFRS 9, Capital Requirements and Loan Covenants* (March 2020), *available at* https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/letter/2020/covid-19-ifrs-9-capital-requirements-and-loan-covenants.pdf?la=en&hash=77F4E1D06F713D2104067EC6642FE95EF2935EBD.

IT Issues

COVID-19 has placed a tremendous pressure to provide services in a virtual or online capacity to avoid contact and transmission of the COVID-19 virus. This in turn places tremendous pressure on IT services. Specifically, guidance has been issued on the following:

- **IT infrastructure:** ensuring that IT infrastructure can support a sharp increase in usage over an extended period and taking steps to safeguard information security.
- **Third-party service providers:** ensuring that external service providers and/or critical suppliers are taking adequate measures and are sufficiently prepared for a scenario in which there will be heavy reliance on their services.
- **Cyber resilience:** remaining vigilant in order to identify and protect vulnerable systems, and detect, respond and recover from cyberattacks.

Resources:

Financial Stability Institute, *FSI Briefs No. 2, Covid-19 and operational resilience: addressing financial institutions' operational challenges in a pandemic* (April 2020), *available at* https://www.bis.org/fsi/fsibriefs2.pdf.

Member Facing Relief Items for Credit Unions to Consider

Many credit unions are placing member needs first and attempting to provide prudent financial services to assist them through the crisis. The following is a list of examples of relief services that have been provided by credit unions around the world:

Member Financial Impact Mitigation:

- **Loan Restructuring: Deferred Payment, Reduced Interest, Interest-Only Payments, Loan Extensions**
- **Debt Consolidation**
- **Advances, Low-Interest Loans for Crisis**
- **Fee Waivers**
- **No Penalty Withdrawal on Certificates of Deposit**
- **Insurance Services**

Other Support Services:

- **Financial Counseling**
- **Identity and Data Protection Guidance/Scam Guidance**
- **Health Information**

Runs on Cash/Liquidity

General advice on issues caused by a significant increase in the demand for cash are necessary to address current concerns regarding access to personal deposits. These heightened demands can often provide pressure on cash supplies and sometimes lead to unwarranted panic by the public. The following are items to consider when addressing and planning for such contingencies:

- In reference to cash, credit unions should analyze their cash/liquidity situation and place proper limits on cash withdrawals (i.e. per day/per week/per month or any combination).
- Consider that during a crisis, regular payments may not occur, thus affecting cash on hand.
- Credit unions should analyze sources of liquidity and get in touch with their corporate or central bank to see what relief they are providing.
- Educate members about how their funds are safe in the credit union and that hoarding cash at home is not necessary or safe. Central banks/prudential regulators should assist them in this effort.
- Note the existence of deposit insurance/guarantee schemes.
- Work closely with regulators to see if they will also impose moratoriums on withdrawals.
- Consider that during a crisis, it may be difficult to have cash replenished to ATMs and your credit union.

Reporting Requirements

Numerous jurisdictions have provided delays in a variety of reporting requirements. Some of these are implemented to provide relief to a credit union so the institution can focus on providing essential services to the public during the crisis. But they are also provided as a way to provide relief to a governmental unit which may also be facing stresses on resources due to employee absenteeism, effects from lockdown orders or other factors. It is worthwhile to consider requesting delays in the following areas:

Reporting Delays:

- Deadlines for Regulatory Reports
    - AML/CFT Reports
    - Required Regulatory Reporting
    - Tax Deadlines
    - Regular Exams
    - Audit Deadlines

Regulatory Relief

The following list represents items to consider when requesting regulatory relief in your jurisdiction. Not all items are necessary or may be appropriate for your country.

Regulatory Flexibility & Relief:

- Flexibility on Restructuring Loans/Documentation
- Allow Credit Unions to Make Loans with Special Terms and Reduced Documentation to Assist Members
- Reduce Provision (ALLL) Requirements for State Mandate Affected Loans
- Ease Restrictions by Correspondent Bank Services to Credit Unions
- Allow for Temporary Provision of Cash & Payment Services to Non-Members
- Allow Flexibility in Allowing Credit Unions to Adjust Hours of Service
- Allow Credit Unions to Conduct Board, Management, Membership Meetings Virtually
- Liquidity Support/Employee Support