



# REGULATORY PROPORTIONALITY

*"The intensity of supervision will depend on the nature, size, complexity and risk profile of a PRFI." - BCFSa Supervisory Framework*

Financial regulation is not national security. Edward Snowden alleged that 'collect it all' was a mantra at the U.S. National Security Agency. But this seems rather heavy-handed for regulatory oversight of small provincial credit unions. As a self-declared 'data-driven regulator', BC Financial Services Authority (BCFSA) appears intent on maximum data collection regardless of its supervisory framework and industry consequences.

## ! More intense regulation. Less risk-based approach

Following the 2008 financial markets crisis, regulators of major global banks duly turned up the heat. New mechanisms were designed and introduced to assess the capital, liquidity and risk profile of regulated financial institutions. Entities that regulators deemed 'too-big-to-fail' or 'globally systemically important banks' (G-SIB) were exposed to incremental costs, being higher compliance costs that were commensurate with their regulatory risk profile. These reporting requirements and supervisory expectations have steadily trickled down to domestic equivalents (D-SIB) and, in Canada, to provincially regulated financial institutions. The extent of due adaptation of G-SIB regulatory requirements for small community credit unions seems variable. Copy-and-paste can be a dangerous tool.

The regulatory environment for B.C. credit unions is wholly unrecognizable from a decade ago. Over recent years then BCFSA - and its predecessor FICOM - introduced numerous regulatory guidelines; escalated prudential supervisory expectations; and intensified regulatory reporting. The number, diversity and complexity of these new regulations are dizzying. By way of illustration, in late 2020, BCFSA launched an overhaul of regulatory reporting requirements for credit unions. The proposal seeks to expand data scope; introduce greater data granularity; on a more frequent basis; and from an increased number of credit unions. As regulated entities, B.C. credit unions have but three choices - comply, strategic transformation, or federal charter.

BCFSA appears to have discarded FICOM's risk-based supervisory framework. Default prudential supervision, and regulatory reporting, was relatively modest. But credit unions of larger size, greater complexity and/or intervention stage rating should be subject to commensurately escalated intensity of prudential supervisory requirement and regulatory reporting. Following a flurry of new regulatory requirements then this approach - proportionality - is now being embraced by OSFI, a federal Canada financial regulator. BCFSA should take note. Instead, BCFSA seems intent on a wholly opposite approach - standardization. Vancity Credit Union (C\$23 billion assets) and Vancouver Police Credit Union (C\$18 million assets) have order-of-magnitude organizational differences, yet BCFSA proposed regulatory reporting would impose substantially similar regulatory reporting requirements. As would credit unions with scarcity or bountiful levels of capital or liquidity. As would credit unions with low-risk or high-risk intervention stage ratings. The objective of regulatory reporting should be to ensure legislative compliance and to assist prudential supervisory assessment of composite risk rating. This risk-based approach wholly aligned with its supervisory framework. No matter. Collect it all. Fill those databases.

Some regulated entities  
have a higher risk profile




*"One of the key priorities identified in OSFI's Strategic Plan 2019-2022 is to further adapt its regulatory approaches to reflect the size, complexity and risk profile of financial institutions." – Source: OSFI 'Advancing Proportionality: Tailoring Capital and Liquidity Requirements for Small and Medium-Sized Deposit-Taking Institutions'*

## ! Credit Unions vary in size, complexity & risk profile

BCFSA should stop and think. What is the purpose of the collected data? Why do the proposed changes fall disproportionately on credit unions with less than C\$1 billion assets? How will the proposed changes have intended and/or unintended consequences on B.C. credit unions?

BCFSA should consider alternative tactics. Perhaps there could be two sets of 'standardized' regulatory reports - a simple set and a comprehensive set. This may mirror efforts in accounting standards - small, private enterprises and large, publicly listed companies produce financial statements of differing complexity. The Financial Accounting Standards Board 'Simplifying Accounting Standards' is exploring various topics related to proportionality in application of accounting standards. Perhaps there are learnings from the U.S. Federal Reserve, that has four intensities of regulatory reporting for deposits based on financial institution size. Perhaps B.C. credit unions could have an opt-in approach with a distant date rather than a near-term effective date (hat tip to peer for this pragmatic idea). Such an approach would allow smaller credit unions to consider banking system changes, resourcing requirements and/or strategic viability of the proposed changes. Perhaps CUDIC excess capital could be rebated, say on an equal dollar value basis across B.C. credit unions, to help fund process improvements, system implementation or other necessary automation to satisfy elevated reporting requirements?





## Some regulated entities have a higher complexity

BCFSA should recognize that there are multiple, diverse & complex changes impacting B.C. credit unions. BCFSA-required transformation of statutory liquidity deposits. Central 1 and membership driven implementation of digital technologies. BCFSA new supervisory expectations, such as the January 2021 Liquidity Guideline. At this time, BCFSA has four active consultations with credit unions - regulatory reporting, CUDIC assessments, IT Security, Outsourcing. Some requirements may even be competitive. For example, if credit unions respond the proposed regulatory reporting by sharing expert resource then this may create resource dependency and outsourcing risk. But if credit unions respond by recruiting dedicated staff or investing in technology then this will impact prudential supervisory assessment of earnings risk. Credit unions less than C\$1 billion assets face a lose-lose situation..

*"It certainly seems possible that BCFSA consequences and Competition Bureau objectives, as they relate to credit union amalgamations, may be significantly misaligned." - Ross McDonald*

Some regulated entities are large, some are small.



## BCFSA proposals will impact minimum efficient scale

Collectively these, mostly BCFSA driven, changes will permanently impact the B.C. credit union system. Ultimately, ever-increasing baseline regulatory requirements must surely translate into fewer provincial credit unions and increased minimum efficient scale. Should BCFSA continue on its seeming path, there may be only a residual few B.C. credit unions with less than C\$1 billion assets by 2025, and perhaps none by 2030. A torrent of amalgamations seems inevitable. Per related member website, the ongoing proposed merger by six B.C. credit unions has been referred to the Competition Bureau. It certainly seems possible that BCFSA consequences and Competition Bureau objectives, as they relate to credit union amalgamations, may be significantly misaligned.

Do-as-I-say, not do-as-I-do. As part of the Ministry of Finance, FICOM reporting to industry was negligible, if anything. As a crown corporation, time will tell if BCFSA complies with the B.C. government 'Performance Reporting Principles For the British Columbia Public Sector'. The related publication, approved by the Auditor General of B.C, frames eight principles of deemed best practice that seek to support an open and accountable government. BCFSA compliance with B.C. government reporting principles for crown corporations require it to provide comprehensive disclosures to industry and to taxpayers. People who live in glass houses shouldn't throw stones.

*“BCFSA compliance with B.C. government reporting principles for crown corporations require it to provide comprehensive disclosures to industry and to taxpayers.” - Ross McDonald*





## ! Regulatory oversight on behalf of taxpayers

BCFSA executive has the near infinite authority over its expanded empire. Oversight lies in its board of directors, and ultimately the B.C. Ministry of Finance. Under the Taxpayer Accountability Principles of the B.C. government state that 'Board members act independently from the organization's executive and have the best interests of taxpayers and shareholder as their primary consideration.' Hopefully this enshrines expectations of a principal-agency relationship. Approximately 40% of British Columbians are members of B.C. credit unions. Collectively B.C. credit unions provide substantial benefit to their members, employees, communities and the B.C. economy. BCFSA Board should ask difficult questions of the executive team; demand a business case for proposed changes; and consider the collective impact on British Columbians.

In the short-term, BCFSA may amass a standardized, NSA-worthy database about B.C. credit unions. Probably significantly more than that required to fulfil the needs of executive management, board oversight or risk-based prudential supervision. In the medium term, this database may become a museum relic. A moment in time record of an industry that was subject to accelerated transformation and proactive consolidation by its regulator. A priceless collector's piece but a needless lament.

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## REFERENCES

OSFI January 2020 'Advancing Proportionality: SMSB Capital & Liquidity Requirements - Consultative Document' - [https://www.osfi-bsif.gc.ca/Eng/fi-if/in-ai/Pages/SMSB20\\_cp.aspx](https://www.osfi-bsif.gc.ca/Eng/fi-if/in-ai/Pages/SMSB20_cp.aspx)

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FICOM/BCFSA June 2012 'Supervisory Framework' - <https://www.bcfca.ca/pdf/aboutus/FICOMSupervisoryFramework.pdf>

FASB 'Simplifying Accounting Standards' - <https://www.fasb.org/simplification>

B.C. Government 2003 - "Performance Reporting Principles" - [https://www2.gov.bc.ca/assets/gov/british-columbians-our-governments/services-policies-for-government/public-sector-management/performance\\_reporting\\_principles.pdf](https://www2.gov.bc.ca/assets/gov/british-columbians-our-governments/services-policies-for-government/public-sector-management/performance_reporting_principles.pdf)

Member website for potential amalgamation of B.C. interior credit unions - <https://www.exploringstrengthandunity.ca/awesometogether.html>

U.S. Federal Reserve Reporting Requirements for deposit reporting: <https://www.federalreserve.gov/monetarypolicy/reserve-maintenance-manual-reporting-requirements.htm>

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# PERSONAL BLOG PUBLICATIONS

## ***“Canadian Credit Union Industry 2030” - Beyond the planning cycle*** (in progress)

Imagine the structure, purpose and value propositions of the Canadian credit union industry in 10 years time. Futuristic report will frame a series of ‘strawman’ scenarios that are designed to be bold, distinct and imaginative.

## ***“Proportionality in Financial Services” - Asset size, business complexity & regulatory risk profile***

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## ***“Empowering CUDIC, Beyond FICOM's Shadow” - Alternative regulatory structure (FIA/CUIA)***

CUDIC has outgrown legacy legislation and FICOM's shadow. CUDIC is responsible for deposit insurance of a C\$77 billion industry that is used by almost half of British Columbians. Larger than most Canadian credit unions then it warrants full-time, permanent executive leadership. Larger than most B.C. Crown Corporations then it deserves independent, empowered and accountable governance oversight.

## ***“Credit Union Deposit Insurance Policy” - Board Discussion Paper***

A policy of unlimited deposit insurance may have significantly supported system growth and membership confidence. But it is unknown outside of Western Canada, may cause moral hazard, and may be increasingly expensive to credit unions in terms of earnings, capital and compliance.

## ***“Leadership Vacancies” - Empty Seats, Visionaries Wanted, Glass Slippers***

There is currently a void of permanent leaders at system-level organizations that impact B.C. credit unions. All leaders of credit union centrals and relevant provincial government entities are currently appointed on an interim, acting or retiring basis. Unquestionably improbable but such are circumstances. Individually each leader has system influence but collectively they wield transformative impact.

## ***“Federal credit union value propositions” - Beyond ice cream & sprinkles***

Ice cream with sprinkles. Provincial credit unions may be framed thus by strategy academics. Some aficionados may celebrate mouthwatering flavours and ingredient providence. But many a face-smeared kid may insist that ice cream is just ice cream, and that the real magic is in choosing sprinkles. Perhaps ice cream and sprinkles represent the commonalities and variations respectively in terms of value propositions across Canadian credit unions.

## ***“Coast Capital Savings - Federal Strategy” - Good Morning Canada!***

In the movie ‘Good Morning Vietnam!’, Robin Williams encouraged troops and energized betterment. Coast Capital Savings Credit Union CEO, Don Coulter, may have executed a similar feat. Though the recent member approval of its federal credit union strategy then Coast Capital Savings has arguably broadcasted ‘Good Morning Canada!’ to the national financial services industry. It seems that industry is listening to the broadcast. A battle may loom, even if the troops wear business attire rather than army uniform. To the victor goes the right to serve members, a group that may be the primary beneficiaries of forthcoming phase of industry evolution.

## ***“Credit union intervention” - an ERM failure?***

John Lennon penned ‘we get by with a little help from our friends’. Credit unions can need help too, say when placed under regulatory intervention. Does such an act signal ineffective Enterprise Risk Management practices of the credit union?

## ***“Coast Capital Savings - Member Vote” - Federal credit union implications for the B.C. system***

One member one vote. A core principle of cooperative organizations. Coast Capital Savings Credit Union is currently conducting an important member vote. Its management and Board seek member approval to submit, and to progress, an application to the federal government for Coast Capital Savings to become a federal credit union. This is a big deal for members of Coast Capital Savings. But it also has significant and diverse implications for the B.C. credit union industry.

## ***“Governance Guideline Compliance” - Yellow card***

Symbolic ‘Olympic yellow card’ issued to the B.C. credit union industry in regards compliance with disclosure requirements of the Governance Guideline of its regulator, FICOM. Several B.C. credit unions demonstrate excellence. But the average rating is depressed by selective or negligible disclosures by many credit unions.