



BANK OF ENGLAND
PRUDENTIAL REGULATION
AUTHORITY

The Board of Directors

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Dear Directors

PRA Annual Assessment of the Credit Union sector

Your credit union is a member of the peer group made up of credit unions with total assets below £15 million and fewer than 10,000 members. While you are not subject to an individual review, we carry out an annual assessment of your credit union as part of a larger peer group. The 2019 assessment for this peer group has now taken place and we write to you with our findings.

This letter should be considered by all directors.

Single Customer View (SCV) and orderly resolution

Where a credit union fails, an up-to-date and accurate Single Customer View (SCV) file is crucial for orderly resolution. Seven credit unions failed since 1 August 2018 and by using the SCV files, the Financial Services Compensation Scheme (FSCS) has been able to make payment to eligible depositors in fewer than seven days in all cases.

While we continue testing credit unions' SCV files, prioritising credit unions where we have concerns about their sustainability and/or viability, we also expect all credit unions, regardless of size, to undertake regular reviews and updates of SCV data, and testing of SCV files and procedures.

Examples of questions that we would expect credit unions to consider while reviewing their SCV policies and procedures include:

- Are you aware of your obligation to notify the PRA of any material change to your SCV system (e.g. upon the introduction of a new IT system linked to the SCV system)?
- Is more than one individual at the credit union able to run/submit the SCV file?
- Are you relying on your IT provider to submit the file? If so, that should not be the case.
- Does the file format meet current requirements?
- How do you ensure that your software and data is up-to-date?
- Are you able to submit the file and SCV Effectiveness Report within 24 hours of a request?
- Are you treating your inactive members correctly? (For the avoidance of doubt, any account that does not meet the legal definition of dormancy, i.e. no customer-initiated transaction for 15 years, must appear on the SCV file.)
- Do you exclude accounts with zero balances?
- How do you treat inactive accounts (including sanctioned or legally disputed) and beneficiary accounts?

You can find further details about the SCV, including Frequently Asked Questions, and practical examples on www.fscs.org.uk/globalassets/scv/2017-03-24-fscs-guide-to-scv--mar-2017-final.pdf.

Governance

Financial difficulties

Should you be in financial difficulty we expect you to notify the PRA as soon as is reasonably possible by contacting the PRA's Firm Enquiries Function on 020 3461 7000 or PRA.FirmEnquiries@bankofengland.co.uk.

Succession planning

We expect the Board to take an active role in succession planning to ensure the credit union can identify, attract and retain directors with relevant skills.

Credit unions must comply not only with PRA requirements, but also with their own rules that set out requirements relating to the composition of the Board and key committees. Where the Board is unable to attract a sufficient number of active directors to continue running the credit union, existing directors must consider the future of the credit union and take appropriate action. If you are in that situation, you should contact the PRA to discuss various options available to you. You should also speak to your trade body.

Prudent management and mitigation of risks

All credit unions must ensure that their boards meet their obligations relating to prudent management and the monitoring and mitigation of risks.

Credit unions must be able to demonstrate that they measure and monitor their compliance with key financial ratios and their underlying financial position in accordance with Section 4 of the PRA's Supervisory Statement SS2/16 (Additional Activities)¹.

Operational risk and resilience and cyber security

Before undertaking strategic initiatives to expand and develop new activities, and especially online activities, it is essential to carry out a comprehensive operational risk assessment, ensuring that appropriate and adequate robust systems and controls are in place.

Important business services

We have seen an increase in the number of operational and cyber incidents in credit unions over the last year. Credit unions should think about their particular business services, how these services could be disrupted and how the credit union might need to adapt to ensure critical services can continue to be delivered through disruptions.

We expect credit unions to notify the PRA as soon as practically possible of any significant operational or cyber incidents or events that may impact on continuity of service by contacting your named supervisor or PRA's Firms Enquiries Functions.

Outsourcing

Where a credit union outsources some of its critical or important operational functions, the credit union remains fully responsible for all of its obligations under the regulatory regime. Outsourcing cannot and must not result in the delegation by the directors of their responsibilities and the credit union must retain the necessary expertise to supervise the outsourced functions.

All credit unions using or considering the use of outsourcing should review their arrangements in light of the requirements listed in Section 14 (Outsourcing) of the Credit Unions Rulebook Part

¹ <https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/supervisory-statement/2017/ss216-update>

(www.prarulebook.co.uk/rulebook/Content/Part/320139/). This includes, amongst other things, demonstrating that the credit union is able to terminate the arrangement where necessary without detriment to the continuity and quality of its provision of services to members. We have seen instances where this has not been the case and this poses a risk to credit unions and their members.

Internal fraud

In the last year, we saw an increase in frauds committed by either members of staff or directors. A number of these cases resulted in significant losses for credit unions, and in some cases it led to failure.

This highlights the importance of active involvement of directors, effective reviews of management information, strong governance and constructive challenge at all levels within credit unions. To minimise the risk of internal fraud, credit unions should have in place arrangements to ensure appropriate segregation of duties and manage conflict of interests as well as an effective internal audit function.

Provisioning

All credit unions are required to make adequate provision for bad debts². We have seen instances where credit unions have treated their bad debt incorrectly and miscalculated their provisions. This has led to instances of financial difficulty and in some cases failure. Directors must ensure that they regularly review management information relating to bad debt and provisions and should take steps such that they can be assured that the information reported to them is being correctly and properly calculated. Management information is likely to include details of rescheduled and delinquent loans and exception reports.

Directors should particularly consider:

- Automated share-to-loans transfers – where a loan in arrears has its payments taken automatically from members' shares, the loan remains in arrears and needs to be accounted for as such;
- Rescheduling loans with very small repayments resulting in breaches of the lending limit set out in the Rulebook³. Please note that – as per the rule - the term of a loan starts from its original provision and not from the date it is rescheduled; and
- Their obligation to maintain provisions where a delinquent loan is rescheduled until the loan has performed for six months⁴.

Where the Board is unsure whether a particular loan can be rescheduled or how it should be provided for, you may wish to discuss the scenario with your auditor, trade body or contact the PRA's Firms Enquiries Function on PRA.FirmEnquiries@bankofengland.co.uk.

Next steps

As directors of a credit union, you have personal and joint obligations to serve your members and to meet regulatory and legal requirements. In doing so, we expect you to bear in mind the points set out above and act appropriately. The content of this letter has been shared with all UK trade bodies and you may wish to discuss with them the points we have made.

If you have any questions about the contents of this letter, please contact the PRA's Firm Enquiries Function on 020 3461 7000 / PRA.FirmEnquiries@bankofengland.co.uk.

Yours faithfully



Marcela Hashim
Credit Unions Team

² PRA Credit Unions Rulebook Part – Rule 3.10 -www.prarulebook.co.uk/rulebook/Content/Chapter/320142/

³ PRA Credit Unions Rulebook Part – Rules 3.2/3.3

⁴ PRA Credit Unions Rulebook Part – Rule 3.12