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 above £15 million and/or with more than 10,000 members. This means that in addition to the individual assessment by your named supervisor once every two years, for which you receive feedback, we also 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.

Governance

<u>Succession planning</u>

While planning for key person risks and succession planning have generally improved in relation to senior management, we noted that some credit unions continue to find it difficult to identify, attract and retain individuals with relevant skills to act as effective directors. We expect credit unions to formalise succession planning not only for senior managers, but also for directors and committees.

We expect credit unions in this peer group to have a sufficiently detailed, comprehensive and clear succession plan with respect to positions on the Board and key responsibilities and functions.

In our judgement, a practical and effective succession plan should:

- identify clearly a potential individual or individuals with the appropriate attributes, qualities and skills to assume the role, responsibilities and duties of the position(s) in question;
- articulate a clear, coherent, comprehensive, objective and transparent process for recruiting and appointing a successor and ensuring as smooth a transition as possible; and
- be reviewed by the Board periodically (at least annually) in order that it may continue to be relevant and fulfil the requirements of the firm and its specific circumstances.

<u>Risk management</u>

Over the last twelve months, we noted significant improvements in how credit unions within this peer group manage risk. The majority of credit unions that we visited have been able to explain their risk management processes and discuss their agreed risk tolerance levels and quantitative measures and triggers used while managing risks. A number of credit unions also strengthened their senior management teams with appointments of dedicated risk and/or compliance officers.

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. We have noted greater co-operation between credit unions in this area, including shared training or engagement of independent specialists to carry out penetration testing.

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.

Credit unions in this peer group should review their incident management framework including considering how they might communicate and take decisions in a period of disruption. Directors should review potential scenarios where the credit union will not be able to operate and consider whether they have designed the organisation, people, processes and technology to adapt and ensure critical services can continue to be delivered through disruptions.

We expect the 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 the PRA's Firm Enquiries Function on 020 3461 7000 or by email on PRA.FirmEnquiries@bankofengland.co.uk.

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 Union Rulebook Part (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.

Management and monitoring of liquidity

Many credit unions within this peer group have been successful in increasing lending over the last twelve months. However, we have noted instances where either an increase in lending and/or an illiquid investment, deposit or reinvestment led to a significant reduction of a credit union's liquidity, with some credit unions falling below the minimum required level. In some cases, credit unions could only rectify their position by taking out short-term loans from other credit unions.

All credit unions are expected to maintain an up-to-date liquidity management policy statement approved by the Board. The Board should review this statement whenever there is a change in credit union's circumstances (and at least annually) as the amount and composition of liquid assets must be prudent and appropriate to the nature, scale and complexity of the business, and must reflect the risk of a sudden adverse cash flow.

Sufficient management information on liquidity, both actual position and comparison to the projected values, should be reviewed by the Board at least monthly.

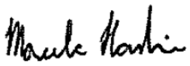
Where the credit unions rely, in a shorter-term, for their liquidity on loans from other credit unions, they should note that the lending limits set out in Rules 3.4 and 3.5 of the PRA Credit Unions Rulebook Part apply to loans between credit unions[1].

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 your name supervisor or the PRA's Firm Enquiries Function on 020 3461 7000/PRA.Firmenquiries@bankofengland.co.uk.

Yours faithfully



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[1] Except subordinated loans where limits do not apply.