

Chapter 2

New Brunswick Credit Union Deposit Insurance Corporation

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New Brunswick Credit Union Deposit Insurance Corporation

Background

2.1 Credit unions and caisses populaires are an important part of the financial services industry in New Brunswick. There are 56 credit unions and caisses populaires in the Province with over 320,000 members. As of December 31, 2005 credit unions held \$2.7 billion in deposits.¹ This was the latest information available to us at the time of our audit.

2.2 The ultimate responsibility for insuring deposits held by credit unions has been assigned to the New Brunswick Credit Union Deposit Insurance Corporation (NBCUDIC). The Province of New Brunswick established NBCUDIC in 1994. The authority and purpose of the corporation are stated in the *Credit Unions Act*.

2.3 As part of a number of regulatory amendments announced in November 2005, the deposit guarantee provided by NBCUDIC was increased from \$100,000 to 100% of eligible deposits.

2.4 The 100% guarantee of eligible deposits, plus the fact that there are 320,000 members of credit unions, were the reasons we decided to conduct an audit of the New Brunswick Credit Union Deposit Insurance Corporation.

2.5 The fieldwork for this audit was conducted between May 2006 and July 2006. We had originally intended to include our findings in our 2006 Report; however, new information arose during the preparation of the final report. Subsequent to the completion of our fieldwork, the Province issued a press release announcing that it had set aside a total of \$60 million in funding to NBCUDIC. The details of the government package to credit unions, announced March 26, 2007, indicate that “about \$40 million will be contributed by government via NBCUDIC to

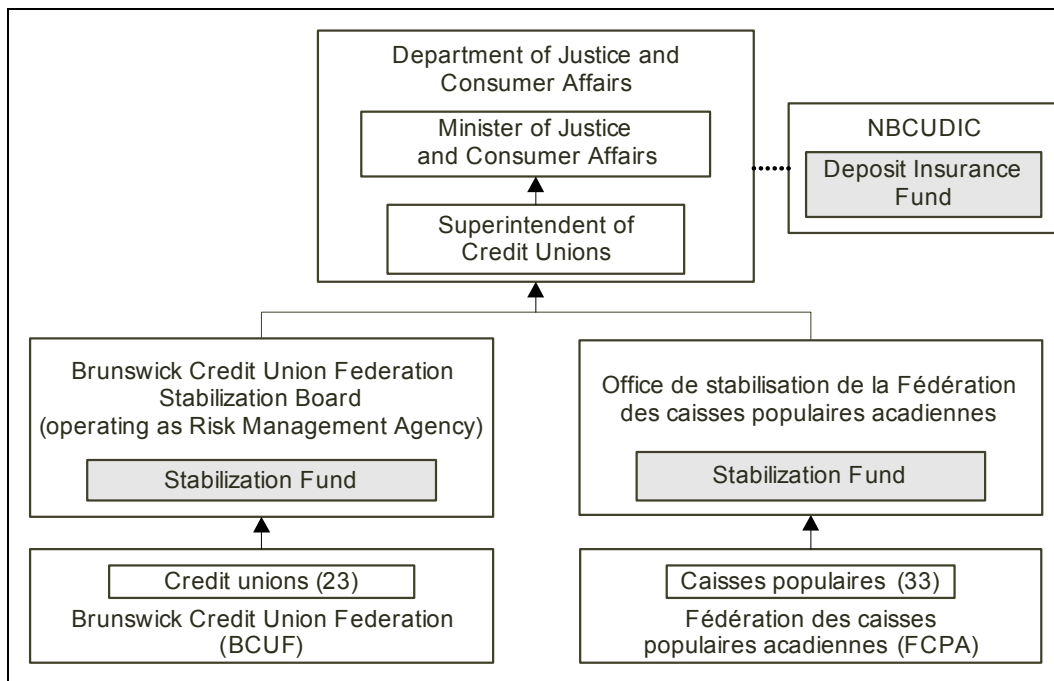
1. Throughout this chapter, the use of the term “credit union” also includes “caisse populaire”.

recapitalize la Caisse populaire de Shippagan, in order to facilitate the transfer of the caisse to la Fédération des caisses populaires acadiennes on June 1, 2007”. It goes on to state that “the remaining amount will stay with the corporation to provide for certain guarantees and contingencies related to the transfer, as well as stabilization and deposit protection for the system in general”.

New Brunswick’s credit union system

2.6 Before we report on our findings, we thought it useful to identify the various groups involved in the credit union system. The *Credit Unions Act*, proclaimed in 1994, sets the regulatory framework within which the credit union system operates. Exhibit 2.1 displays the main parties in the system.

Exhibit 2.1
Credit union system in New Brunswick



2.7 In order to carry on business in New Brunswick, all credit unions in the Province must belong to a federation; either the Brunswick Credit Union Federation Limited (BCUF) or the Fédération des caisses populaires acadiennes limitée (FCPA). Of the 56 credit unions and caisse populaires in New Brunswick, 23 are members of the BCUF while 33 belong to the FCPA¹. As stated in section 164 the *Credit Unions Act*, the purposes of a federation are:

1. As of December 31, 2005

- to receive and manage deposits made by member credit unions in relation to liquidity requirements;
- to develop and provide financial, advisory, educational and research services to member credit unions;
- to develop and promote sound business and financial policies and procedures for member credit unions;
- to promote the organization, development and welfare of credit unions in New Brunswick; and
- to encourage cooperation among cooperatives and credit unions.

2.8 Credit unions are also members of the stabilization board established in relation to the federation of which the credit union is a member. There are two stabilization boards in New Brunswick: the Brunswick Credit Union Federation Stabilization Board Limited (which operates under the name of Risk Management Agency) and l'Office de stabilisation de la Fédération des caisses populaires acadiennes limitée. The Act states in section 196 that their purposes are:

- to protect member credit unions against financial losses and insolvency;
 - by promoting the development and implementation of sound business and financial policies and procedures by credit unions;
 - by establishing and implementing loss prevention programs and other controls; and
 - by establishing and maintaining a stabilization fund.
- to provide financial assistance to member credit unions for the purpose of stabilization.

2.9 The business and affairs of a stabilization board are managed by a board of directors consisting of eight individuals: three are elected by the representatives of its member credit unions; two are appointed by the Minister; two are appointed by the board of directors of the federation for which the stabilization board was established; and the Superintendent of Credit Unions. The superintendent is a non-voting member of both stabilization boards.¹

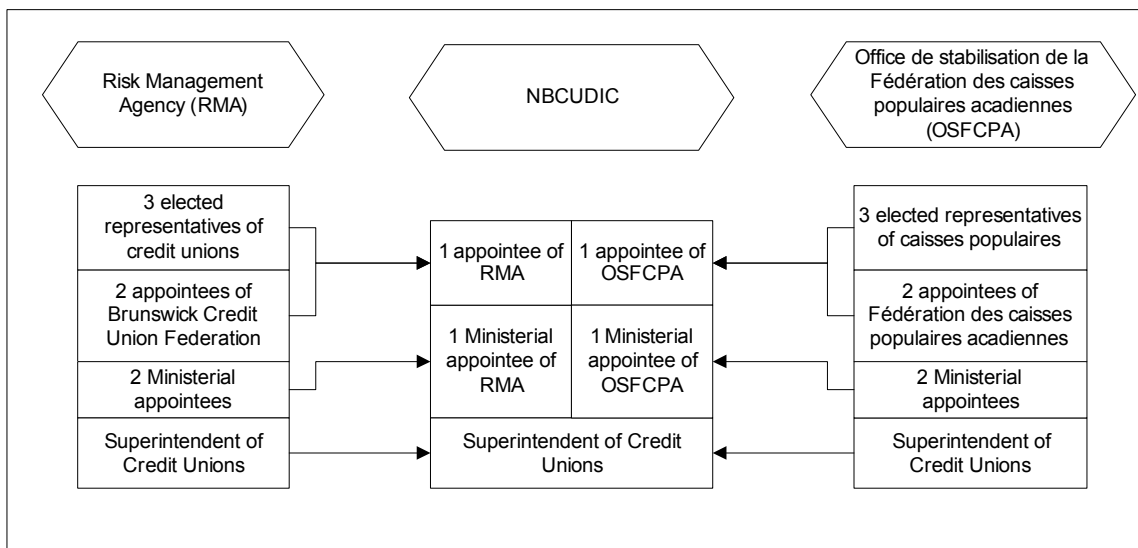
2.10 Each stabilization board has a stabilization fund, accumulated through fees paid by member credit unions. The funds can be used to provide assistance to credit unions for stabilization

1. Per section 203(1) of the *Credit Unions Act*.

purposes¹. The term “stabilization” is not defined in the *Credit Unions Act*; in our opinion, for the purposes of this chapter, it refers to a monitoring and intervention process to ensure that credit unions achieve and maintain certain prescribed financial benchmarks, such as meeting a prescribed level of equity. If a credit union falls below the prescribed level, it may need financial assistance to be “stabilized”; in other words, to attain the prescribed level once again.

2.11 As shown in Exhibit 2.2, the New Brunswick Credit Union Deposit Insurance Corporation is governed by a board of directors made up of two representatives from each stabilization board, in addition to the Superintendent of Credit Unions, who also serves as chair.² The superintendent is appointed by and employed by the Minister of Justice and Consumer Affairs. The Minister is ultimately responsible for the general administration of the *Credit Unions Act* and its regulations.

Exhibit 2.2
Board compositions



Scope

2.12 Our audit objective was:

To assess whether the New Brunswick Credit Union Deposit Insurance Corporation has adequate structures, processes and procedures in place to fulfill its obligation

1. Per sections 201, 202(2) and 202(3) of the *Credit Unions Act*.
 2. Per sections 229(1) and 230(1) of the *Credit Unions Act*.

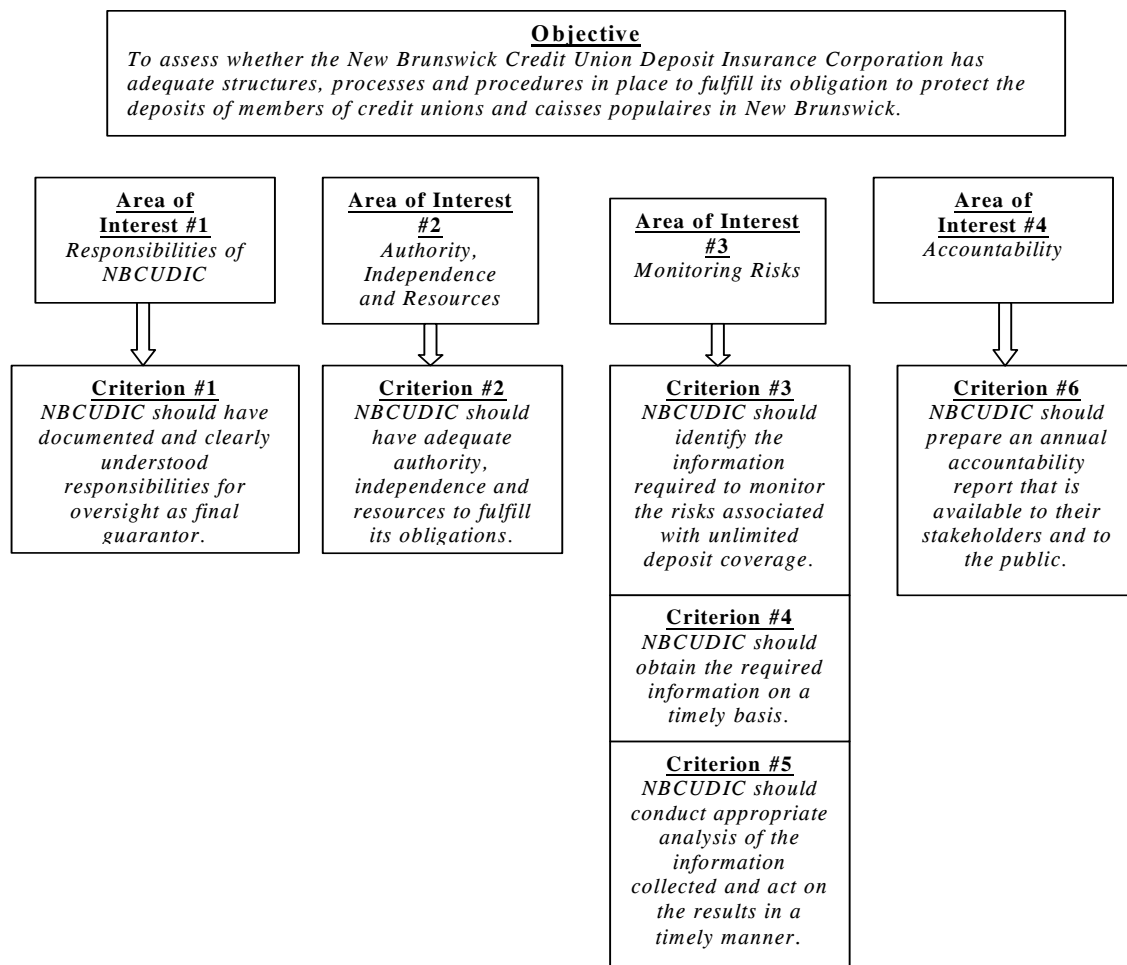
to protect the deposits of members of credit unions and caisses populaires in New Brunswick.

2.13 To further focus our audit efforts, we identified six audit criteria covering the following four areas of interest:

- responsibilities of the New Brunswick Credit Union Deposit Insurance Corporation;
- authority, independence and resources of the corporation;
- information and analysis required by NBCUDIC to adequately monitor its risks; and
- accountability of the corporation.

2.14 A summary of our audit objective and criteria can be found in Exhibit 2.3.

*Exhibit 2.3
Summary of Objective and Criteria*



2.15 Our audit was performed in accordance with standards for assurance engagements, encompassing value for money and compliance, established by the Canadian Institute of Chartered Accountants, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

Results in brief

2.16 We found that there are documented responsibilities for NBCUDIC, and that the board understands these responsibilities.

2.17 The board has identified some of the information it feels is needed to fulfill its obligations, and is receiving this information. However, there is a need to share an increased amount of information within the board to ensure directors are in an informed position. Because the board does not have adequate authority and resources, it is difficult for the board to identify further information needed. Even if the board could identify its information needs, it is unclear whether the information could be obtained.

2.18 Improvements to the annual report are needed for NBCUDIC to be adequately accountable to their stakeholders and the public.

2.19 In our opinion, NBCUDIC does not have the adequate authority, independence or resources it needs to fulfill its obligations. We therefore recommend the Province either give NBCUDIC the authority, independence and resources it needs to fulfill its mandate, or consider dissolving NBCUDIC.

Responsibilities of the New Brunswick Credit Union Deposit Insurance Corporation

Responsibilities are documented

2.20 Our first criterion is:

NBCUDIC should have documented and clearly understood responsibilities for oversight as final guarantor.

2.21 As the insurer of the deposits held in New Brunswick credit unions, we believe it is important that NBCUDIC have documented responsibilities and that the board of NBCUDIC clearly understands its responsibilities. We found two sources that identify the purposes of NBCUDIC; the *Credit Unions Act* and the corporation's annual report.

2.22 Section 216 of the Act states that the purposes of NBCUDIC are:

- to provide, for the benefit of persons having deposits with credit unions in New Brunswick, deposit insurance against loss of part or all of such deposits by making payment to the persons to the extent and in the manner authorized by the Act and the regulations; and
- to assist the stabilization boards in providing financial assistance to credit unions for the purpose of stabilization.

2.23 Meanwhile, in its 2005 annual report, NBCUDIC states that its purposes are to:

- establish and maintain a deposit insurance fund;
- provide deposit insurance against the loss of part or of all deposits for the benefit of persons having such deposits with credit unions and caisses populaires in New Brunswick;
- assist the two stabilization boards in providing financial assistance to credit unions and caisses populaires for the purposes of stabilization; and
- minimize the corporation's exposure to loss.

2.24 These purposes articulate the responsibilities of NBCUDIC. The fourth component stated in the annual report, "minimize the corporation's exposure to loss", is not directly indicated in the Act as a responsibility. For the purpose of our analysis, we used NBCUDIC's interpretation of its purposes as described in its 2005 annual report.

2.25 We discussed the responsibilities of NBCUDIC with the members of the board. We concluded that they understand the responsibilities of the corporation.

Conclusion

2.26 This criterion is met. We found that there are documented responsibilities for NBCUDIC, and that the board understands these responsibilities.

NBCUDIC's authority, independence and resources

2.27 Our second criterion is:

NBCUDIC should have adequate authority, independence, and resources to fulfill its obligations.

2.28 We have broken our discussion of this criterion into three components. They are:

- authority
- independence
- resources

Authority

2.29 In order to carry out its purpose, we believe it is important that NBCUDIC have adequate authority.

2.30 We reviewed the Act in its entirety to determine what authority has been granted to the corporation and to the other parties involved in the credit union system. We summarized the authority granted to the various parties, along with any reporting relationships, in Appendix A.

2.31 To ensure that the corporation has the required authority to fulfill its legislated purpose, we compared the authority granted by the Act to NBCUDIC to its purpose as stated in its annual report. Our findings are shown in Exhibit 2.4.

*Exhibit 2.4
Comparison of purpose and authority of NBCUDIC*

Purpose of New Brunswick Credit Union Deposit Insurance Corporation as per 2005 annual report	Authority of New Brunswick Credit Union Deposit Insurance Corporation under the <i>Credit Unions Act</i>
<ul style="list-style-type: none"> • Establish and maintain a deposit insurance fund. 	<ul style="list-style-type: none"> • Maintain deposit insurance fund. • Determine amount to be levied from credit unions (for deposit insurance fund).
<ul style="list-style-type: none"> • Provide deposit insurance. 	<ul style="list-style-type: none"> • Insure deposits.
<ul style="list-style-type: none"> • Provide assistance to stabilization boards. 	<ul style="list-style-type: none"> • Make loans or advances to stabilization boards, guarantee loans or make investments for deposit insurance fund. • Maintain deposit insurance fund. • Make or cause to be made inspections and examinations of credit unions.
<ul style="list-style-type: none"> • Minimize the corporation’s exposure to loss. 	<ul style="list-style-type: none"> • Make or cause to be made inspections and examinations of credit unions. • Maintain deposit insurance fund. • Determine amount to be levied from credit unions (for deposit insurance fund). • Borrow money on the credit of the corporation. • Apply to the Minister for loans and guarantee of loans.

2.32 It appears that NBCUDIC has the authority to fulfill the first three components of its purpose. While it has some ways to deal

with losses once they are known, it has limited authority to minimize its exposure to loss.

NBCUDIC has limited authority to minimize the corporation's exposure to loss

2.33 NBCUDIC's ability to minimize its exposure to loss is limited due to the following factors.

- Even though NBCUDIC has the authority to inspect a credit union, it does not have the authority to take direct action against a credit union that is posing a risk to the system and exposing the corporation to loss. Both the Superintendent and the stabilization boards can take action against a credit union by placing them under supervision or causing them to be placed under supervision, but NBCUDIC cannot.
- The stabilization boards are required to inspect and examine credit unions at least every 18 months, and either have staff or have contracted the services of others to carry out these inspections and examinations. However, NBCUDIC does not have the authority to obtain the results of these inspections and examinations. The results are reported to the Superintendent, the directors and auditor of the credit union, and the directors of the federation, but not NBCUDIC.

2.34 NBCUDIC does have some authority to identify the risks it faces, but its primary method to do so is direct inspection of credit unions, rather than having access to all sources of relevant information. Also, because it cannot take direct action, it does not have adequate authority to minimize the losses it faces. Even if the risks are known, the corporation has limited ability to minimize the loss to a reasonable level.

Independence

2.35 The second component of this criterion is the need for independence. In this section we examine the independence of NBCUDIC board members.

2.36 One example of independence requirements in the credit union sector in Canada can be found in the governance practices of The Credit Union Deposit Guarantee Corporation of Alberta. It has established governance practices consistent with the Guidelines for Improved Corporate Governance in Canada adopted by the Toronto Stock Exchange. Their corporate governance practices on independence require that a majority of board members should be independent of management and free from any business or other

relationships which would be perceived to interfere with the director's ability to act in the best interest of the corporation.

2.37 The *Credit Unions Act* recognizes the need for independence on the stabilization boards. It specifically says that an employee, director or officer of a credit union, federation or another stabilization board cannot be a director of a stabilization board.

Board composition is determined by legislation

2.38 Section 229 of the *Credit Unions Act* describes the composition of the board of directors of NBCUDIC. The composition of the board of NBCUDIC is shown in Exhibit 2.2.

Lack of independence in current board composition requirements

2.39 Independence is not a requirement for appointment to the board of NBCUDIC.

2.40 NBCUDIC's board is made up of four stabilization board members and the superintendent. In their 2005 annual report, NBCUDIC states "each stabilization board exercises significant influence on the activities of the Corporation". This can create conflicts between the members of the board because:

- The stabilization boards and NBCUDIC are both part of the deposit insurance protection program and there could be conflicts about the role and level of financial involvement each should have in any specific situation requiring stabilization.
- NBCUDIC board members representing a stabilization board may be reluctant to share information with the NBCUDIC board about one of their credit unions because in their role as board members of the stabilization board they would normally protect this information.
- The Minister of Justice and Consumer Affairs appoints and employs the superintendent. Since the superintendent is not an employee of the board of NBCUDIC, it is not possible for the board to direct the actions of the superintendent. In fact, the *Credit Unions Act* states that the superintendent shall act under the instructions of the Minister. Based on our discussions with board members, conflicts have occurred in the past when the superintendent gave priority to issues significant to the Minister (employer) at the expense of issues of priority to the board of NBCUDIC.

2.41 NBCUDIC needs more independence at the board level, as well as independence from the Department.

Resources

2.42 The final component of this criterion addresses the need for adequate resources. In this section, we discuss the human resources and financial resources of NBCUDIC.

Human resources

2.43 NBCUDIC has an agreement with the Credit Unions, Cooperatives, and Trust Companies Branch of the Department of Justice and Consumer Affairs to provide the required human resources to the corporation. However, the branch itself operated without a director since November 2001 and has had numerous staff shortages. These vacancies were a source of frustration for the members of the NBCUDIC board. The branch has recently begun recruiting and filling positions.

2.44 When the board of NBCUDIC wishes to act on or pursue an issue, it must rely on the superintendent or his/her staff to move the issue forward towards resolution. We have been told that, in the past, this has created problems in getting work done, due to the superintendent's other responsibilities at the Department. When this occurs, the board is powerless because they cannot direct nor take action against the superintendent since that individual is not their employee, nor can they assign the work to another individual because NBCUDIC itself has no staff.

2.45 Furthermore, from March 2002 to April 2006, there was an acting Superintendent of Credit Unions. During that time, the statutory responsibilities were assigned to the Assistant Deputy Minister of the Justice Services Division of the Department. From our review of board minutes, the board has been very frustrated with staff shortages, and stated on one occasion that the "continual monitoring of the system is in jeopardy."

2.46 Since the only means for the board of NBCUDIC to get work done is to assign the task to a staff person at the branch, it is important that the branch maintain the human resources necessary to fulfill the needs of the corporation.

Financial resources

2.47 NBCUDIC needs access to financial resources because of its 100% guarantee of eligible deposits as well as any role it might play in assisting stabilization boards in providing financial assistance to credit unions. To assess the adequacy of NBCUDIC's financial

resources we considered possible circumstances under which NBCUDIC would be required to exercise its guarantee.

Three levels of protection to safeguard deposits

2.48 NBCUDIC's "Guide to Enhanced Deposit Insurance Protection in New Brunswick Credit Unions" describes deposit protection in New Brunswick. It states that deposits in New Brunswick credit unions are safeguarded by three levels of protection. The guide describes the protection as follows:

1. At the credit union level:

The Act requires that each credit union maintain a minimum level of equity to provide protection against potential financial losses.

2. At the level of the two stabilization boards:

Credit unions and caisses populaires have pooled resources to establish stabilization funds through their respective stabilization boards. This level of protection is unique to these financial institutions. A stabilization fund may be used to provide financial assistance to member credit unions to meet equity requirements or to provide further protection against financial losses.

Under provincial legislation, each stabilization board is administered by an eight-person board of directors, five of whom are appointed or elected by member credit unions and their federation. The other three are appointed by government.

In addition to providing financial assistance, stabilization boards carry out inspections and monitor the financial condition and standards of sound business and financial practices of all credit unions on an ongoing basis.

3. At the NBCUDIC level:

NBCUDIC guarantees the 100% repayment of all eligible deposits held at New Brunswick credit unions, including accrued interest. Deposit insurance is part of a comprehensive protection program in all New Brunswick credit unions.

Explanation of the three levels of protection

Credit union level of equity

2.49 Credit union regulation requires that credit unions maintain a level of equity equal to 5% of total assets, unless a credit union is under supervision. Prior to January 30, 1999 the level of equity required was 2% of total assets. On January 31, 1999 the required

level was increased to 3% of total assets, and finally reached its current level of 5% on January 31, 2004.¹ This 5% equity requirement is based on total assets. It does not take into consideration the risks associated with individual assets. We found evidence in the minutes of NBCUDIC board meetings of discussions about equity requirement methods used in other jurisdictions.

2.50 Exhibit 2.5 compares equity to total assets for credit unions by federation. In this exhibit, we used the figures for total assets and equity of credit unions as reported to the Credit Unions branch in audited financial statements of credit unions. The amounts related to la Caisse populaire de Shippagan have been excluded from the figures of the Brunswick Credit Union Federation because of an adjustment of \$45.7 million made to the caisse's financial statements, which negatively affected its June 1, 2003 opening retained earnings but was not allocated to prior fiscal years.

Exhibit 2.5

Equity and total assets of credit unions by federation

Year	Brunswick Credit Union Federation (excluding la Caisse populaire de Shippagan)			Fédération des caisses populaires acadiennes		
	Equity	Total Assets	Equity/ Assets	Equity	Total Assets	Equity/ Assets
2001	\$29,318,681	\$455,168,600	6.44%	\$104,034,777	\$1,646,116,896	6.32%
2002	\$33,425,659	\$526,846,173	6.34%	\$106,717,319	\$1,777,755,768	6.00%
2003	\$37,794,657	\$577,572,387	6.54%	\$113,025,312	\$1,896,361,714	5.96%
2004	\$44,617,203	\$619,396,939	7.20%	\$122,925,119	\$2,010,497,285	6.11%
2005	\$47,166,279	\$652,020,840	7.23%	\$131,853,333	\$2,048,434,534	6.44%

2.51 In la Caisse populaire de Shippagan's adjusted financial statements for 2005, total assets were \$239,478,568 with a negative equity of \$25,135,865, for a negative ratio of 10.5%.

2.52 Under section 108(2) of the *Credit Unions Act*, the Superintendent has the authority to specify that financial statements can be prepared using accounting principles that deviate from generally accepted accounting principles. In February 2002, the Superintendent granted the following exceptions to credit unions that are members of FCPA:

1. Per paragraphs 11(1) to 11(6) of New Brunswick Regulation 94-5 of the *Credit Unions Act*.

(...) I give my approval to the two following exceptions in order to establish a general allowance for the credit risk:

1. Establish a 1.5% general allowance for the credit risk, spread over a maximum of five years. The credit unions will be able to expense a minimum amount of \$0.20 per \$100 of asset per year during the five years or until the risk assets reach 1.5%, unless special authorization is obtained from the Office de stabilisation;
2. Include in the capitalization calculation the amount posted by a credit union in the general allowance for the credit risk. [Translation]

2.53 These exceptions, presumably issued under the authority of section 108(2), have been interpreted to allow the FCPA-member credit unions to remove the general provision for credit risk of 1.5% of assets from the regulatory calculation of equity. We understand that this adjustment is intended to result in a consistent method for calculating the equity to asset ratio of all credit unions. Exhibit 2.6 displays the equity to asset ratios using the adjusted figures for assets and equity as provided by l'Office (these figures are not from audited financial statements). The general provision has been added back for the purposes of this calculation. The result is higher ratios than those shown in Exhibit 2.5.

Exhibit 2.6

Equity and assets of credit unions for members of la Fédération des caisses populaires acadiennes (unaudited figures)

Fédération des caisses populaires acadiennes			
Year	Equity	Total Assets	Equity/Assets
2001	\$110,055,000	\$1,663,825,000	6.61%
2002	\$117,721,000	\$1,785,065,000	6.59%
2003	\$131,833,000	\$1,921,316,000	6.86%
2004	\$145,057,000	\$2,025,236,000	7.16%
2005	\$159,445,000	\$2,104,726,000	7.58%

2.54 Since these exceptions apply only to members of FCPA, credit unions who are members of RMA, including la Caisse populaire de Shippagan, have not been required by the Superintendent to establish a general provision. This requirement was not extended to RMA's credit unions, even though the

Superintendent stated that recording a general provision “...ensures a healthy and prudent management of the credit risk. Our department is confident that this procedure is essential, as Canadian financial institutions and the Caisses populaires Desjardins have adopted this procedure several years ago.”[Translation].

2.55 We feel that the Superintendent should review the practice of recording general provisions by all credit unions to ensure consistency and the prudent management of risk. Further, this will eliminate the need to deviate from generally accepted accounting principles for regulatory purposes.

2.56 In November 2005, the Credit Union Regulation was amended to require a credit union under supervision that would require a significant amount of stabilization funding to meet the following equity levels:

- establish a level of equity of 2% within three years;
- establish a level of equity of 3% within five years; and
- establish a level of equity of 5% within ten years.

Stabilization funds

2.57 There are two stabilization funds in New Brunswick. Credit unions pay into the fund through levies paid to their respective stabilization board. The annual amount of the levy, as determined by paragraph 15(1) of regulation 94-5, is based on a percentage of total deposits held by credit unions and amounts previously borrowed from the stabilization board. The Act requires that the levy be collected as long as the value of the fund is less than 1.5% of the total assets held by member credit unions. A stabilization fund may be used to provide financial assistance to member credit unions to meet equity requirements or to provide further protection against financial losses¹. Exhibit 2.7 compares the value of the stabilization fund to assets in member credit unions for each stabilization board. For the purposes of this exhibit, the amounts related to la Caisse populaire de Shippagan have been excluded from the figures of Risk Management Agency because of an adjustment of \$45.7 million made to the caisse’s financial statements, which negatively affected its June 1, 2003 opening retained earnings but was not allocated to prior fiscal years.

1. Per “Your Guide to Enhanced Deposit Insurance Protection in New Brunswick Credit Unions”, published by New Brunswick Credit Union Deposit Insurance Corporation.

Exhibit 2.7

Comparison of stabilization fund to assets

Year	Risk Management Agency			Office de stabilisation de la Fédération des caisses populaires acadiennes		
	Stabilization fund	Credit Union assets	Fund/ Assets	Stabilization fund	Credit Union assets	Fund/ Assets
2001	\$11,226,398	\$455,168,600	2.47%	\$43,675,255	\$1,646,116,896	2.65%
2002	\$12,605,981	\$526,846,173	2.39%	\$48,691,255	\$1,777,755,768	2.74%
2003	\$13,491,616	\$577,572,387	2.34%	\$52,747,018	\$1,896,361,714	2.78%
2004	\$13,642,916	\$619,396,939	2.20%	\$55,721,506	\$2,010,497,285	2.77%
2005	\$11,780,266	\$652,020,840	1.80%	\$58,524,683	\$2,048,434,534	2.86%

2.58 As of December 31, 2005, Risk Management Agency's fund, excluding figures for la Caisse populaire de Shippagan, was valued at \$11,780,266. This amounts to 1.80% of the assets of its member credit unions which were valued at \$652,020,840. At that same date, l'Office de stabilisation de la Fédération des caisses populaires acadiennes had a stabilization fund of \$58,524,683, 2.86% of the assets of its member credit unions.

2.59 During the course of our work, we were unsure of when, and under what circumstances, a stabilization fund could be accessed. However, the current Superintendent of Credit Unions and the current members of the NBCUDIC board are of the opinion that each stabilization fund is only available to stabilize credit unions that are members of that stabilization board.

2.60 The speed with which a stabilization fund could be accessed would depend on the investments held in the fund. We have not done any work to determine the liquidity of the holdings of the stabilization funds.

Deposit Insurance Fund

2.61 The final level of protection is provided by NBCUDIC's deposit insurance. In November 2005, through regulation 94-5, the Province increased coverage from \$100,000 to 100% of eligible deposits. Previously, regulation 94-5 stated that *the maximum amount (...) shall be an amount equal to the maximum amount insured by the Canada Deposit Insurance Corporation established under the Canada Deposit Insurance Corporation Act (Canada)*. The amended regulation now states that *the maximum amount (...) shall be an amount equal to the amount contained in the deposit accounts of the member.*"

2.62 Section 223 of the *Credit Unions Act* states that NBCUDIC shall maintain a deposit insurance fund. However, neither the Act nor the regulations stipulate the amount to be held in the fund. The stabilization boards are required to pay into the deposit insurance fund based on individual risk assessments of their member credit unions. As at December 31, 2005 NBCUDIC's deposit insurance fund was \$2.8 million - \$2.33 million of which was provided by Risk Management Agency and \$470,000 of which was provided by l'Office de stabilisation de la Fédération des caisses populaires acadiennes in relation to deposits in their member credit unions. Each year, stabilization boards provide a risk rating to the Credit Unions Branch as well as a list of the amount of deposits held by each credit union at December 31. Using a model adopted by the board, the branch determines the amount that must be maintained in the fund by each stabilization board.

2.63 The \$2,800,277 deposit insurance fund is held in two accounts in trust for NBCUDIC. As trustees of the fund, the two stabilization boards invest and manage the fund in accordance with the approved investment policies of NBCUDIC. RMA holds and invests \$2,330,613 while l'Office holds an amount of \$469,664.

2.64 There are inherent weaknesses in the application of this method. For example, despite the fact that Risk Management Agency had its largest credit union, which held 27% of the assets in the RMA system, under supervision, the contribution required from RMA actually decreased in 2005. This resulted in NBCUDIC paying a distribution of \$47,134 to RMA. This illustrates that one of the deficiencies in the current method is that it does not take into account the fact that some credit unions can represent a disproportionate amount of system deposits.

2.65 In addition, the environment in which the model was developed varies from that in which NBCUDIC currently operates. For instance, it was not adjusted when the level of deposit insurance increased from \$100,000 to the current 100% guarantee of eligible deposits. Also, the model was developed based on a system that is much larger than the New Brunswick credit union system.

2.66 Finally, the model does not consider credit unions in unusually high risk situations. As we noted in our management letter resulting from our audit of the December 31, 2005 financial statements of NBCUDIC:

It is evident that the present model does not meet the needs of the corporation as the Brunswick Credit Union Federation Stabilization Board trust fund actually decreased from the prior year, while the risk of payout remains unusually high given the state of la Caisse populaire de Shippagan Limitée. The current methodology creates a general allowance for payout of deposit insurance as opposed to a specific allowance for credit unions presenting an unusually high risk situation.

2.67 We went on to recommend that “..... the Corporation revisit the methodology used to calculate the level of net assets to be maintained in the deposit insurance fund.”

2.68 Subsequent to the completion of our fieldwork, government announced \$60 million in funding to NBCUDIC. It was announced that, of this amount, approximately \$20 million will “.....provide for certain guarantees and contingencies related to the transfer, as well as stabilization and deposit protection for the system in general”. This is a significant contribution to the deposit insurance fund that did not come from the credit union system.

Ad hoc provincial guarantee

2.69 Recently, the events surrounding the supervision of la Caisse populaire de Shippagan have illustrated that the current regulatory system of protections is not complete. These events clearly indicate that the Province has not provided NBCUDIC with a regular operational method to access funds should it ever be required to exercise its deposit guarantee. Therefore, the guarantee of deposits beyond the modest fund held by NBCUDIC is really a guarantee by the Province, a guarantee that is ad hoc in its execution. This ad hoc approach by the Province, combined with the restrictions on authority and human resources mentioned previously, makes it difficult to ensure an orderly resolution to a problem that moved through the first two levels of protection – to the frustration of the participants in the system of protection.

2.70 In their 2005 Annual Report, NBCUDIC states that in 2006 they will take the necessary steps to obtain and maintain a borrowing facility to meet unexpected claims. The annual report also states that this access “is an important element in NBCUDIC’s depositor protection mandate and provides assurance to insured depositors that NBCUDIC can meet its statutory obligations to pay claims if and when a member institution fails”. To date, the borrowing authority has not been put in place.

2.71 In practice, the ultimate protection is not provided by NBCUDIC. We believe that the final guarantor of deposits is the Province and not NBCUDIC, and the Province should acknowledge this obligation.

Summary of weaknesses

2.72 In summary, we have identified the following weaknesses in the authority, independence and resources available to NBCUDIC to fulfill its obligations:

- NBCUDIC does not have access to all sources of relevant information that would allow it to minimize its exposure to loss.
- NBCUDIC cannot take direct action to prevent or avoid a situation that would affect the safety of deposits or otherwise expose the corporation to losses.
- The composition of the board of NBCUDIC as determined by the Act means that board members may have conflicts of interest.
- NBCUDIC has no control over the filling of positions or setting the work priorities of the staff of the Superintendent's office.
- The method to determine the contribution levied by NBCUDIC on the stabilization boards for the purpose of accumulating the deposit insurance fund does not take into account all risk factors.
- The *Credit Unions Act* does not stipulate the amount to be held in the deposit insurance fund.
- The Province has not provided NBCUDIC with a regular operational method to access funds should it ever be required to exercise its deposit guarantee.
- The Province is not clear on its obligation to depositors when NBCUDIC does not possess the funds required for purposes of stabilization or deposit insurance.

Conclusion

2.73 This criterion is not met. NBCUDIC does not have adequate authority, independence or resources it needs to fulfill its obligations.

Monitoring the risks associated with unlimited deposit insurance coverage

2.74 Our next three criteria involve the corporation's need to monitor the risks associated with providing unlimited deposit insurance coverage. They address the need to identify the information required for monitoring; to obtain this information in a timely manner; and to analyze and act on the information as needed.

2.75 An informed board is an important element of good governance, and we will discuss this topic with our next three criteria. They are:

NBCUDIC should identify the information required to monitor the risks associated with unlimited deposit coverage.

NBCUDIC should obtain the required information on a timely basis.

NBCUDIC should conduct appropriate analysis of the information collected and act on the results in a timely manner.

Limited reporting to NBCUDIC

2.76 When we reviewed the *Credit Unions Act*, we noted that even though NBCUDIC is the insurer of deposits, no information flows directly to the board of NBCUDIC. As shown in Appendix A, the majority of information and reporting is made to the stabilization boards and the Superintendent of Credit Unions.

2.77 Because representatives of both stabilization boards and the superintendent, who are the parties privileged with information, come together at board meetings, we expected to find a great deal of information being exchanged at these meetings. To determine what information is being received and what information is being exchanged at meetings, we did the following:

- reviewed the minutes of board meetings held since 2001;
- reviewed a sample of documents provided to board members to determine what information board members received prior to their meetings;
- reviewed a sample of credit union files at the superintendent's office to determine whether required information was being submitted to the superintendent for the years 2002 to 2005; and
- interviewed board members to determine what information is being exchanged at the board.

2.78 When we reviewed the reports provided to board members at meetings, we found that there are reports that are provided consistently at each meeting. They are externally generated reports from the Superintendent of Credit Unions and reports from each of the stabilization boards.

2.79 For the dates we sampled, the report of the superintendent appears to be provided either verbally or in written form. In the case of the reports of the stabilization boards, the content and format of the reports were consistent. The stabilization boards provided written reports, in summary form, of the financial condition of their member credit unions as a whole. These reports include information on the adequacy of system equity, as well as a number of financial indicators, such as financial margins and delinquency. Areas of information that are not included but could be useful to the board include:

- trends in key financial indicators on a system-wide basis;
- major areas of risks or emerging risks;
- established benchmarks for financial indicators; and
- findings from inspections and examinations of credit unions, including best practices.

2.80 When we interviewed the members of the board, it was clear that some of the members do not feel they are kept informed. Specifically, they felt there were instances where needed information was not being shared for the stated reason of confidentiality. The intent of the Act may have been that information would be shared amongst the parties at the board, but this does not appear to be happening. The superintendent is the only member of the board who has access to all information because this individual attends the meetings of both stabilization boards and receives copies of all reports required in the *Credit Unions Act*.

2.81 In our review of the board minutes, we found references to certain issues being discussed; however, the level of detail recorded in the minutes did not provide enough information for us to evaluate the extent of discussions.

2.82 In addition, it became clear from discussions with board members that the lack of adequate authority, independence and resources makes it difficult for the board to identify the information needed to fulfill its purposes.

Reports and inspections

2.83 Since it is our understanding that NBCUDIC relies on the stabilization boards and the superintendent, we reviewed a sample of files at the superintendent's office to determine if the reporting and analytical requirements were being met. NBCUDIC should satisfy itself that its reliance on these parties is appropriate. We tested reports for the period of 2002 to 2005.

2.84 The reporting requirements of the *Credit Unions Act* are summarized in Exhibit 2.8, along with our findings.

Exhibit 2.8
Reporting requirements

Annual reporting requirements of the <i>Credit Unions Act</i>	Findings	Notes
Credit unions must file an information return with the superintendent showing the name and address of the credit union, date of the last annual meeting, names of directors, officers and general manager of the credit union.	<ul style="list-style-type: none"> 65% of the files we sampled had information returns for all three years tested. 35% of the files we sampled were missing 1 or 2 information returns for the three years tested. 	1
Credit unions must file a copy of their financial statements as well as the report of the auditor with the superintendent.	<ul style="list-style-type: none"> 90% of credit unions we sampled had filed copies of their financial statements and auditors report for the three years tested. 	2
Stabilization boards must file a copy of their financial statements as well as the report of the auditor with the superintendent.	<ul style="list-style-type: none"> We found all financial statements and auditors report as required for the three years tested. 	
Stabilization boards must file a report of their inspection and examination of the business and affairs of each member credit union with the superintendent.	<ul style="list-style-type: none"> All credit unions we sampled had been inspected at least once during the three years tested. A report of the inspection was filed. 	

Notes:

- 1) La Caisse Populaire de Shippagan did not hold an annual general meeting between the dates of September 29, 2003 and March 26, 2007.
- 2) We noted that all caisses populaires who are members of l'Office de stabilisation de la Fédération des caisses populaires acadiennes (OSFCPA) had the same year end, while for the nine credit unions of Risk Management Agency (RMA) we tested, we found eight different year ends.

2.85 In addition to reporting requirements, the Act requires certain inspections to take place. Exhibit 2.9 summarizes the requirements and our findings.

Exhibit 2.9
Inspection requirements

Inspection requirements of the <i>Credit Unions Act</i>	Findings	Notes
Superintendent must make annual (or at such other intervals as considered necessary) inspections and examinations of the business and affairs of each federation and stabilization board.	<ul style="list-style-type: none"> • We found that there has not been an inspection of a stabilization board or a federation by the superintendent since 1999. 	1
Stabilization boards must make an inspection and examination of the business and affairs of each of its member credit unions at least every 18 months.	<ul style="list-style-type: none"> • All credit unions we sampled had been inspected at least once during the three-year period tested. • For 10% of the credit unions sampled, the interval between inspections exceeded 18 months. 	2 3 4

Notes:

- 1) This is particularly significant given the reliance placed on the stabilization boards by the system itself (as regulators) and by other parties such as the Superintendent of Credit Unions and NBCUDIC.
- 2) Credit union inspections, required every 18 months, are performed by either RMA (for member credit unions) or Services Unis de Vérification et d'Inspection (SUVI) (for members of OSFCPA). We did note some differences between the inspections reports. Those reports provided by SUVI included a rating similar to that used for calculating the deposit insurance fund. This rating is based on a scale of 1 (unacceptable) to 5 (very good). In addition, each report included a comparison to the rating the credit union had received during the previous inspection, as well as a benchmark rate for the group. The reports provided by RMA included a rating only in those reports for 2005 (prior reports included no rating). Their rating was based on 3 levels: satisfactory, needs improvement or unacceptable. No comparative information on ratings was provided in the report. Per discussions with branch staff, RMA provides the numerical 1-5 rating at a later date.
- 3) Only 25% of the files we tested had copies of the credit union's response to the inspection reports; the majority of files tested were missing one or more of the responses.
- 4) The findings of these inspections and examinations are not reported to the board of NBCUDIC.

Timeliness of information

2.86 Since the only opportunity for the NBCUDIC board to exchange information is during board meetings, we reviewed the number of board meetings the corporation has had in recent years. In 2003, the directors of the board took the extraordinary measure of sending a letter to the chair (the superintendent) to request that a meeting take place. The by-laws of the corporation were subsequently amended to require quarterly meetings of the board. Exhibit 2.10 shows the number of meetings held in recent years. The frequency of meetings has significantly increased since 2001.

*Exhibit 2.10**Number of board meetings (including conference calls) held between 2001 and 2005*

Year	Number of regular meetings	Number of conference calls	Average number of months between meetings
2001	2	0	6
2002	2	0	6
2003	3	2	2.4
2004	4	3	1.7
2005	5	1	2

No analysis of information is conducted by the board itself

2.87 Based on our findings, no analysis is conducted on the information presented at the board meetings. Although we expected to find some analysis prepared in relation to the increase in deposit insurance coverage, we became aware that the NBCUDIC board did not take part in the decision to increase deposit insurance coverage. Though this major decision to increase deposit insurance from \$100,000 to an unlimited amount occurred in 2005, the value of NBCUDIC's deposit insurance fund only increased by \$37,222. This serves as another indication that the true commitment to guarantee deposits in credit unions lies with government.

Conclusion

2.88 These three criteria are not met.

2.89 The board has identified some of the information it feels is needed to fulfill its obligations, and is receiving this information. However, there is a need to share an increased amount of information within the board to ensure directors are in an informed position. Because the board does not have adequate authority and resources, it is difficult for the board to identify further information needed. Even if the board could identify its information needs, it is unclear whether the information could be obtained.

Accountability to stakeholders

2.90 Our final criterion looks at NBCUDIC's annual accountability reporting:

NBCUDIC should prepare an annual accountability report that is available to their stakeholders and to the public.

2.91 NBCUDIC is accountable to both the Province (Department of Justice and Consumer Affairs) and the public (members of credit unions in New Brunswick). During our audit, we found that

NBCUDIC communicates with its stakeholders in a number of ways:

- annual reports;
- credit union brochure; and
- website.

Annual report

Compliance with annual report policy

2.92 The Province's policy on annual reports states that the objective of an annual report is to be the major accountability document for the Legislative Assembly and the general public, serving as the key link between the objectives and plans of an organization and the results obtained.

2.93 The policy identifies the requirements for annual reports:

- The annual report should include a clear account of goals, objectives and performance indicators.
- The report should show the extent to which a program continues to be relevant.
- The report should show how well the organization performed in achieving its plans.
- The report should show how well a program was accepted by its client groups.
- Actual and budget financial information in summary form and narrative explaining major variances as well as other aspects of financial performance are to be included in all annual reports.
- Annual reports should be written in clear and simple language, avoiding technical terms and phrases as much as possible.

2.94 We tested NBCUDIC's 2005 annual report against the requirements of the annual report policy. Our findings are summarized in Exhibit 2.11.

2.95 Although the corporation states its purpose, we found that there were no objectives, goals or performance indicators in the annual report. Since there are no objectives or goals set for NBCUDIC, there is no discussion of achievement of plans in its annual report. Also missing is a discussion of client acceptance of the deposit insurance program. NBCUDIC is not funded by

government; therefore there is no budget allocation. The corporation is funded by the stabilization boards based on its costs, which are mainly administrative expenses. The annual report does include financial information in their financial statements and summary information on assets of the corporation with a comparison to previous year. The annual report should also include information on other aspects of financial performance. Although some information is provided, additional information should have been included on the risks and implications of the increased level of deposit insurance. In addition, there was no discussion of the situation with la Caisse populaire de Shippagan other than a note to the financial statements.

Exhibit 2.11

Compliance with Annual Report Policy

Requirement	Met?	
	Yes	No
Clear account of goals, objectives and performance indicators		X
Extent of program relevance	X	
Achievement of plans		X
Acceptance by client groups		X
Actual and budget information in summary form	X	
Explanation of major financial variances as well as other aspects of financial performance		X
Clear and simple language	X	

Contradictions in the annual report

2.96 The risk faced by NBCUDIC is not fully reported in the annual report of NBCUDIC. In its 2005 report, we found contradictions between the annual report and the financial statements.

2.97 The annual report states that deposits are well protected, yet note 4 in NBCUDIC's financial statements indicates that funds required to stabilize a large credit union in the province exceed the assets of the stabilization board and the assets of NBCUDIC. It goes on to state that the Province may make a loan to NBCUDIC; however, access to funding from the Province is not automatic.

2.98 In our opinion, the ultimate responsibility for deposit protection rests with the Province. Specifically, the 100% guarantee is a contingency and should be disclosed in the Province's financial statements. Although the outcome cannot be determined, should there be significant financial difficulty in a credit union requiring stabilization or guarantee of deposits, NBCUDIC lacks the

resources and authority to fulfill its obligation. In other jurisdictions such as Alberta and Prince Edward Island, governments have declared that they will ensure the obligations of the deposit insurance organization will be fulfilled in the event of a loss.

Conclusion

2.99 This criterion is not met. Improvements to the annual report are needed for NBCUDIC to be adequately accountable to their stakeholders and the public.

Recommendations

2.100 In our opinion, NBCUDIC does not have the adequate authority, independence or resources it needs to fulfill its obligations. **We therefore recommend the Province either give NBCUDIC the authority, independence and resources it needs to fulfill its mandate, or consider dissolving NBCUDIC.**

2.101 We recommend the Province disclose its obligation for deposit insurance in the notes to the Province's financial statements.

2.102 We recommend the Province amend the *Credit Unions Act* to clearly state the Province's obligation for deposit insurance.

2.103 We recommend the Superintendent review the practice of recording general provisions against accounts receivable by all credit unions to ensure consistency and to eliminate the need to make adjustments for regulatory purposes.

2.104 If the Province decides to strengthen the authority, independence and resources of NBCUDIC, we have the following recommendations.

2.105 We recommend the Department of Justice and Consumer Affairs amend the *Credit Unions Act* to clarify NBCUDIC's ability to access information about credit unions and stabilization boards.

2.106 We recommend the Province review the composition of the NBCUDIC board and make changes to the *Credit Unions Act* to ensure the board can act independently.

2.107 We recommend NBCUDIC and the Credit Unions, Cooperatives, and Trust Companies branch of the Department amend their memorandum of understanding to include specific operating parameters such as length of time to fill positions and establishing work priorities.

2.108 We recommend that NBCUDIC and the Department establish a minimum value for the Deposit Insurance Fund. If the existing balance is determined to be insufficient, a funding plan with appropriate levies should be put in place.

2.109 As we stated in our management letter resulting from our financial audit of NBCUDIC, we recommend that the Corporation revisit the methodology used to calculate the level of net assets to be maintained in the deposit insurance fund.

2.110 We recommend the Province provide NBCUDIC with a specific process to access funds in order for NBCUDIC to fulfill its purposes as stated in the Act.

2.111 Because of NBCUDIC's reliance on the work of the superintendent, NBCUDIC should request the superintendent to carry out more frequent inspections of stabilization boards as required by the *Credit Unions Act*.

2.112 We recommend NBCUDIC review the content of its annual report to comply with government's annual report policy.

NBCUDIC Board response

Authority
(paragraphs 2.29 to 2.34)

2.113 The Board of NBCUDIC provided the following response to our report and recommendations:

The Board supports the conclusion that the Corporation has limited authority to minimize the Corporation's exposure to loss. The Board has overseen the risk-mitigation practices of both the Superintendent of Credit Unions and the stabilization boards by receiving reports from these regulators at regular meetings with the objective of identifying significant concerns that would expose the Corporation to loss. At the same time, the Board is of the opinion that it is not the intention of the legislation for the Corporation to duplicate work performed by the Office of the Superintendent of Credit Unions, stabilization boards, and federations.

The Chair of the Board, the Superintendent, has access to all the information held by the stabilization boards, federations, and credit unions including the results of the inspections and examinations of each of these bodies. The Board believes it is the intent of the legislation for the Superintendent to provide the Corporation with all relevant information required to carry out its mandate. As a result of the shortage of resources in the Office of the

Superintendent, as pointed out in the Auditor General's Report, this did not always occur.

Furthermore, the Board's constitution provides for two Board directors appointed by each stabilization board who have access to all the information in their respective systems. Therefore, although not specifically provided for in the legislation, the Board has access to all pertinent information to carry out its mandate. Regardless, the Board recognizes the need for more formal information sharing and in 2006 took initial steps in developing information sharing agreements.

Credit union level of equity
(Exhibit 2.5)

The Board is of the opinion Exhibit 2.5 by itself and as currently presented without information concerning the Caisse populaire de Shippagan leads the reader to an erroneous conclusion with respect to the system's equity position.

Although the Auditor General's Report provides additional information on the Caisse populaire de Shippagan in the surrounding text, the Board believes the true picture of the relative financial situation of each system is more accurately reflected by incorporating the financial information of the Caisse populaire de Shippagan in Exhibit 2.5 as shown in the Restated Exhibit 2.5 below. In this restated exhibit BCUFL figures include reported and restated audited financial information for this Caisse for all the years presented. A significant prior period adjustment of \$45.7 million is shown to negatively affect BCUFL's 2003 equity.

Restated Exhibit 2.5
Equity and total assets of credit unions by federation
(Including the Caisse populaire de Shippagan)

Year	Brunswick Credit Union Federation Limited (BCUFL)			Fédération des caisses populaires acadiennes (FCPA)		
	Equity	Total Assets	Equity/Assets	Equity	Total Assets	Equity/Assets
2001	\$51,156,169	\$697,265,024	7.34%	\$104,034,777	\$1,646,116,896	6.32%
2002	\$56,438,489	\$804,186,553	7.02%	\$106,717,319	\$1,777,755,768	6.00%
2003	\$16,560,393	\$823,346,042	2.01%	\$113,025,312	\$1,896,361,714	5.96%
2004	\$18,981,367	\$888,987,479	2.14%	\$122,925,119	\$2,010,497,285	6.11%
2005	\$21,077,412	\$891,499,408	2.36%	\$131,853,333	\$2,048,434,534	6.43%

It is the Board's opinion the above Restated Exhibit 2.5 reveals the impact of the significant losses by the Caisse populaire de Shippagan on BCUFL's system and provides an accurate comparative between the two systems.

Stabilization funds
(Exhibit 2.7)

The Board is of the opinion that Exhibit 2.7 by itself and as currently presented without the information concerning the Caisse populaire de Shippagan leads the reader to an erroneous conclusion with respect to the sufficiency of the stabilization funds of the respective systems.

Although the Auditor General's Report provides additional information on the Caisse populaire de Shippagan in the surrounding text, the Board believes the true picture of the relative financial strength of each of the stabilization funds is more accurately reflected by incorporating the financial information of the Caisse populaire de Shippagan into Exhibit 2.7 as shown in the Restated Exhibit 2.7 below.

Restated Exhibit 2.7
Comparison of stabilization fund to assets
(Including the Caisse populaire de Shippagan)

Year	Brunswick Credit Union Federation Stabilization Board Limited (RMA)			Office de stabilisation de la Fédération des caisses populaires acadiennes (Office)		
	Stabilization Fund	Total Credit Union Assets	Fund/ Assets	Stabilization Fund	Total Assets	Fund/ Assets
2001	\$11,226,398	\$697,265,024	1.61%	\$43,675,255	\$1,646,116,896	2.65%
2002	\$12,605,981	\$804,186,553	1.57%	\$48,691,255	\$1,777,755,768	2.74%
2003	\$13,491,616	\$823,346,042	1.64%	\$52,747,018	\$1,896,361,714	2.78%
2004	\$13,642,916	\$888,987,479	1.54%	\$55,721,506	\$2,010,497,285	2.77%
2005	\$11,780,266	\$891,499,408	1.32%*	\$58,524,683	\$2,048,434,534	2.86%

*The 2005 ratio is 1.16% when adjusted for approximately \$1.4 million held by RMA as loans and investments in member credit unions.

Further, the Board believes that the Auditor General's Report should note the value of the RMA stabilization fund as of December 31, 2005 is subject to a significant contingent liability related to RMA's legislated requirement to provide financial assistance to the Caisse populaire de Shippagan in future years.

Provisions against accounts receivable (paragraph 2.103)	<i>The Board is of the opinion that the practice of using a general provision helps to ensure the healthy and prudent management of credit risk in the credit union system. The Board supports the use of a general provision by caisses populaires and would like to see credit unions adopt this practice.</i>
Credit union level of equity (paragraphs 2.49 to 2.56)	<i>The Board believes this section of the audit report should outline the conditions referred to in subsection 11(7) of the Credit Unions Act. Subsection 11(7) permits certain credit unions under supervision to take up to ten years to attain a five percent regulatory equity level under the circumstances whereby a stabilization board would otherwise be required to provide a credit union with financial assistance that is more than twenty-five per cent of the total amount held in its stabilization fund and is greater than ten million dollars.</i>
Minimum value for the Deposit Insurance Fund (paragraph 2.108)	<i>The Board believes this recommendation should go further to require an amendment to be made to the legislation that requires stabilization boards to fully utilize their respective stabilization funds prior to making any request to the Corporation for financial assistance.</i>
Inspections of stabilization boards (paragraph 2.111)	<i>The Board supports the recommendation which states the Corporation should request the Superintendent to carry out more frequent inspections of the stabilization boards. The Board believes this recommendation should be made stronger to require an inspection or examination of the respective stabilization boards at least every eighteen months and that this requirement be included in any amendments to the legislation. Currently, an eighteen month inspection interval is seen in the Credit Unions Act under which stabilization boards are required to perform inspections and examinations of member credit unions at least every eighteen months.</i>
Lack of independence in current board composition (paragraphs 2.39 to 2.41)	<i>The Auditor General's Report fails to identify what conflicts it perceives to exist as a result of the Board's composition. In the Board's opinion, the only potential foreseeable conflict lies in the sequence of funds to be used in the event a credit union has financial difficulties. The Board feels this potential conflict could be remedied if the legislation were amended to require the use of the entire</i>

stabilization fund of the system whose member credit union requires financial assistance prior to any request by that stabilization board for financial assistance from the Corporation or for the use of any of the deposit insurance funds of the Corporation.

The Board, therefore, questions the concerns regarding lack of independence of the Corporation. It is also relevant to note that the current legislation requires the Minister to appoint three (3) of the five (5) directors of the Board, including the Superintendent.

Overall comments

The Board believes the audit report attempted, in its scope, to focus on the role of the Corporation which forms one component of the credit union system of regulation. Rather, the Board is of the opinion that it would be more informative for the Auditor General to review the major components of the system of credit union regulation which also includes the stabilization boards, federations and the Office of the Superintendent. As a result, the Board feels the audit report is not as relevant to the public as it could have been.

The Board is of the opinion the current system of regulation has many controls which are important to the effective functioning of the credit union system. Recent events have confirmed that certain controls within this system failed. The Board is of the opinion that prior to any amendments to the Credit Unions Act a review should be undertaken to determine why these controls did not function as intended.

Finally, the Board believes the audit report references a number of issues that fall outside the Corporation's mandate and that a number of the Auditor General's recommendations should be made directly to the Office of the Superintendent in a separate report. As such, comments have not been provided by the Board on parts of the audit report which, in its opinion, fall outside its mandate.

Further to the Auditor General's recommendations the Board believes the Credit Unions Act should be amended to provide for a stabilization board to be automatically

placed under supervision in the event its capitalization level falls under a specified minimum amount after making adjustments for the shortfalls in the equity of member credit unions.

Departmental response

2.114 The Department of Justice and Consumer Affairs provided the following comments on our report and recommendations:

The Department understands that the Board of NBCUDIC has responded to areas of your report and recommendations that fall within its mandate. The Department has reviewed the draft response of NBCUDIC and agrees with the comments contained therein.

The Department shares the concerns expressed by the Board of NBCUDIC that the report does not look at the system of credit union regulation in New Brunswick as a whole, but only one part of the entire system which includes the stabilization boards, federations and the Office of the Superintendent. The Department is of the view that there is a need to review all elements of the system of regulation of credit unions in New Brunswick, including issues related to the mandates, structures and board appointment processes of NBCUDIC, the stabilization boards and the federations and the role and responsibilities of the Office of the Superintendent.

Government has indicated concern with the unlimited deposit insurance protection currently in place. The level and manner of deposit insurance protection is being reviewed by the Department as part of a comprehensive examination of the legislation and regulations governing the credit union system in New Brunswick. A legislative and regulatory proposal will be developed for Government's consideration in the coming months.

This legislative and regulatory proposal will address many of the areas of concern highlighted in your report, in the context of the credit union regulatory system as a whole. The Department will give full consideration and take into account the comments and recommendations in your report and any subsequent reports of the Auditor General related to the credit union system, as well as advice and recommendations from other sources, as we develop this proposal.

Appendix A – Summary of authority and reporting requirements in the Credit Unions Act

