



REGULATORY GUIDANCE FOR CREDIT UNIONS ST. KITTS AND NEVIS

THE TREATMENT OF THE LOAN MORATORIA AND OTHER MEASURES TO SUPPORT THE RESILIENCE OF CREDIT UNIONS IN RESPONSE TO THE CHALLENGES POSED BY THE COVID-19 PANDEMIC

1. Introduction

The Financial Services Regulatory Commission (FSRC) recognizes the need to build resilience of credit unions and improve stability of the Credit Union Sector in response to the socio-economic challenges posed and the emerging financial impact of the COVID-19 pandemic. The need for credit unions to sustain strong capital and liquidity buffers, develop effective risk management systems and revise crisis management and strategic plans for short-term, medium-term and long-term intervals, are all mitigating strategies to weather the emerging financial impact on their operations.

The loan moratoria granted to credit union members, to alleviate the impact of the COVID-19 pandemic, is scheduled to end on 31 December 2021. While there is high uncertainty surrounding the path of the COVID-19 pandemic, this Guidance seek to outline the treatment of the loan moratoria portfolio and several near-term regulatory mandates and flexibilities of key financial indicators.

The contents of this Guidance apply to all registered credit unions pursuant to Sections 125, 198, 200 and 201 of the Co-operatives Societies Act, Cap. 21.04 (hereafter referred to as ‘the Act’).

2. Treatment of COVID-19 Pandemic Related Deferred Loan Payments

In March 2020, registered credit unions implemented an “Ease the Burden” programme for credit union members as a holistic approach to help the general membership address the economic and social consequences from the COVID-19 pandemic. The Program included moratorium on loan payments with the aim of supporting the short-term operational and liquidity challenges faced by the general membership. The treatment of the loan moratoria portfolio and the classification of these loans prior to and subsequent to 31 December 2021 are detailed below.

The following provisions are applicable prior to 31 December 2021:

1. In the current regulatory framework, the loan moratoria suspend, postpone or reduce the payments of principal and/or interest of a loan for a member who is experiencing or is likely to experience financial difficulty in repaying a loan(s) as a result of circumstances brought about by the COVID-19 pandemic. Subsequent to an assessment of the repayment capacity of the member, the credit union may grant the moratorium on loan payments specific to the financial circumstances of the member and the loan agreement. These loans have been deemed “performing loans”.
2. The loan schedule of payment for loans classified under the loan moratoria may result in an extended duration of the loan or in increased payments after the loan moratoria end.
3. The moratorium on loan payments does not apply to new loans granted after the implementation of the loan moratoria as it has been established that the loan moratoria address the performing loans in existence at the time of the COVID-19 pandemic and is not intended to be applied to new credit granted after the outbreak in 2020. The terms of new loans granted after the implementation of the moratorium shall therefore comply with the normal credit policies of the credit union and shall be based on the assessment of the creditworthiness of the member.
4. Credit unions shall:
 - i. Collect and maintain data on the loan moratoria including:
 - ✓ the number and value of the loan moratoria requests received and the loan moratoria granted;
 - ✓ the number and value of the loan moratoria that have been restructured; and
 - ✓ the number and value of the loans that have been removed from the loan moratoria portfolio and have been reclassified under normal loan terms. The data should be arranged by date, loan categories and by sector and is required to be submitted to the Registrar of Credit Unions on a quarterly basis.
 - ii. Complete a detailed valuation of the quality of the loan moratoria portfolio and segment loans by probability of recovery.
 - iii. Intensify recovery actions such as restructuring and other collection procedures in accordance with the credit unions loan and collections policies and procedures.

- iv. Assess the credit quality of loans benefiting from the moratorium and identify those loans with a high probability of default.

All credit unions are required to be guided by the following provisions subsequent to 31 December 2021:

1. Collections and recovery procedures should continue to be prioritized and intensified and should be accompanied by financial counseling for the general membership.
2. On or before 31 January 2022, the Board of Directors (BOD) and Management of the respective credit unions are required to develop and submit an Action Plan to the Registrar of Credit Unions outlining its approach to address the credit union's delinquency position, provisioning strategy and increased credit risk exposure as at 31 December 2021.

3. Application of Accounting Standards

IFRS 9

Effective 1 January 2018, the IFRS 9 established how credit unions should classify and measure financial assets and financial liabilities including the recognition of impairment. Under the expected credit loss (ECL) impairment framework outlined in IFRS 9, credit unions are required to recognize ECLs at all times, taking into account past events, current conditions and forecast information, and to update the amount of ECLs recognized at each reporting date to reflect changes in an asset's credit risk. It is a more forward-looking approach than its predecessor "incurred credit loss" and will result in timely recognition of credit losses.

Pursuant to Section 201 of the Act, credit unions are permitted to suspend the requirements under the ECL methodology for estimating allowances for credit losses for loan modifications related to the COVID-19 pandemic that would otherwise be categorized as impaired, under-performing or non-performing for provisioning purposes.

Any such suspension shall be applicable for the term of the loan moratoria, but solely with respect to any loan modification, including a loan deferral arrangement, an interest rate modification, a repayment plan, and any other similar arrangement that defers or delays the payment of the loan principal and/or interest, that occurs during the applicable period, for a loan that was not more than 30 days past due as of 31 March 2020. This suspension shall not apply to any adverse impact on the credit obligation of a member that is not related to the COVID-19 pandemic.

Credit unions are, however, encouraged to ensure that proper documentation and support is obtained and maintained on file to validate collateral values that have been and would be used in determining IFRS 9 provisioning and the ECL computation associated with these loans.

This provision shall be repealed on 31 December 2021.

PEARLS Provisioning Standards

Credit Union operations are also guided by the PEARLS Prudential Standards, which require loan loss provisions at the rate of thirty-five per cent (35%) on loan balances less than 12 months aged and one hundred per cent (100%) on loan balances more than 12 months aged.

In accordance with Section 201 of the Act and given that the moratorium on loan payments define these loans as ‘performing’, the provisioning of loan losses under the PEARLS standards for the loan moratoria portfolio shall be relaxed.

The relaxation of the PEARLS loan loss provision shall be discontinued on 31 December 2021.

4. Institutional Capital and Statutory Reserves

Section 125(6) of the Act states that if a credit union’s institutional capital does not exceed 10% of total assets at the end of a financial year, a transfer of a minimum of 25% of net income to the statutory reserve is required however, the BOD and Management are encouraged to transfer a greater portion of net income to statutory reserve to complement capital preservation.

The statutory reserve capital, a component of institutional capital, is expected to act as a buffer against exogenous shocks. Pursuant to Section 125(2) of the Act, the statutory reserves, subject to the approval of the Registrar of Credit Unions, may be used by the credit union to address unforeseen losses, any unexpected shortfall in liquidity and to avoid external borrowings. The use of the statutory reserve capital will be considered on a case-by-case basis.

5. Liquidity and Cash Flow Management

The need to effectively manage liquidity resources is necessary to normalize the credit unions’ operations during the COVID-19 pandemic to provide long-term operational stability.

- Cash management and liquidity plans should therefore be closely monitored and updated.

- Credit unions should curtail or eliminate **non-essential** spending during the pandemic. Projects and capital expenditures should be reviewed and re-evaluated by identifying those that could be delayed or cancelled by considering the merits of each capital project including the availability of funding, whether the projects support continued operations or address short to medium-term safety risks.

- It is necessary that credit unions take aggressive actions to improve liquidity by restructuring and supporting long-term cash preservation. Credit unions are encouraged to:
 - i. Determine the possibility of reduction of cash inflows based on the effects of changes to the performing loan portfolio and the credit growth;
 - ii. Monitor growth in savings deposit and perform a sector-specific assessment to identify the source of the increase and determine whether the growth in deposits is sustainable for operational use; and
 - iii. Assess current investments and make a determination if profitability can be sustained and whether increases in investments should be made.

Please be reminded that cash flow management is essential to balancing inflows and outflows of cash and minimizing liquidity stress in the credit union.

6. Implementation

This Regulatory Guidance shall be adopted with immediate effect.

The Regulatory Guidance may be revised depending on the unfolding of events associated with the COVID-19 pandemic.



ST. KITTS BRANCH
Registrar of Credit Unions
Financial Services Regulatory Commission
27 September 2021