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Differential Premium System Consultation

Consultation Summary Report

BCFSA 

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Introduction

The *Financial Institutions Act* (“FIA”) authorizes Credit Union Deposit Insurance Corporation of BC (“CUDIC”) to guarantee the deposits and non-equity shares (issued prior to January 1, 2020) of credit unions in British Columbia. This guarantee provides confidence for credit union depositors knowing that they are protected by CUDIC in the event of a credit union failure.

On June 29, 2021, BC Financial Services Authority (“BCFSA”) released an advisory to announce the implementation of the new premium assessment methodology, which will replace the risk-based assessment methodology on April 1, 2023. Within that advisory, BCFSA stated that it will work with credit unions to review and communicate the ranges to be used in the determination of the 2023 CUDIC premium assessment scores for credit unions.

From November 14 to December 14, 2022, BCFSA held a consultation on the proposed CUDIC Differential Premium System (“DPS”) ranges to be implemented for the 2023 premium assessment process.

Consultation Process Overview

On November 14, 2022, BCFSA opened a consultation on the proposed CUDIC Differential Premium System (“DPS”) ranges to be implemented for the 2023 premium assessment process. The formal consultation period extended through to December 14, 2022, though BCFSA allowed responses to be received up until January 14, 2023. BCFSA hosted a virtual information session on November 30, 2022, and participated in a working group meeting on January 10, 2023, organized by the Canadian Credit Union Association (“CCUA”).

This report summarizes the consultation and working group feedback received from B.C. credit unions and includes BCFSA’s responses and next steps.

BCFSA values the feedback it received during the consultation period and thanks the B.C. credit unions who actively participated in the working group and participated in the dialogue throughout the consultation process.

For information on the DPS ranges, see the [consultation page](#) on BCFSA’s website.

Summary of Feedback

The feedback received from B.C. credit unions and BCFSA's responses are provided in the following table.

	Feedback Received (Summarized)	Response
1	Capital Adequacy Ratio (C1), Leverage Ratio (C2), and the Liquidity Coverage Ratio (L1) have changed since the previous publication in 2021 of the DPS Calculation Manual but should be fixed scoring. Since these are fixed ranges, why are they changing?	Capital Adequacy Ratio, Leverage Ratio, and the Liquidity Coverage Ratio are fixed ranges and will not be changed unless there is a significant change in the economic environment and/or a change in the regulatory requirement. The proposed changes are to the increment of points within each range to ensure that differentiation among credit unions is maximized.
2	Asset Quality metrics (A1 and A2), Non-Performing Loans to Total Loans, and Commercial Loans Rated 4/5 to Total Loans should not have an upper bound of zero as credit unions are not in the business of taking zero risk. Please provide further rationale behind the range determination. Further, for Commercial Loans Rated 4/5 to Total Loans, is zero per cent an appropriate starting point as the upper range is skewed by the number of credit unions with limit exposure to commercial lending?	<p>Asset Quality metrics (A1 and A2), Non-Performing Loans to Total Loans, and Commercial Loans Rated 4/5 to Total Loans ranges were determined to allow for the greatest differentiation among the credit unions. For Non-Performing Loans to Total Loans, a zero upper bound was set to reflect the risk mitigating actions taken by credit unions in the form of credit allowances (i.e., provisioning) for non-performing loans. These credit allowances resulted in negative values within this metric range, supporting an upper bound of zero. Furthermore, the analysis performed by BCFSA supports the zero to 0.84 per cent range, allowing for the greater differentiation among credit unions.</p> <p>In the case of Commercial Loans Rated 4/5 to Total Loans, BCFSA analyzed credit union exposure and found that most credit unions have some commercial loan exposure, thereby, limiting the skewness of the range. Furthermore, credit unions with similar commercial loan</p>

		<p>exposures display different Commercial Loans Rated 4/5 ratios.</p> <p>Notwithstanding the previous, the calculation of these metrics was reviewed with the following findings:</p> <ul style="list-style-type: none"> • The calculation of the denominator was updated from Total Loans (deducting credit allowances) to Gross Total Loans as prescribed in the DPS Manual. This change was necessary as the Reporting Instructions: Financial and Statistical Return Total Loans figure includes the deduction of credit allowances and accrued interest. • With the change in the denominator, the ranges for the A1 and A2 were updated. The scoring range to score four points for each metric has been widened. <p>Considering these adjustments, the DPS ranges for these metrics included minor changes</p>
3	<p>The Net Operating Income metric (E1) has changed since the 2021 publication of the DPS Calculation Manual and has increased comparatively to the variable assessment range used previously. What was the rationale behind this change?</p>	<p>The change to the formula used to determine the Net Operating Income within the DPS versus the previous variable assessment methodology was discussed and agreed upon during the consultation process from 2016 to 2019. The ranges within each methodology should not be compared. The DPS range for the updated Net Operating Income metric was determined through statistical analysis based on a five-year historical data.</p>
4	<p>Should Securitizations to Total Deposits (L2) and Agent Deposits to Total Deposits (L3) ranges be increased to allow for the diversification on funding?</p>	<p>BCFSA increased the upper bound for both metrics from zero. Increasing the upper bound further would cause no differentiation within these two metrics. Furthermore, BCFSA has removed the Agent Deposits greater than 12 months from the credit union exposure to ensure that the metric is capturing the risk appropriately. The proposed range is supported by the statistics observed.</p>

Consultation Outcomes and Next Steps

BCFSA values the feedback received and thanks the B.C. credit unions that actively participated in the dialogue throughout the consultation process and working group. The DPS methodology is to be implemented on April 1, 2023..



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