Banc Ceannais na hÉireann
Central Bank of Ireland
Eurosystem

T +353 (0)1 224 6000

Bosca PO 559
Baile Átha Cliath 1

PO Box 559
Dublin 1

www.centralbank.ie

8 June 2020

RE: COVID-19 – Payment Breaks in Credit Unions

Dear Chair,

First and foremost, the Registry team and I hope you, your colleagues, families and loved ones all remain safe and well throughout this difficult time.

As communicated to all credit unions in our COVID-19 related circular issued on 31 March 2020, we recognise the key role that credit unions play in the delivery of financial services in local communities across Ireland, the need for which is heightened at this time.

As the crisis initially unfolded, individual credit unions took the decision to provide loan forbearance arrangements to their members affected by COVID-19. The Central Bank of Ireland (Central Bank) is focused on ensuring that the interests of borrowers affected by COVID-19 are appropriately protected. We note that credit unions have and continue to engage directly with individual member borrowers impacted by COVID-19. The Central Bank is working with lenders, including credit unions, to ensure that COVID-19 related forbearance measures operate in borrowers' best interests.

As you know we have engaged directly with credit unions over the recent weeks to gather specific information in relation to member requests for modification of loan repayments in the context of COVID-19. I would like to take this opportunity to thank you for engaging constructively with Registry on this important work.

More specifically, on requests to credit unions from their members for loan forbearance, our engagement with individual credit unions indicates that, to date, the overall level of such requests by number and by value, is not substantial in the context of total credit union sector lending. Overall, the reported level of forbearance requests represent c.5% of gross loans outstanding. The nature of loan forbearance reported by individual credit unions to date, indicates a variety of different approaches / practices being adopted. These include in the case of short term loans arrangements covering interest only, part capital and interest reductions and savings to loan transfers. For house loans, the majority of arrangements relate to full moratorium / payment break requests. In addition, some credit unions have advised that they are providing new credit facilities to members affected by COVID-19.

Set against the evolving economic background, we set out further details below on this key area for credit unions, including from both a member protection and prudential perspective, together with an articulation of our related supervisory expectations which are reflective of the tailored and proportionate supervisory approach for credit unions.

The Central Bank's expectations regarding payment breaks

The Central Bank expects that:

1. ***Credit unions act in a way that protects the best interests of borrowers and in line with the relevant regulatory requirements.***

   COVID-19 clearly presents challenges for borrowers which for some will lead to requests for flexibility from lenders including credit unions. In terms of the overall approach in dealing with borrowers in such circumstances, the Central Bank expects regulated firms to take a consumer-focused approach, and act in their customers' best interests in the current environment.

   With regard to any decisions by individual credit unions to provide additional credit or temporary payment flexibility to their members affected by COVID-19, as set out in our circular of 31 March 2020, we expect individual boards to retain ownership for credit underwriting assessment and decision making.

2. ***Credit unions give appropriate support to borrowers whose incomes and affordability have been affected by COVID-19.***

   We recognise credit unions will need to take action to support members affected by COVID-19. It is fundamentally important that a prudent approach is maintained to all aspects of a credit unions' business, including lending, investments, liquidity and capital, as it will best serve the longer term interests of credit unions and their members.

3. ***Payment breaks should be a generally available option to affected borrowers, including those borrowers' already in financial distress. Credit unions should ensure approaches are consistent with existing arrears strategies and operations.***

   Our supervisory expectations when considering such requests are that individual credit union boards should take account of the relevant regulatory framework requirements, their own stated credit risk appetite and the financial position of their credit union.

   In our supervisory engagements, we will expect credit unions that have granted their members credit forbearance related to COVID-19, to have conducted effective credit assessments and to have clearly documented their decisions and any related matters. In this way, it will be clear where a credit union has operated in line with its stated risk appetite, and to the extent that it has not, the rationale for this will be clearly recorded and available for review. Credit union board ownership is central to this process.

4. ***Credit unions are operationally ready and prepared to engage with borrowers during, or at expiry of, the payment break in order to identify whether or not the borrower requires further support, and if so, to consider appropriate and sustainable solutions, as soon as possible.***

   Ongoing engagement with distressed borrowers is important, to ensure that the most appropriate and sustainable solutions are put in place for them tailored to their circumstances.

5. ***Credit unions are fully transparent and clear to borrowers as to what will happen after the term of the payment break, including setting out the available options to repay the loan and the full costs of the payment break. Credit unions should also make clear to borrowers, how their case will be treated if they continue to experience financial difficulties after the term of the payment break.***

   It is important that credit union members in receipt of such temporary payment flexibility, be provided with sufficient information to understand how the arrangement will operate, including the impact and costs to the member (e.g. increase in monthly repayments versus term extensions) and the overall financial impact on their loan, and how their case will be treated when the arrangement comes to an end.

6. ***Credit unions have board approved plans to deliver an assessment of all borrowers on payment breaks to ensure that appropriate and sustainable solutions are identified in a timely manner for those borrowers who are not able to return to paying full capital and interest at the end of the payment break. Engagement with the borrower now and throughout the term of the payment break should have this outcome in mind.***

   COVID-19 impacts will include different consequences for member capacity to repay loans in line with contract. Some borrowers may be impacted on a temporary basis, and their loan repayments will shortly resume in line with contract. For others, impacts may be longer term in nature and may have a more significant impact on their ongoing ability to repay their loan. These particular factors and circumstances need to be considered by each credit union board, as part of their objective loan provisioning assessment in line with the existing provisioning framework. It has never been more important to ensure that distress within individual credit union loan books is not underestimated through loan classification and provisioning assessments.

7. ***The prioritisation of borrower engagement, assessment and determination of an appropriate and sustainable solution should be determined by the risk profile of the borrower i.e. those at higher risk of not being able to return to paying full capital and interest should be prioritised to ensure that they can avail of appropriately tailored treatments at the earliest possible stage (i.e. potentially before the end of the payment break term).***

8. ***The level of distress in the credit unions' loan books should be prudently considered and be reflected in provisioning levels.***

   Central Bank Provisioning Guidelines

   The purpose of provisioning is to ensure that loan losses are recognised as early as possible to support clarity and transparency on the performance of loan books and the financial position of individual credit unions.

   Financial Reporting Standard 102 (FRS 102) - the accounting standard applicable to credit unions - requires an *'incurred loss'* approach to the calculation of bad debt provisions on loans. FRS 102 permits that a provision may be required on a group of loans where there is observable data which indicates that there has been a measurable decrease in the estimated future cash flows on the group of loans since their initial recognition, even though the decrease cannot yet be identified within the individual loans in the group. Credit unions should assess all loans for objective evidence of impairment based on all available information including current information and events at the date of assessment. Certain information and events can be seen as impairment triggers that may affect the likelihood of loss events occurring, and therefore the appropriate levels of provisions for loans.

Our Provisioning Guidelines for Credit Unions (April 2018) were put in place to ensure credit unions have appropriate procedures for assessing and measuring credit risk, to support judgements about the risk of lending exposures. Under the guidelines, the Central Bank expects that credit unions undertake a loan impairment review on at least a quarterly basis, to help to ensure the recognition of loan losses as early as possible in accordance with applicable accounting standards.

As set out in the guidelines, it is the overall responsibility of the board of each credit union to ensure the adequacy and accuracy of its loan provisioning. The Central Bank expects credit unions to continue to apply a conservative and comparable approach in the measurement of provisions, and to regularly assess loans for objective evidence of impairment. This will be based on all available information at assessment, including for instance unforeseen changes in the economic cycle.

9. ***Sufficiently granular and timely reporting of the take-up of payment breaks across borrower type and sector should be readily available and used to inform key decision-making processes in credit unions.***

   Credit unions need to ensure that instances of loan forbearance are clearly designated and identiable in their records / systems, with accurate and timely management information reports available as required.

Central Credit Register

When a lender agrees a payment break with a borrower, the lender should not report this to the Central Credit Register as being payments being “missed” or “past due” or the loan as being “restructured”, during the period of the payment break.

Reporting of Rescheduled Loans

As referenced earlier, the Central Bank is gathering specific information (via completed template submissions) from all credit unions in relation to member requests for modification of loan repayments in the context of COVID-19. As this data is already being reported by credit unions, credit unions should exclude these modified loans from the rescheduled loans table in the June Prudential Returns submitted to this office.

Other Matters

More broadly, through Risk Mitigation Programmes (RMPs) and our supervisory interactions, we have stressed the importance of credit unions continuing to focus on identifying, managing and mitigating risks. Credit risk is clearly a key risk given that loan portfolios can come under stress in a crisis. Robust governance and effective risk management remain fundamental to the ongoing protection of members’ funds.

Credit union boards must understand and plan for the potential impacts of COVID-19 on the financial performance and financial resilience of their credit union. Credit unions should identify potential lending concentration risks within their loan books to those sectors that could be most affected by the changed economic environment. The range of risk considerations arising from COVID-19 should remain an area for continual assessment by credit unions, given the wider economic and financial impacts.

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Summary

Finally, we will continue to engage with all credit unions in delivering on our statutory mandate - to ensure the protection by each credit union of the funds of its members and the maintenance of the financial stability and well-being of credit unions generally.

We recognise credit unions will need to take action to support members affected by COVID-19. It is fundamentally important that a prudent approach is maintained to all aspects of a credit unions' business, including lending, investments, liquidity and capital, as it will best serve the longer term interests of credit unions and their members.

Given the ever-changing developments associated with COVID-19, we stress the continued need for early engagement by credit unions on any emerging issues with their supervisor in the Registry of Credit Unions.

Yours sincerely,

Patrick Casey

Patrick Casey
Registrar of Credit Unions