PD-ABY-680

World Council of Credit Unions, Inc.

Savings Best Practices

Sponsored by the United States Agency for International Development
Cooperative Agreement No. LAG-A-00-00-00027-00

Final Project Report
January 31, 2003

Prepared by: **Janette Klaehn, Savings Best Practices Project Manager**

Submitted to: **Wiliam Brands, Acting Team Leader for Broad-based Economic Growth Group, LAC/RSD**
Dana Doo Soghoian, Agreement Officer, M/OP/EER/DGLA

WOCCU

World Council of Credit Unions, Inc. • 5710 Mineral Point Road • PO Box 2982 • Madison, WI 53701-2982
Phone: (608) 231-7130 • Fax: (608) 238-8020 • E-mail: mail@woccu.org • Home Page: www.woccu.org

A

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LIST OF ATTACHMENTS

I. PROJECT OVERVIEW

A. Project Dates

September 28, 2001- November 30, 2002, with a no-cost extension until January 31, 2003

B. Meeting the Project Objectives

The purpose of the Savings Best Practices project was to capture and spread the best practices learned from credit union savings experience. The program offered an opportunity for credit unions to share grass roots savings mobilization lessons learned with other microfinance institutions in the field. At the same time, it offered credit unions the opportunity to place savings mobilization within the safety and soundness context of an adequate regulatory and supervisory framework.

During the first year of the project, WOCCU conducted field studies of existing savings and supervision practices and conducted one regional seminar on Supervision Best Practices in Quito, Ecuador and one regional conference on Savings Best Practices in Lima, Peru.

During the second year of the project, WOCCU developed an on-line presence for the project on the WOCCU website; conducted one regional conference on Supervision Best Practices in Mexico City, Mexico and one regional training workshop on Savings Best Practices in Managua, Nicaragua; implemented a conference on savings best practices for the larger international microfinance community in Washington, DC; published the operational guide *A Technical Guide to Savings Mobilization: Lessons from the Credit Union Experience*; published the book *Striking the Balance in Microfinance: A Practical Guide to Mobilizing Savings*, in both English and Spanish; and published a best practices series on the supervision of credit unions and produced a summary paper on credit union regulation and supervision in Latin America.

C. Project Outcomes

The following table, submitted to USAID in the first annual report of the project, outlines the development and acheivements of the Savings Best Practices project.

PROJECT OUTCOMES	PROJECTED	YEAR 1	YEAR 2
Intermediate Outcomes			
Savings Literature Review, Attachment 4	Year 1	Ongoing	
Credit Union Supervision Literature Review	Year 1	Replaced by Best Practice Series	
Field Assessment Results, Attachments 5, 6 and 7	Year 1	Completed	
Training Materials for Savings Best Practices conference in Peru, submitted in first annual report	Year 1	Completed	
Training Materials for CU Supervision Best Practices Seminar in Ecuador, submitted in first annual report	Year 1	Completed	
Savings Product Pilot Testing Tool Kits/Reports	Years 1 and 2	Discontinued	
Survey of Savings Best Practices Conference Participants	Year 1	Completed	
Training Materials for Savings Best Practices Conference in Nicaragua, Attachment 9	Year 2		Completed
Training Materials for Supervision Best Practices Seminar in Mexico, Attachment 11	Year 2		Completed
Regional Training Conferences and Seminars			
Supervision Best Practices seminar in Ecuador	Year 1	Aug. 2001	
Savings Best Practices conference in Peru	Year 1	Oct. 2001	
Supervision Best Practices seminar, Mexico	Year 2		May 2002
Savings Best Practices conference, Nicaragua	Year 2		April 2002
Final Products			
Impact Survey of Savings Best Practices Participants	Year 2	Not Completed, book published instead	
Impact Survey of Supervision Best Practices Participants	Year 2	Not Completed, series published instead	
Tool Kit for Mobilizing Savings, Attachments 15, 16, and 17	Year 2		Book published
Paper on Supervision Best Practices Guidelines, Attachments 18 and 19	Year 2		Completed
Final Conference in Washington, D.C., Attachment 13	Year 2		Nov. 2002

D. Budget

Year To Date

Total project budget expended as of January 31, 2003 was $717,548.12, which represents 89.69 percent of the total project budget. The total project funds expended are broken down into the following line items:

Total Program:	$382,416.71
Total Procurement:	$95,523.60
Total Training:	$82,377.54
Indirect Costs*:	$154,876.31
Project Total:	**$717,548.12**

*Final direct costs adjustments will be made at end of year 2003, with WOCCU's approved NICRA rate applied to January 2003.

Cost Share: Year 1

WOCCU entered into a Memorandum of Collaboration with El Deutscher Genossenschafts-und Raiffeisenverband e.V. (DGRV) whereby both organizations agreed to work together in the implementation of the Best Practices project. DGRV agreed to finance some costs related to field assessments, savings conferences, supervision seminars, and the final international conference in Washington, D.C. (See Attachment 1.)

Total cost share as of November 30, 2001 was $92,746.57, which represented 58 percent of the total cost share required by the Project Agreement.

Cost Share: Year 2

WOCCU continued it's collaboration with El Deutscher Genossenschafts-und Raiffeisenverband e.V. (DGRV) during the second year of the project. The cost share during the second year of the project was $163,022. Total calculated cost share at project-end was $249,683, 138 percent of the cost share required by the Project Agreement.

Also, WOCCU entered into a relationship with Pact Publications, Inc. (See Attachment 14) so that Pact assumed the substantial printing costs associated with publishing the book that was the final output of the project.

Registration Fees

Under the terms of the Project Agreement, project income was not included as part of the project cost share. Rather, project income was deducted from the total project, or program allowable cost, in determining the net allowable costs on which the Federal share of costs was based, as stated in CFR226.24, (d). However, WOCCU deemed it reasonable to consider registration costs as reimbursement of costs. Since WOCCU did not make any profit and charged only a minimal fee in order to recover some of the costs of the workshop, any money received was credited to expense line items. Registration fees amounted to a total of $19,170.62 over the life of the project.

F. Contract Modifications

Change in Key Personnel

Pursuant to section 1.6 of the schedule in the Project Agreement, WOCCU designated Nathalie Gons to be the project coordinator, or the personnel key to the successful completion of the objective of this award. Ms. Gons resigned from WOCCU as of December 3, 2001. WOCCU sought and received the approval of the USAID Cognizant Technical Officer to designate Janette Klaehn as the project manager through completion of the project in November 2002.

Change in Location of Supervision Conference

After serious consideration, WOCCU determined that Mexico would be a more appropriate location than Nicaragua for the second Supervision Best Practices seminar. The principal reason for moving out of Nicaragua was that supervision of credit unions there was less developed than in other countries in Latin America. WOCCU believed it would be more beneficial to both participants and the host country regulatory body if the seminar were conducted in a country with more developed supervision practices, such as in Mexico. The second Savings Best Practice Conference was held in Nicaragua.

Removal of the Mexico Component

Per agreement between USAID and WOCCU in August 2001, the project description was modified such that the microsavings field assessment in Mexico was removed. Funds allocated to the Mexican microsavings field assessment were reprogrammed accordingly to the remaining activities of the project (See Attachment 2).

No-cost Extension

WOCCU proposed and received a three-month no-cost extension on the project in order to be able to publish the book in both English and Spanish (See Attachment 3).

II. PRE TRAINING EVENT OUTPUTS

Activities conducted prior to the project training events are summarized below.

A. Marketing: Spreading Savings Best Practices

The Savings Best Practices Project aimed to share credit union lessons learned in savings mobilization with both credit union and non-credit union microfinance institutions. During the project, effective marketing channels were identified and utilized to disseminate information about the Savings Best Practices training events to the latter target audience group. Marketing channels utilized include the Consultative Group to Assist the Poorest (CGAP), the Small Enterprise Education and Promotion Network (SEEP) website and listserve, the Devfin listserve, Global Network for Banking Innovation in Microfinance (GNBI) meetings and the Women's World Banking/GNBI newsletter.

B. Savings Literature Review

An initial review of the latest savings research was necessary in order to enable the project publications and training events to address the concerns of a broader microfinance audience. A savings literature review was compiled during Year 1. Literature reviewed as of February 2001 confirmed the lack of practical tools in existence and underscored the need for a comprehensive set of operational guidelines and tools necessary to deliver small and micro savings via sound institutions.

C. Field Assessments

Field assessments in both savings and supervision practices served to document case-study examples of practices employed on the operational level. These onsite visits also allowed WOCCU team members to interact with local actors instrumental to attaining the desired breadth of outreach.

Credit Union Savings Field Assessment

Three site visits were conducted to WOCCU projects in Nicaragua (Jan. 15-26, 2001), Ecuador (Feb.12-24, 2001) and Guatemala (March 5-16, 2001) to document current savings practices in the region. Interviews were conducted with credit union managers and staff to document pre-conditions, methodologies, products and marketing strategies. The interviews followed guided questions drawn from the survey tool designed by WOCCU for the field assessment (modified slightly per credit union and local context). The Nicaraguan field assessment was most informative about the conditions an institution must establish before mobilizing savings (pre-conditions). The Ecuadorian field assessment exhibited how institutions can manage their savings. The Guatemalan field assessment discovered the use of innovative savings products. For a savings field assessment scope of work and working drafts of assessment results, see Attachments 4 and 5.

Credit Union Supervision Field Assessment

WOCCU and DGRV teamed up to assess current credit union supervision practices in Peru, Bolivia and Ecuador, May 6-19, 2001. Some field study results were distributed at the first Supervision seminar in Quito, Ecuador. For a scope of work and assessment results, see Attachment 6.

III. TRAINING EVENTS

A. Savings Mobilization Best Practices Training Conferences

Savings Mobilization Best Practices Conference 1

Date: October 2001
Location: Lima, Peru

Objectives

The training conference presented savings mobilization in a comprehensive framework of the key operations necessary to prudently install, mobilize and manage savings. Consistent with project goals, the Savings Mobilization Best Practices conference (i.) was practical and participatory; (ii.) was relevant to a broad audience that included credit unions as well as non-credit union MFIs; and (iii.) presented regional best practices experiences.

Implementation
The training conference offered a comprehensive framework of the key operations that comprise savings mobilization best practices. Participatory workshops in both front and back end operations optimized participant learning. Case study presentations highlighted lessons learned in successful savings mobilization in some Latin American countries.

Results
The conference in Peru brought together almost 180 participants from credit union organizations, *financieras, cajas municipales*, EPYMES, other non-government organizations providing financial services and technical assistance providers, representing a total of 13 countries. All conference presentations were posted on the WOCCU website for the duration of the SBP project. The presentations and participant list were submitted to USAID in the first annual report.

<u>Savings Mobilization Best Practices Conference 2</u>
Date: April 2002
Location: Managua, Nicaragua

Objectives
The agenda for the second Savings Mobilization Best Practices Conference reflected the lessons learned in the first conference and incorporated comments received from participants. WOCCU had also conducted an internal review of the presentations from the first Savings Best Practices Conference in Peru to identify the topics presented in Nicaragua. This second conference had the multiple purposes of attracting a broader base of microfinance institutions to learn about savings best practices, allowing past and new participants to learn about savings mobilization through focused plenary discussions and longer participatory workshops and providing WOCCU authors with the opportunity to refine their guides and tools for the final project publication.

Implementation
The training conference presented savings mobilization in a comprehensive framework of the key operations necessary to prudently install, mobilize and manage savings. Consistent with project goals, the Savings Mobilization Best Practices conference (i.) was practical and participatory; (ii.) was relevant to a broad audience that included credit unions as well as non-credit union MFIs; and (iii.) presented regional best practices experiences. Specialized, in-depth workshops enabled participants to learn in-depth information about various components of savings mobilization.

Results
The conference in Nicaragua brought together almost 270 participants from credit union organizations, *financieras, cajas municipales*, EPYMES, other non-government organizations providing financial services and technical assistance providers, representing a total of 16 countries. All conference presentations were posted on the WOCCU website for the duration of the SBP project. See Attachments 8 and 9 for participant list and presentations.

Savings Mobilization Best Practices Final Conference

Date: November 2002
Location: Washington, DC

Objectives
The final conference on savings mobilization had the objectives of discussing and disseminating best practices in savings mobilization from all types of microfinance institutions to all types of microfinance institutions. All institutions interested in initiating or expanding savings programs and international donors and policymakers were invited to attend.

Implementation
The two-day conference presented panel discussions of experts in savings mobilzation. The panel topics included savings patterns of the poor; making the transition to savings-based financial intermediaries; designing, managing and marketing innovative savings products; assessing the costs of savings mobilization; and the effective supervision of savings institutions. All participants were invited to share their perspectives and experiences in open discussions following each panel.

Results
The conference brought together 155 participants, including microfinance experts and practitioners, international donors and credit union practioners, from 35 countries. All conference presentations were posted on the WOCCU website for six months after the conference. See Attachments 12 and 13 for participant list and presentations.

B. Supervision Best Practices Seminars

Supervision Best Practices Seminar 1

Date: August 2001
Location: Quito, Ecuador

Objectives
The objectives of the first Supervision seminar were to foster dialogue among credit union regulators regarding what constitutes supervision best practices, both in terms of the underlying legal and theoretical framework as well as in terms of the practices and tools used to implement credit union supervision in Latin America.

Implementation
The two-day seminar, held in Quito, Ecuador, provided a forum of exchange for credit union regulators, policymakers and technical assistance providers from 13 countries, including experts from USAID, IDB, ASBA, DGRV and WOCCU. Credit union supervision best practices were presented on a theoretical level by international experts and then juxtaposed with the experiences of regional regulators. Key components of credit union supervision included supervision models, laws and regulations, tools and practices.

Results
The Supervision conference in Ecuador brought together 74 participants from 13 countries. Participants included regulators, supervisors, policymakers and donors. All conference

presentations were posted on the WOCCU website for the duration of the SBP project. The presentations and participant list were submitted to USAID in the first annual report.

Supervision Best Practices Seminar 2

Date: May 2002
Location: Mexico City, Mexico

Objectives

The first Supervision seminar presented a comprehensive regional perspective of current credit union supervision tools and practices. The second seminar presented fewer topics in more depth and included participatory workshops on key supervision tools and practices.

Implementation

Implementation of the second Supervision seminar reflected participant comments and incorporated recommendations from WOCCU internal evaluations. WOCCU increased the duration of the seminar from two days to three days. This seminar offered two days of theoretical discussions followed by a full day of participatory workshops.

Results

The Supervision conference in Mexico brought together 165 participants from 18 countries. Participants included regulators, supervisors, policymakers, Mexican federation representatives and donors. All conference presentations were posted on the WOCCU website for the duration of the SBP project. See Attachments 10 and 11 for participant list and presentations.

III. WRITTEN OUTPUTS

A. *Technical Guide to Savings Mobilization: Lessons from the Credit Union Experience*

As a predecessor to the final publication of the SBP project, WOCCU published a 14-page technical guide in March 2002 to summarize the key areas of savings mobilization and present data on savings in WOCCU projects worldwide. The guide was distributed to more than 2,000 individuals from international donor institutions, technical assistance agencies, credit unions and other microfinance institutions worldwide.

B. *Striking the Balance in Microfinance: A Practical Guide to Mobilizing Savings/ El logro del equilibrio en las microfinanzas: guía práctica para movilizar los ahorros*

In collaboration with Pact Publications, WOCCU published the final publication of the SBP project in both English and Spanish. *Striking the Balance in Microfinance: A Practical Guide to Mobilizing Savings* is a groundbreaking guide to savings mobilization, complete with operational tools for implementation, written by practitioners for practitioners. This book takes readers through the process of mobilizing savings, from assessing the readiness of their own institutions to capture deposits responsibly, through establishing policies and procedures, developing products and marketing strategies, launching marketing campaigns and determining the costs of mobilizing savings. Case studies demonstrate how credit unions were able to implement successful savings programs to grow their institutions and better serve their communities. The toolbox provides worksheets, surveys and sample forms for readers to utilize in their own organizations. The book was published in both English and Spanish. It was distributed to more than 500 readers around the world and continues on sale through Pact Publications at www.pactpublications.org. See Attachments 16 and 17 for the book.

C. Guidelines and Best Practices in Credit Union Supervision

WOCCU produced a white paper overview of best practices in the supervision of credit unions in Latin America. The paper is based on the lessons learned and best practices presented in the two supervision seminars of this project. WOCCU also published a series on best practices in Supervision on its website at www.woccu.org. See Attachments 18 and 19 for drafts of the papers.

V. CONCLUSION

As illustrated in the present report, the Savings Best Practices Project met the objective set out in the Project Agreement: to capture and spread best practices learned from credit union savings experience. Initially, the project compiled a frame of reference for savings mobilization through the development of a literature review and the conducting of field assessments of current savings and supervision practices in Latin America. Participants in the Savings Mobilization Best Practices conferences learned from the best practices presented there and left the conferences armed with many of the tools required to implement them. At the same time, through the Supervision seminars, WOCCU spread supervision best practices throughout the region so that credit unions are able to mobilize savings within the safety and soundness context of improved regulatory frameworks. The summary paper and web series continue to disseminate best practices in supervision

Best practices for mobilizing savings, further defined through the activities of this project, were shared with the larger international microfinance community at an open conference in Washington, D.C. WOCCU published *Striking the Balance in Microfinance: A Practical Guide to Mobilizing Savings* to serve as a resource for institutions expanding or initiating savings services. As intended, the project successfully captured and spread savings best practices to credit unions and non-credit union microfinance institutions worldwide and supervision best practices to regulators throughout Latin America.

VI. ATTACHMENTS

Attachment 1

Memorandum of Collaboration between WOCCU and DGRV

MEMORANDUM OF COLLABORATION: DGRV-WOCCU BEST PRACTICES PROJECT

WOCCU and DGRV hereby agree to collaborate in the implementation of the Best Practices project. Collaboration will include: (i) a field assessment of credit union best practices in savings mobilization; (ii) a field assessment of best practices in credit union supervision; (iii) 2 savings mobilization best practices workshops – one in Peru and one in Nicaragua; (iv) 2 supervision best practices seminars – one in Ecuador and one in Nicaragua; (v) one international conference about savings mobilization best practices in Washington D.C.

WOCCU asks DGRV for counterpart contributions up to US$150,000, out of the total project cost of US$960,000. DGRV's counterpart contribution is not a cash transfer to WOCCU but comprises costs incurred by activities related to the Best Practices project, which may include:

- Participation of DGRV employees in evaluations, seminars, workshops and other events implemented on behalf of the Best Practices project.
- Organizing and financing the participation of other experts in credit union savings mobilization and supervision of credit unions, such as colleagues of DGRV.
- Financing costs associated with the implementation of workshops, seminars and other events related to the Best Practices project.

WOCCU asks DGRV to disclose their counterpart contribution in a written format to WOCCU, including costs incurred by DGRV staff to participate in events related to the Best Practices project, such as salary, travel costs, local transportation, communications, lodging, per diems, and any other project-related cost incurred, such as renting a conference room, catering, etc. WOCCU asks DGRV to save original receipts for costs incurred on behalf of the Best Practices project in the event that WOCCU is subject to an audit at the request of USAID.

WOCCU and DGRV agree on collaborating in the implementation of the Best Practices project including making contributions towards the costs incurred on behalf of this project during the period of September 28, 2001 to November 30, 2002.

World Council of Credit Unions, Inc.	**El Deutscher Genossenschafts-und Raiffeisenverband e.V.**
By: [signature]	By: [signature]
Brian Branch Vice-President	Paul Armbruster Director, Department of International Relations
Date: 6/10/01	Date: 22-06-01

World Council of Credit Unions, Inc.
Savings Best Practices

Attachment 2

Letter of Agreement for Removal of Mexico Component

14

USAID

U.S. AGENCY FOR INTERNATIONAL DEVELOPMENT

COPY

AUG 9 2001

Mr. Brian Branch
Vice President
World Council of Credit Unions, Inc.
5710 Mineral Point Road
Madison, WI 53701-2982

SUBJECT: Grant No. LAG-G-00-00-00027-00
Modification No. 01

Dear Mr. Branch:

Please have an authorized official sign the **original** and **all copies** of the enclosed modification. Return the **original and one copy** to the addresses listed below. Your copy is marked with the yellow post-it.

Regular Mail:

U.S. Agency for International Development
M/OP/EER/DGLA - Office of Procurement
Room 7.09-082, RRB - 7th Floor
13th Street and Pennsylvania Avenue
Washington, DC 20523-1700

Delivered by Courier or Express Mail:

U.S. Agency for International Development
M/OP/EER/DGLA - Office of Procurement
Ronald Reagan Building - 14th Street Entrance
Washington, DC 20523-7100
Telephone No.: 202-712-5671

Sincerely

Dana P. Doo-Soghoian

Dana P. Doo-Soghoian
Grant Officer
Office of Procurement
M/OP/EER/DGLA

Enclosures: a/s

MODIFICATION OF ASSISTANCE

1. MODIFICATION NUMBER	2. EFFECTIVE DATE OF MODIFICATION	3. AWARD NUMBER:	4. EFFECTIVE DATE OF AWARD:
01	See Block 15	LAG-G-00-00-00027-00	09-28-2000

5. GRANTEE:
World Council of Credit Unions, Inc.
5710 Mineral Point Road

Madison WI 53701-2982

DUNS NO.: 078949013
TIN NO. : 391143339

6. ADMINISTERED BY:
U.S. Agency for Int'l Development
Office of Procurement
M/OP/EER/DGLA, Rm. 7.09-082, RRB
1300 Pennsylvania Avenue, NW
Washington DC 20523-7100

7. FISCAL DATA: Amount Obligated: $500,000.00

Budget Fiscal Year: 2001
Operating Unit: LAC/RSD
Strategic Objective: 598-017
Team/Division: n/a
Benefiting Geo Area: 598
Object Class: 410000
NMS No.: 824

8. TECHNICAL OFFICE:
LAC/RSD-BBEG (Jeremy Smith)

9. PAYMENT OFFICE:
U.S. Agency for Int'l Development
M/FM/CMP/MP, Rm. 7.07-018 RRB
Office of Financial Management
1300 Pennsylvania Avenue, NW
Washington DC 20523

10. FUNDING SUMMARY:

	Obligated Amount	Total Est. Amt.
Amount Prior to this Modification:	$300,000.00	$800,000.00
Change Made by this Modification:	500,000.00	
New/Current Total:	$800,000.00	$800,000.00

11. DESCRIPTION OF MODIFICATION:

The purpose of this modification is to fully fund the grant in the amount of $500,000 and to eliminate the third component in the Program Description.

The specific changes are as follows:

A. ACCOUNTING AND APPROPRIATION

1. Section A.2., GENERAL, delete the amount of "$300,000" and substitute in lieu thereof "$500,000."

(continued on Page 2)

12. THIS MODIFICATION IS ENTERED INTO PURSUANT TO THE AUTHORITY OF the Foreign Assistance Act of 1961 AS AMENDED. EXCEPT AS SPECIFICALLY HEREIN AMENDED, ALL TERMS AND CONDITIONS OF THE GRANT REFERENCED IN BLOCK #3 ABOVE, AS IT MAY HAVE HERETOFORE BEEN AMENDED, REMAIN UNCHANGED AND IN FULL FORCE AND EFFECT.

13. GRANTEE: [X] IS [ ] IS NOT REQUIRED TO SIGN THIS DOCUMENT TO RECONFIRM ITS AGREEMENT WITH THE CHANGES EFFECTED HEREIN

14. GRANTEE:

BY: Mary J. Chapman
MARY CHAPMAN
(Name Typed or Printed)
TITLE: VP & CFO
DATE: August 14, 2001

15. THE UNITED STATES OF AMERICA
U.S. AGENCY FOR INTERNATIONAL DEVELOPMENT

BY: Dana P. Doo-Soghoian
Dana P. Doo-Soghoian
(Name Typed or Printed)
TITLE: Grant Officer
DATE: AUG 9 2001

ASSISTANCE NO.	MODIFICATION NO.		
LAG-G-00-00-00027-00	01		

DESCRIPTION OF MODIFICATION (CONTINUED)

2. Section B., Specific, add the following fiscal data:

"NMS Request ID No.: 824
Organization ID: 10258
BBFY: 2001
EBFY: 2002
Fund: DV
OP Unit: LAC/RSD
SO: 598-017
Geo Area: 598
SOC: 410000
Amount Obligated: $500,000"

B. ATTACHMENT 2 - PROGRAM DESCRIPTION, delete any and all references made to a micro savings/credit union sector field research and assessment in Mexico. Reprogram funds accordingly to the remaining two activities stated in the *Program Description*.

World Council of Credit Unions, Inc.
Savings Best Practices

Attachment 3

No-cost Extension Proposal and Approval

copy: WOT. fry BHR ✓

USAID

S. AGENCY FOR
INTERNATIONAL
DEVELOPMENT

SEP 2 1 2002

Ms. Janette Klaehn
World Council of Credit Unions, Inc.
5710 Mineral Point Road
Madison, WI 53701-2982

SUBJECT: Grant No. LAG-G-00-00-00027-00
Modification No. 02

Dear Ms. Klaehn:

Please have an authorized official sign the **original** and **all copies** of the enclosed modification. Return the **original and one copy** to the addresses listed below. Your copy is marked with a colored post-it.

Regular Mail:

U.S. Agency for International Development
M/OP/EER/DGLA - Office of Procurement
Room 7.09-085, RRB - 7th Floor
13th Street and Pennsylvania Avenue
Washington, DC 20523-7803

Delivered by Courier or Express Mail:

U.S. Agency for International Development
M/OP/EER/DGLA - Office of Procurement
Ronald Reagan Building - 14th Street Entrance
Washington, DC 20523-7803
Telephone No.: 202-712-5671

Sincerely

Dana P. Doo-Soghoian

Dana P. Doo-Soghoian
Grant Officer
Office of Procurement
M/OP/EER/DGLA

Enclosures: a/s

MODIFICATION OF ASSISTANCE

1. MODIFICATION NUMBER	2. EFFECTIVE DATE OF MODIFICATION	3. AWARD NUMBER:	4. EFFECTIVE DATE OF AWARD:
002	See Block 15.	LAG-G-00-00-00027-00	09-28-2000

5. GRANTEE:
World Council of Credit Unions, Inc
5710 Mineral Point Road

Madison WI 53701-2982

DUNS NO.: 078949013
TIN NO. : 391143339 LOC NO.: 98A9P

6. ADMINISTERED BY:
US Agency for International Development
Office of Procurement
M/OP/EER/DGLA, Rm. 7.09-085, RRB
1300 Pennsylvania Avenue, NW
Washington DC 20523-7803

7. FISCAL DATA: Amount Obligated: $.00

Budget Fiscal Year:	2001
Operating Unit:	LAC/RSD
Strategic Objective:	598-017
Team/Division:	n/a
Benefiting Geo Area:	598
Object Class:	410000

8. TECHNICAL OFFICE:
LAC/RSD-BBEG

9. PAYMENT OFFICE:
US Agency for International Development
M/FM/CMP/MP, Rm. 7.07-018 RRB
Office of Financial Management
1300 Pennsylvania Avenue, NW
Washington DC 20523

10. FUNDING SUMMARY:

	Obligated Amount	Total Est. Amt.
Amount Prior to this Modification:	$800,000.00	$800,000.00
Change Made by this Modification:		
New/Current Total:	$800,000.00	$800,000.00

11. DESCRIPTION OF MODIFICATION:
The purpose of this modification is to extend the estimated completion date from November 30, 2002 to January 31, 2003 at no cost to either party and to make a change in the key personnel.

The specific changes are as follows:
I. COVER PAGE, second paragraph, delete the ending date of "30 November 2002" and substitute in lieu thereof "January 31, 2003."

II. ATTACHMENT 1, SCHEDULE
A. Section 1.2, PERIOD OF AGREEMENT, delete the estimated completion date of "30 November 2002".

12. THIS MODIFICATION IS ENTERED INTO PURSUANT TO THE AUTHORITY OF the Foreign Assistance Act of 1961 AS AMENDED. EXCEPT AS SPECIFICALLY HEREIN AMENDED, ALL TERMS AND CONDITIONS OF THE GRANT REFERENCED IN BLOCK #3 ABOVE, AS IT MAY HAVE HERETOFORE BEEN AMENDED, REMAIN UNCHANGED AND IN FULL FORCE AND EFFECT.

13. GRANTEE: ☒ IS ☐ IS NOT REQUIRED TO SIGN THIS DOCUMENT TO RECONFIRM ITS AGREEMENT WITH THE CHANGES EFFECTED HEREIN

14. GRANTEE:

BY: Mary J. Chapman
MARY J. CHAPMAN
(Name Typed or Printed)
TITLE: Vice President & CFO
DATE: September 30, 2002

15. THE UNITED STATES OF AMERICA
U.S. AGENCY FOR INTERNATIONAL DEVELOPMENT

BY: Dana P. Doo-Soghoian
Dana P. Doo-Soghoian
(Name Typed or Printed)
TITLE: Grant Officer
DATE: 09-21-2002

MODIFICATION OF ASSISTANCE CONTINUATION PAGE

ASSISTANCE NO.	MODIFICATION NO.		
LAG-G-00-00-00027-00	002		

11. DESCRIPTION OF MODIFICATION (CONTINUED)

B. Section 1.2, PERIOD OF AGREEMENT, second paragraph, delete the date of "30 September 2001" and substitute in lieu thereof "January 31, 2003."

C. Section 1.6, KEY PERSONNEL, delete the name of "Nathalie Gons" and replace it with "Janette Klaehn."

All other terms and conditions of this grant remain unchanged.

World Council of Credit Unions, Inc.

October 1, 2002

Dana P. Doo-Soghoian
Grant Officer
Office of Procurement
M/OP/EER/DGLA
U.S. Agency for International Development
Ronald Reagan Building – 14th Street Entrance
Washington, DC 20523-7803

Subject: **No-cost Extension and Change in Key Personnel for Grant No. LAG-G-00-00-00027-00**

Dear Ms. Do-Soghoian:

Enclosed please find the signed original and one copy of Modification No. 2, for the no-cost extension and change in key personnel for Grant No. LAG-G-00-00-00027-00.

Thank you for allowing us to extend the project and change the key personnel. We very much appreciate your attention to this matter.

Sincerely,

Janette Klaehn

Janette Klaehn
Savings Best Practices Project Manager

Enclosures

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"Quality Credit Unions for Everyone!"

Attachment 4

Savings Literature Review

WOCCU Savings Best Practices: Savings Literature Review

February 10, 2001

Nathalie Gons
WOCCU
Savings Best Practices Project
LAG-G-00-00-00027-00

THIS IS A WORKING DRAFT, PLEASE DIRECT ANY COMMENTS TO
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Summary of Literature Review

A large portion of NGO/donor Microsavings literature (MSL) provides a convincing case, using both empirical and theoretical evidence, that the poor can and do save. Therefore, as financial service providers to the poor, MFIs are under growing pressure to offer voluntary and withdrawable savings services to the poor.

Another portion of MSL literature explores how the poor save, using observations from informal savings strategies as well as from NGOs such as SafeSave as benchmarks for MFIs savings product development, i.e. general guidelines of the poor's demand for savings products. This group of literature highlights the role of market research, focus groups, pilot testing and follow up etc. Some general conclusions of this demand-side analysis include that it is imperative to offer voluntary withdrawable savings (as demanded by the poor) in order to mobilize large-scale savings. CGAP/GTZ literature also argues that savings mobilization will result in a greater outreach to the poor.

The NGO literature does not provide a supply-side analysis. In other words, a thorough consideration of the institutional factors involved in mobilizing savings is void in the literature reviewed here. Instead, one finds a general discussion of: the difficulty of transforming institutions that are in the habit of mobilizing forced savings into ones mobilizing voluntary savings, lack of adequate regulatory and insurance mechanisms. MSL does assuage some of the fears of those MFIs practicing forced savings strategies by citing some cases of MFIs offering withdrawable savings that did not experience subsequent decapitalization.

NGO/donor microsavings literature cites successful cases of microsavings mobilization, of which 4/6 are of state and/or commercial banks (see 34,36,39,42). These case studies may be of limited practical relevancy to NGOs that are transforming into financial intermediaries and/or that do not benefit from an elaborate and integrated infrastructure network like banks generally do.

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MicroSavings Literature Review[1]

[1] Several reports cover various topic areas. These reports are marked with an *; a summary will appear only when it is cited for the first time.

WHY MICROFINANCE INITIATIVES SHOULD INCLUDE A SAVINGS COMPONENT

1. *Otero, Maria (1989), "A handful of rice: Savings mobilization by microenterprise programs and perspectives for the future", Acción International: monograph no. 3.

Discusses why microenterprise programs should mobilize savings from low-income households. Cites successful experiences the Grameen Bank, BKK and the Cameroon Cooperative CU League and the reasons motivating a savings component in ACCION affiliates. Guidelines for practitioners is organized by: linking structure, efficient systems and procedures, interest rate structure, savings as a requirement, individual and group savings

2. Hunte, C. Kenrick (1997), "The impact of savings mobilization on credit rationing: Empirical evidence from Jamaica", 22(4).

Analyzes financial records of 584 clients from 42 People's Cooperative Banks in Jamaica to explore the question: do savings reduce credit rationing and expand credit access. Conclusion = yes. In addition the following observations are made: offering positive interest rates is imperative to reducing external dependency.

3. Wright, Graham (1999a), "The case for voluntary, open access savings facilities and why Bangladesh's largest MFIs were slow to react", *Challenges of Microsavings Mobilization-Concepts and Views from the Field.*

Discusses the successful microsavings mobilization experience of BURO Tangail, a Bangaldeshi NGO and juxtaposes it to the large MFIs in Bangladesh, who practiced forced-savings. BURO Tanagial's success was perhaps the impetus for the large MFIs (Grameen, BRAC and ASA) who started offering voluntary withdrawable savings starting mid-1990's. The article mentions institutional obstacles for savings mobilization. The withdrawable savings system was put to the test as a severe natural disaster struck in 1998; MFIs offering withdrawable savings did not result in massive withdrawals as was expected. Evidence from Uganda yields a similar conclusion.

The paper concludes that voluntary open-access savings can yield more net savings /client than compulsory savings can. Therefore savings mobilization is not only an inherent component of the microfinance mission, it is also an institutionally beneficial strategy.

4. Wright, Graham (1999b), "Beyond Basic Credit and Savings: Developing New Financial Service Products for the Poor", *Challenges of Microsavings Mobilization-Concepts and Views from the Field.*

Offers guidelines for savings product development. The 4 main phases of product development are: research to identify needs and opportunities; design and pilot test; monitor and evaluate the pilot test's results; revise and scale-up implementation.

EVIDENCE THAT THE POOR SAVE & CHARACTERISTICS OF THEIR SAVINGS BEHAVIOR: IMPLICATIONS FOR MICROSAVINGS INITIATIVES (PRODUCT DEVELOPMENT)

5. *Goldstein, Gilles and Issa Barro (1999), "The role and impact of savings mobilization in West Africa: A study of the informal and intermediary financial sectors", Vol. I, Study commissioned by MicroSave Africa: February-March.

Documents how the poor save and discusses organizations that respond to this demand, which includes an extensive overview of SACCOs.

6. Goldstein, Gilles and Issa Barro (1999), "The role and impact of savings mobilization in West Africa: A study of the informal and intermediary financial sectors", Vol. II, Study commissioned by MicroSave Africa: February-March.

Vol.II summarizes the microfinance sector in 6 West African countries and outlines savings and loan products available to the poor through Savings and Credit Cooperatives.

7. Matin, Imran, Stuart Rutherford and Md Maniruzzaman (2000), "Exploring Client Preferences in microfinance: some observations from *Safe*Save", SafeSave Focus Note No.18.

Observations SafeSave client behavior provides insight into the demand of poor people for savings services. Poor people may have various savings strategies, one can save to spend and one can save to save, the purpose of microfinance organizations is to offer flexible products that allow for people to change their strategy.

8. Mutesasira, L. (1999), "Savings and needs: An infinite variety", UNDP/SUM.

Underlying the poor's motivations to save are risk protection and management considerations. The author classifies risks as: *lifecycle risks*, *structural risks* and *crisis risks*
Risk management strategies of the poor include investing in human, physical and social assets.

9. Ndanshau, Michael O.A. (1998), "Dependency Rates, Poverty and Savings Rates in he LDCs: Evidence from Cross-Sectional Household Data in Tanzania", *African Review of Money, Finance and Banking*, No.s 1-2.

Discusses the adverse effect of high dependency rates on household savings (a "dependent" is a non-income earners in a household). This study surveyed 256 rural households in N. Tanzania. Conclusions include: dependents exert a significant positive influence on savings in poor households and a positive but insignificant influence on savings in rich households. "Poor are not 'too poor to save', rather they have less and thus exhibit a smaller marginal propensity to save than rich households." Income associated with rich households savings; wealth significantly influences the savings capacities of the poor."(p91)

10. 10 Obwona, Marios B. and John Ddumba-Ssentamu (1998), "Household Savings in Developing Economies: Evidence from Microdata in Uganda", *African Review of Money, Finance and Banking*, No.s 1-2.

Presents a logit analysis of primary data collected on household savings: 727 rural households and 754 urban households in Uganda. Results include: income is associated with savings in urban households, not rural households; rural households are more likely to save in non-monetary forms, which is associated with dominance of subsistence production and low level of monetization in rural areas; education is the most significant variable correlated with monetary saving in rural households, not in urban; dependency ratio has a significant impact on urban monetary savings decisions, not for rural households.

11. Rutherford, Stuart (1999), " The poor and their money: An essay about financial services for poor people", Institute for Development Policy and Management, University of Manchester, January.

Explores how the poor use financial services, which points to ways in which the semi-formal/formal provision of financial services to the poor can be improved. One of Rutherford's facts: the poor can and do save. One of Rutherford's central research questions: how can financial services allow people to convert a series of savings into a useful lump sum?

12. Rutherford, Stuart (1999a), "Savings and the poor: The methods, use and impact of savings by the poor of East Africa", Study commissioned by MicroSave Africa: May.

Explains why and how the poor save and suggests how institutions can help this process. Summarizes the means used by poor households in Africa in the formal, semi-formal and formal sectors.

13. *Robinson, Marguerite S. (1992), "The role of savings in local financial markets: The Indonesian experience", GEMINI Working Paper No. 33, November.

Summarizes the myths and reality of the poor's savings behavior. Discusses the poor's savings strategies in non-financial and financial savings instruments. Discusses some structural incentives to stimulate the latter.

14. Wright, Graham A.N. (1999), "A Critical Review of Services in Africa and Elsewhere", Study commissioned by MicroSave Africa: September.

Two central study questions are: (i) why & how the poor save?; (ii) can MFIs meet the poor's savings needs? Points to the conflict that can arise out of the client's strategy, coined a strategy of "replication and multiplication" and the institution's strategy, coined a "permanence and growth" strategy. The latter encourages the long-term build up of funds through relatively slow steady. This is great for long-term borrowing needs but fails to provide service suitable the poors' savings strategy, which requires short-term savings products. Classifies savings needs of the poor into lifecycle needs, emergencies and opportunities

15. Wright, Graham A.N. (2000), *Microfinance Systems: Designing Quality Financial Services for the Poor*. Zed Books, Ltd: London.

Discusses why offering savings services is central in the pursuit to offer financial services to the poor. Focuses on how products can be developed in order to ensure they are taylored to the needs of the poor (as opposed to implementing savings products for the sole purpose of providing a source of capital for the institution). Uses the experiences of the the Central Cordillera Agricultural Program in the Philippines and BURO Tangail in Bangladesh as case studies of client-focused product design and implementation.

16. Zeller, M. (1995), " The demands for financial services by rural households: conceptual framework and empirical findings", *Zeitschrift fur asulandische Landwirtschaft*, 43(2).

Financial service demands of rural population include savings, credit and insurance. Article is critical of the conventional microfinance practices (targeting credit to specific uses etc.). Rural poor are able to save, are credit worthy and are willing to pay insurance premiums to cover certain risks. Notes that the informal financial market addresses demand for credit, savings and insurance.

HOW CAN MFIs MOBILIZE SAVINGS — GENERAL DISCUSSION

17. Bass, J. and K. Henderson (2000), "The Microfinance experience with savings mobilization", Microenterprise Best Practices Publications.

Offers the pros and cons of savings products from an institutional perspective and provides guidelines for product development and implementation, including: using a "funnel; process" to determine the most successful savings products; using market studies, pilot studies, and monitor. Defines the most important product qualities as: security, convenience, liquidity, and positive real return. Draws on W. African experience to give examples of short-term and long-term savings products.

18. Beverly, Sondra G. and Michael Sherraden (1999), "Institutional determinants of savings: implications for low-income households and public policy", *The Journal of Socio Economics*, 28, February.

Examines if the poor within the US have the ability to save and how programs and policies could facilitate their savings. The analysis explores the limitations of existing savings and asset accumulation theories in capturing the stages of saving in low-income households. These conventional theories are juxtaposed with Sherraden's institutional theory (see #21), which does incorporate a focus on the poor.

The article defines savings determinants in low-income households to fall under the following categories: demographic, psychological, sociological, behavioral, and institutional. The latter addresses: (i)an individual's access to institutional savings mechanisms; (ii) one's level of financial education; (iii) the affect of incentives offered by institutions; (iv) the role of institutions in facilitating savings; (v)an individual's access to credit or the affect of liquidity constraints.

19. Elser, Laura, Alfred Hannig, and Sylvia Wisniwski (1999), "Comparative analysis of savings mobilization strategies", *Challenges of Microsavings Mobilization-Concepts and Views from the Field.*

Synthesizes the results of 6 case studies of successful savings mobilization: 1.Bank for Agriculture and Agricultural Cooperatives in Thailand, Bank Rakyat Indonesia-Unit Des System, Rural Bank of Panabo in the Philippines, Banco Caja Social in Colombia, Caissess Villageoises d'Epargne et de credit Autogerées in Mali, and the Fédération desl Caisses dÉpargne et de Crédit Agricole Mutuel in Benin.
Presents an analytical framework for planning a successful savings mobilization strategy: institutional type, governance and organizational structure; demand-oriented savings products and technologies; management capabilities (esp. risk & liquidity management); regulation and supervisory framework; cost analysis.

Some conclusion include:
Savings respond to a financial service demand of the poor and is a commercially viable source of funds;
The most successful savings methodology is individual voluntary savings;
Implementing savings is more complex than credit

20. Robinson, Marguerite S. (1997), "Introducing savings in microcredit institutions: When and how?", *CGAP Focus Notes,* No.8.

Suggests that microcredit institutions should introduce savings when it is operating in enabling macroeconomic environment, with an adequate legal & regulatory framework, political stability and suitable demographic conditions, when they are subject to government supervision, and have good operational practices.
Provides general guidelines on how microcredit institutions should introduce savings, stating that voluntary and compulsory savings products are incompatible, products should be designed and priced together, deposit instruments should be appropriate for local demand, new marketing strategies will be needed, and attention must be paid to sequencing.

21. Sherraden, Michael (1991), *Assets and the Poor: A New American Welfare Policy.* M.E. Sharpe, Inc.: New York.

Proposals on how the poor can accumulate assets within the US banking sector. More specifically, Sherraden explores the structural barriers to saving faced by poor households. Offers policy proposals on how institutions can create incentives, focusing on individual development accounts (IDA), which match a certain percentage of the poor's savings depending in part on the purpose of that savings account. This is funded by local, federal, and philanthropic funds.

HOW CAN MFIs MOBILIZE SAVINGS — OPERATIONAL TOOLS

22. CGAP/MicroSave Africa (2001), "Costing/Pricing of Financial Services"
Anticipated completion date end of Feb.2001-Lorna Grace@CGAP.

23. FENACOAC (1998), *Manual de Movilización de Depósitos Para Cooperativas de Ahorro.*

24. FENACOAC (1992), "Marco conceptual del programa de mercadeo para cooperativas de ahorro y crédito afiliadas a FENACOAC, R.L.", March.

25. Linares, José (1996), "Desarrollo de la imagen y el ahorro en el sector de cooperatives de ahorro y crédito de Costa Rica (Mayo 1992-Diciembre 1994)", World Council of Credit Unions, Inc.

26. Morales, Gerardo René (1996), "Marketing program implementation in FEDECACES Credit Unions participating in project 'CRECER' ", World Council of Credit Unions, Inc., April.

27. Oliva, Oswaldo, Gerardo Morales and David Richardson (1997), "Model Credit Union policies: Credit policies, payment policies, internal control policies and savings policies", World Council of Credit Unions, Inc., June.

28. WOCCU-Nicaragua (1998), Policy and Procedure Manual for Savings and Deposits (Manual de Politicas y Procedimientos de Ahorros y Depositos).

SYNOPSIS OF MICROSAVINGS ISSUES

29. Fiebig, Michael, Alfred Hannig, and Sylvia Wisniwski (1999), "Savings in the context of microfinance–State of Knowledge", *Challenges of Microsavings Mobilization-Concepts and Views from the Field.*

Summarizes the main issues associated with microsavings for the client and for the institution. Some notable areas of discussion include cost management, savings vs. other sources of funds, and sequencing. It lists the following areas as key issues for future research and discussion:

- Institutional types and organizational structures
- Demand-driven savings products
- Management capabilities, esp. risk & liquidily management
- Internal & external regulation
- Cost accounting

30. Hannig, Alfred (1999), "Mobilizing Microsavings: The Millennium Challenge in Microfinance", Sixth Consultative Group Meeting of CGAP, June.

Summarizes the benefits of offering savings services to the poor and to the microfinance institution that is serving the poor. Compares the experiences of microsavings mobilization of the Bank for Agriculture and Agricultural Cooperatives in Thailand, Bank Rakyat Indonesia-Unit Des System, Rural Bank of Panabo in the Philippines, Banco Caja Social in Colombia, Caissess Villageoises d'Epargne et de credit Autogerées in Mali, the Fédération desl Caisses dÉpargne et de Crédit Agricole Mutuel in Benin and theCentenary Rural Development Bank in Uganda. The 4 areas that are compared are: savings products, technologies and marketing strategies, management skills, external and internal regulation and supervision and the costs of mobilizing and administering savings. (See #18 for a lengthier comparative report of the same institutions minus the Centenary Rural Development Bank in Uganda)

31. Wisniwski, Sylvia (1999a), "Microsavings Compared to Other Sources of Funds", *Challenges of Microsavings Mobilization-Concepts and Views from the Field.*

Discusses the advantages and disadvantages of different sources of funds in terms of cost and risk associated which each type of fund. Discussion of the latter suggests that microsavings can be a source of stable funds. Concludes that savings-led institutions and commercial banks are more likely the NGOs to be sustainable institutions with the institutional savvy able to offer a broad array of financial services.

CASE STUDIES OF SUCCESSFUL SAVINGS MOBILIZATION EXPERIENCES

32. CGAP (1998), "Savings mobilization strategies: Lessons from four experiences", *CGAP Focus Notes,* No.13.

Draws on the experiences of the Thai state-owned Bank for Agriculture and Agricultural Cooperatives (BAAC), state-owned Bank Rakyat Indonesia (BRI), Colombian church-owned Banco Caja Social and the privately-owned Rural Bank of Panabo (RBP) in the Philippines.

Compares the "7" key factors contributing to their successful microsavings mobilization:

- Economic reform and financial liberalization
- Institutional type and governance
- Organizational structure
- Savings products and technologies
- Risk management
- Liquidity management
- Regulatory framework and internal control
- Ways to lower the cost of savings mobilization

33. Chao-Beroff, Renee (1999), "Caisses villageoises d'épargne et de crédit autogerées (CVECA), Mali (Case Study), *Challenges of Microsavings Mobilization-Concepts and Views from the Field.*

Profiles CVECA's organizational structure (village bank) & governance structure; savings products, product design & roll-out; management capacity; regulatory & supervisory framework; and cost analysis (mainly donor-funded vs. network funded).

34. Fitchett, Delbert (1999), "Bank for Agriculture and Agricultural Cooperatives (BAAC), Thailand (Case Study)", *Challenges of Microsavings Mobilization-Concepts and Views from the Field.*

Profiles BAAC's organizational structure (state bank), savings products & governance structure; savings products, product design & roll-out; management capacity; regulatory & supervisory framework; and cost analysis (transaction costs of savings program, financial costs and cost of mobilization).

35. Hannig, Alfred (1998), "Successful mobilization of small and microsavings: Experiences from seven deposit-taking institutions", Presented at *Innovations in Micro-finance for the Rural Poor–Exchange of Knowledge and Implications for Policy, Ghana,* November.

Draws on the same case studies his other papers.
P15: Ways of reducing administrative costs of small savings:
Lean structure-use min. staffing and infrastructure
Accountability and incentives for increasing operational efficiency-"profit center organizations" (?) in branches as in BRI, BAAC etc. increase the transparency of costs and instill accountability
Streamlining of operations-computerize operations, simple design of savings products
Outsourcing and networking-access support structures such as one's holding company to do certain admin tasks, private consultancy , or alliance with eg. commercial bank

36. Maurer, Klaus (1999), "Bank Rakyat Indonesia (BRI), Indonesia (Case Study)", *Challenges of Microsavings Mobilization-Concepts and Views from the Field.*

Profiles BRIs organizational structure (state bank), savings products & governance structure; savings products, product design & roll-out; management capacity; regulatory & supervisory framework; and cost analysis.

37. *Otero, Maria (1989), "A handful of rice: Savings mobilization by microenterprise programs and perspectives for the future", Accion International: monograph no. 3.

38. * Robinson, Marguerite S. (1992), "The role of savings in local financial markets: The Indonesian experience", GEMINI Working Paper No. 33, November.

39. Wehnert, Ulrich (1999), "Rural Bank of Panabo (RBP), Philippines (Case Study)", *Challenges of Microsavings Mobilization-Concepts and Views from the Field.*
Profiles RBP's organizational structure (state bank), savings products & governance structure; savings products, product design & roll-out; management capacity; regulatory & supervisory framework; and cost analysis.

40. Westercamp, Chrstine (1999), "Féderation des caisses d'épargne et de crédit agricole mutuel du Benin (FECECAM), Benin (Case Study)", *Challenges of Microsavings Mobilization-Concepts and Views from the Field.*
Profiles FECECAM's organizational structure (credit union federation), savings products & governance structure; savings products, product design & roll-out; management capacity; regulatory & supervisory framework; and cost analysis.

41. Wisniwski, Sylvia (1999b), "Banco Caja Social (BCS), Colombia (Case Study)", *Challenges of Microsavings Mobilization-Concepts and Views from the Field.*
Profiles BCS's organizational structure (used to be owned by the Catholic Church; since 1991 it has been a commercial bank), savings products & governance structure; savings products, product design & roll-out; management capacity; regulatory & supervisory framework; and cost analysis.

42. Women's World Banking (1993), "Building strong credit and savings operations: Volume I".
Reports on the lessons learned by WWB affiliates over the last 12 years.
Includes training material on: building a savings program; staffing a credit & savings program; and cost-effectiveness and financial management.

43. Women's World Banking (1993), "Building strong credit and savings operations: Volume II".
Presents case studies and sample forms to use with training in the topics covered in Vol. I.

WHY SAVINGS MOBILIZATION IS TOO EXPENSIVE FOR MFIS & WHY SAVING MAY NOT BE A PRIORITY FOR THE POOR

44. Bredenbeck, Kristen (1997), "Savings Mobilization: Lessons from the Peruvian Municipal Savings Banks in Trujillo and Sullana", *Savings and Development*, 21(1).
Analyzes a Municipal Savings Banks' member survey. Data shows that low-income households often do not have a significant savings capacity, which means that a financial institution cannot rely primarily on the savings of low-income households. This is why more affluent savers are drawn into the membership base.

45. Herberto Olmos Olmos (1997), "Movilización de ahorros en mercados financieros emergentes (Serie Ahorro 1)", Fundación para la Producción (FUNDA-PRO), Foro de Microfinanzas, December.
Postulates that microentrepreneurs demand credit and will only be inclined to transfer this credit into savings deposits if interest rates paid on savings were higher than the profitability resulting from investing in their business (p14). Since this is not the case in Bolivia, savings is not believed to be considered a priority by the poor.

46. Rosales (2000), "Ampliación del Marco Normativo de las Microfinanzas", International Consulting Consortium.
Savings services provide an important potential source of funds for institutions and it is in this light that institutions should develop the proper technology for mobilizing savings. However, savings mobilization is not an area that the state should subsidize, or provide a legal framework that decides who is and who is not allowed to mobilize savings, esp. since this process would include unsafe institutions and because the sate cannot ensure long-term macroeconomic stability to safeguard savings.

47. Scmidt, Reinhardt H. and C.P. Zeitinger (1994), "Critical Issues in Small and Microbusiness Finance," International Project Consult, September.
Provides a critical account of the successful cases of savings mobilization, pointing to unique characteristics that are not shared by NGOs: BRI-UD is a successful case because the government guarantees its deposits. Argues that microsavings is too expensive; points to high interest rate costs. *Contrast this view with that of GTZ/CGAP, which foreshadows positive externalities associated with economies of scope between lending and savings operations.* Argues that microsavings do not provide a substantial amount of funds, despite offering market-driven interest rates, citing the case of the Peruvian municipal savings banks. Argues that an institution must first be able to cover costs of its lending operations before considering expanding into savings services.

MISCELLANEOUS

48. Johnson, Susan and Thalia Kidder (1999), "Globalization and gender-dilemmas for microfinance organizations", *Small Enterprise Development*, 10(3).
Argues that women have a great need for liquidity and risk management in their household role ("reproductive labor"); savings products allow them to achieve this.
Not all of the poor are "budding entrepreneurs..., perhaps it is access to a savings account, which enables better money management" (p6).
Argues that there is a need for a savings product that allows women to deposit money and have complete control and confidentiality over their finances.

49. MicroSave Africa (1999), "Savings as an Instrument for Poverty Reduction", Workshop facilitated by the UNDP's Special Unit for Microfinance(SUM and UNDP Africa, October.
Discusses the potential role of postal savings banks as vehicles for savings mobilization in Africa. Notes the success of the Japan Postal Savings Bureau.

50. Vogel, Robert and Dale W Adams (1997), "Old and New Paradigms in Development Finance", *Savings and Development*, 22(4).
Compares and contrasts the directed-credit with the financial market schools of thought by discussing each paradigm's position on: problem definition, developmental role of financial markets, perception of the end-users (clients), sources of funds, etc.

51. World Savings Banks Institute (2000), "Report on the 6th Africa Regional Group Meeting of the World Savings Bank Institute", Arusha International Conference Center, March.

Discusses the role of postal savings banks in Africa.

52. Paxton, Julia and Cécile Fruman (1997), "Outreach and Sustainability: A Comparative Analysis of Savings-First vs. Credit-First Institutions", *Sustainable Banking with the Poor.* World Bank, January.

Examines the performance of CF and SF institutions in reconciling sustainability and outreach to excluded groups, including women, rural communities, the poor and the illiterate. Savings-led programs were successful in reaching rural clients

53. United States Agency for International Development (1991), *Mobilizing Savings and Rural Finance: the A.I.D. Experience*

Discusses problems, progress and lessons learned from projects sponsored by USAID, focusing on the experiences in Honduras, the Dominican Republic, Bangladesh and Niger.

World Council of Credit Unions, Inc.
Savings Best Practices

Attachment 5

Savings Best Practices: RCUP Credit Unions in Nicaragua

SAVINGS BEST PRACTICES: WOCCU-NICARAGUA'S RURAL CREDIT UNION PROJECT (CASE STUDY)

February 24, 2001

By N. Gons
WOCCU

Savings Best Practices Project
LAG-G-00-00-00027-00

THIS IS A WORKING DRAFT, PLEASE DIRECT ANY COMMENTS TO
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"People here don't save. They are poor — they don't save." -RCUP CU Manager

INTRODUCTION

In 1996 World Council of Credit Unions, Inc. (WOCCU) received funding from the United States Agency of International Development (USAID) to implement the Rural Credit Union Project (RCUP) in Nicaragua. RCUP's objective has been to assist Nicaraguan credit unions with an interest in reforming their operations in order to become financially sustainable and hereby expand their scope and scale of financial services. The crux of RCUP-led credit union reform was to transform participating credit unions into financial intermediaries who mobilize voluntary savings from the public.

None of the Nicaraguan credit unions participating in RCUP (RCUP CUs) mobilized voluntary savings prior to affiliating to RCUP. Instead, the extent of their savings operations was limited to collecting forced "savings", which served both as a source of institutional capital and a source of liquidity. **The objective of this report is to document how RCUP CUs evolved from institutions practicing forced savings into institutions whose primary source of funds are voluntary withdrawable savings from its members.** Section I will discuss the institutional requirements that must be in place before mobilizing savings. Section II will discuss savings products, including pricing and promotion of savings products. Section III will discuss prudential savings management.

RCUP CUs had to "start from scratch" and, with relatively little funds evolved over the last 4 years from very small (1,600 total members at RCUP inception) and rudimentary CUs (operating at a loss and suffered from delinquency rates as high as 50%) into financially sustainable institutions (Subsidy Dependence Index decreased in 12/18 RCUP CUs) that are rapidly growing in voluntary savings mobilization (real growth in voluntary savings was 390% in 1997, 181% in 1998, 315% in 1999 and 90% in 2000).

The case of savings mobilization in RCUP CUs is exemplary for all financial institutions that are considering or expanding savings services to the poor. As of June 2000 RCUP CUs have 2 savers/borrower. The average voluntary savings deposit is US$116, ranging from a low of US58$ to a high of US$196. Noteworthy is that the median savings deposit is US$32; half of all savings accounts are for amounts less than US$32. RCUP CUs' experience with this depth of savings is services commonly referred to as microsavings (this data corresponds to 10 RCUP CUs, cited from *The Road to Jinotega*).
MORE RECENT DATA?

> The most recent inflation rate reported by the Central Bank of Nicaragua is 11.81% in August 2000. RCUP CUs have used the Central Bank's inflation estimate; RCUP business plan starting in 6/30/99 lists inflation as 13.1%, which is equal to the inflation rate reported by the Central Bank for this month. However, RCUP has estimated inflation to be higher than the BCN suggests it thinks; RCUP business plans estimate inflation to be 17% until 6/30/01.
> The national devaluation adjustment (deslizamiento) is determined by the Central Bank of Nicaragua, and is currently 6%.
> The exchange rate is currently at 13.3C$/1US$.
> MENTION BANKING SECTOR'S INSTABILITY
>
> Local context info.: illiteracy/education (summarize in relevant sections eg. (marketing)

I. INSTITUTIONAL PRECONDITIONS FOR MOBILIZING SAVINGS

By agreeing to participate in RCUP, credit unions had to not only change their institutional vision, they had to reform and adopt a set of policies and procedures before they could even consider extending their financial services to include voluntary savings mobilization. This process of institutional preparation is undoubtedly the most challenging for any institution wanting to offer voluntary savings services.

INSTITUTIONAL VISION

Pre-RCUP CUs had received significant support from external funds, granted by international donors and national organizations (INSERT FIGURES). Institutional dependence on external capital lasted for as long as 20 years in some cases (INSERT NAMES). Their relationships with outside donors had sustained weak policies and practices, notably the share-to-loan practice that effectively led to a subsidization of borrowers on behalf of savers. Indeed, credit union members were encouraged to save for the sole purpose of obtaining a loan while savers were penalized for saving. The repercussions of this practice can be generally stated as creating a borrower-dominated structure whose governance mechanisms did not curb weak credit union policies and practices. Thus weak credit union policies remained and resulted in perpetual liquidity shortages and high delinquency rates (see *The Road to Jinotega, Part II* for more elaborate discussion). Instead of addressing structural deficiencies, credit unions sustained mediocre operations by borrowing increasing amounts of funds from external sources, exacerbating their overall dependency on outside funds.

As credit unions agreed to participate in RCUP, they committed to implementing voluntary savings services and had to change their institutional vision accordingly. In order to establish an internal framework that would lay the groundwork for prudential savings mobilization, RCUP CUs had to execute a radical reform of policies and procedures. This reform included instituting a whole new set of policies and procedures that forms the framework for prudential savings mobilization (such as implementing an array of financial disciplines) as well as transforming existing policies (such as its lending methodology in order to apply a more sophisticated credit methodology that is both more stringent and more open to all members of the public).

Contemporaneous with a redirection of internal orientation, RCUP CUs had to incorporate an outward-oriented vision in their overall operations. It is relatively easy to find a demand for credit; it is relatively difficult to conjure members' trust to deposit their savings in one's financial institution. Mobilizing voluntary savings required more extensive marketing, including the creation and implementation of a strong and professional institutional vision as well as direct marketing about savings services. First and foremost, RCUP CUs had to convey their ability to manage and safeguard their members' savings, mainly through improving their institutional image. Furthermore, as voluntary savings mobilization was to become the motor of credit union growth, RCUP CUs had to proactively reach out to their communities.

Proactive outreach was new to institutional vision; before committing to a savings-driven development model, credit unions had felt virtually no need to grow membership since they had focused on lending while suffering from liquidity shortages. An outward-oriented vision required adding a marketing component, which became an integral part of RCUP CU operations.

"Under the old bylaws we could not meet the disciplines and we could not mobilize [voluntary] *savings. In the future we will need to make more adjustments."*-RCUP *Manager (Iaguei & Avances)*

<u>*Legislation Governing Credit Unions in Nicaragua*</u>

National level: See Rosales for a summary of Nicaraguan legislation that enables some financial institutions to mobilize savings and others to not.
Legal Constraints:
Financial cooperative members must be at least 18 years old.
Financial cooperatives are not allowed to offer checks.

STRUCTURAL REFORM

Bylaw Reform

Before implementing RCUP CUs' new institutional vision, it had to first be defined in the credit union bylaws. The objective of bylaw reform was to define a more (1) efficient organizational structure, (2) establish financial disciplines and internal controls that form the framework for prudential savings mobilization.

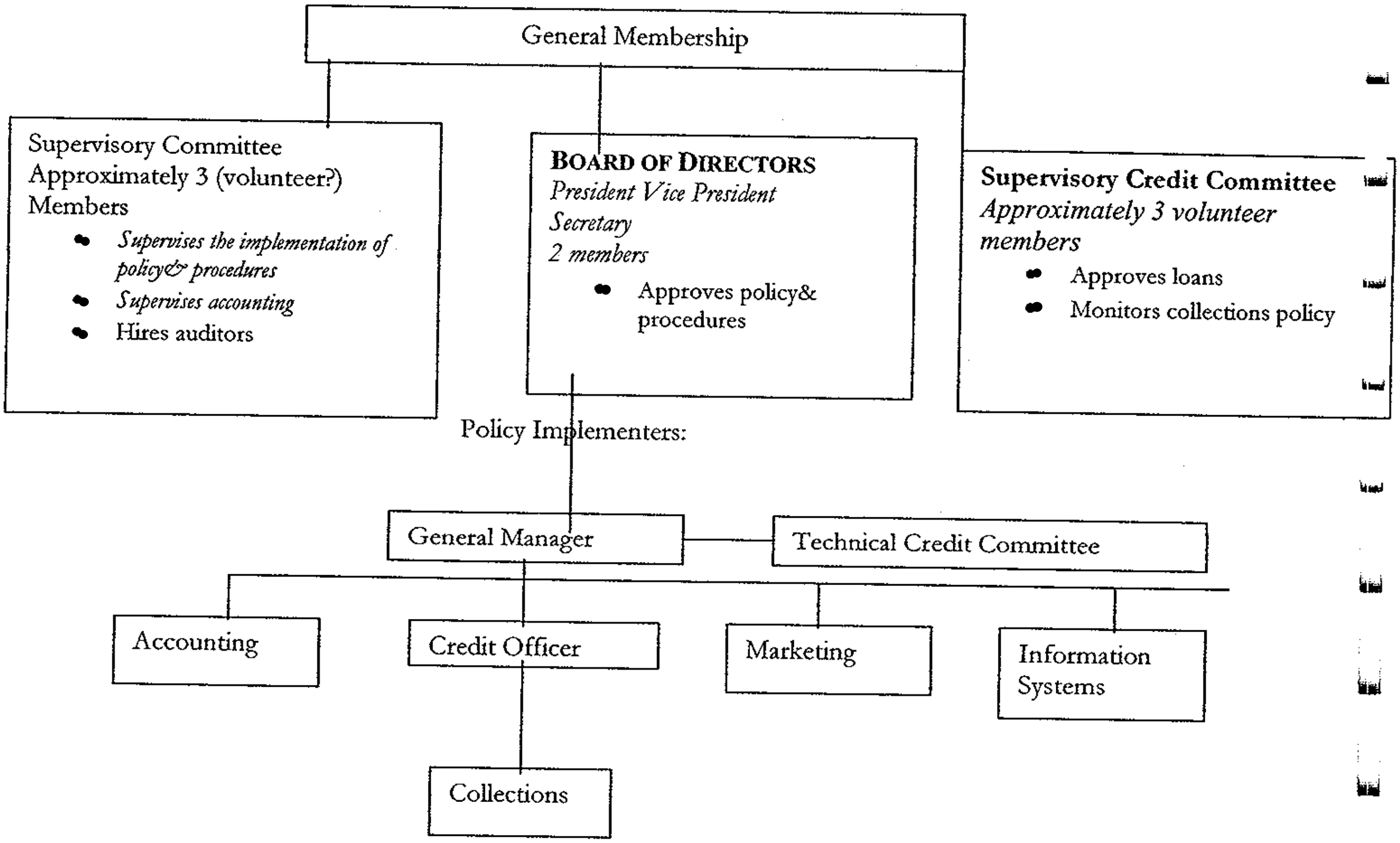
Creating a more efficient organizational structure

The new bylaws created a more efficient organizational structure by classifying functions into implementers and policy- makers and allocated the roles and responsibilities of each function according to these two categories. [Furthermore, credit union staff that had been composed of member volunteers were supplemented with members serving as volunteers were replaced by formally trained professionals]=not a product of bylaw reform

Before RCUP
INSERT

New Bylaws formulated by RCUP

Policy Makers:



"*At first it was very difficult to convince people of the changes* [in the bylaws]. *But our old bylaws required a share account of C$100 —people wanted withdrawable savings.*"-RCUP CU Manager (Avances)

Note that most RCUP CUs have an average of 4 employees: a Manager, a teller, a loan officer and an accountant. The new Bylaws accounts for future growth and therefore has defined roles and responsibilities as if there were one person dedicated to each listed function. At this time, however, many RCUP CUs cannot afford to hire one full time staff member for each function. For example, the loan officer may also be in charge of collections and marketing functions.

Process/Challenges

Reforming credit union bylaws was a very arduous process. It required extensive deliberation between the individual credit unions and RCUP staff, as well as lobbying for legal approval; RCUP's Managers and full-time legal expert led consultations with national legal bodies, such as DIGECOOP and the Superintendency of Banks.

Effects of new institutional vision and structure:

Credit union membership eligibility: The new Bylaws broadly define credit union membership to include all Nicaraguan residents above 18 years old are eligible to become RCUP CU members.

More member-oriented: Prior to bylaw reform, the membership application process had a lengthy approval procedure. The new Bylaws allow the Manager to approve a new member, making membership at the credit union more appealing and effective to newcomers (see Appendix A).

Demand-driven: Under the new Bylaws, policy decision was determined by market conditions as opposed to the opinions of credit union Board of Directors. In other words, the institution became more demand-driven.

Balanced financial intermediary: Over time net savers became represented on the Board of Directors and Committees, hereby creating a more balanced intermediary vs. a borrower-dominated intermediary. As the credit union's source of funds is increasingly made up of its member's savings, the institution will be more responsive to its members needs (as opposed to donor's needs).

Improved Operational Efficiency: As RCUP CUs were in the process of implementing financial disciplines they had to become more efficient. As RCUP CUs (all of which operated at a loss before participating in RCUP) had to allocate funds to loan loss provisions, liquidity reserves, institutional capital reserves they were in effect "forced" to become more efficient and meet the operating cost discipline.

Establishing a framework for prudential savings mobilization

Instituting Financial Disciplines

In addition to strengthening the credit union organizational framework, credit unions had to drastically reform their policies and procedures before they could consider mobilizing savings. More specifically, credit unions had to institute a set of financial disciplines that serve as a protective framework for member savings. Instituting financial disciplines is imperative for a community financial intermediary that does not benefit from national deposit insurance schemes. Although financial disciplines do not replace the need for a deposit insurance fund, strict adherence will allow for prudent savings mobilization.

The requisite financial disciplines stipulated in the new credit union bylaws are:

Financial Discipline	RCUP	Pre-RCUP
Strict calculation and control of delinquent loans	Delinquency must be calculated as the outstanding balance of the delinquent loan, regardless of the number of payments that are actually missed. Delinquency must remain 5-10% on new loans. (In order to meet this discipline, credit unions had to begin to track and report on delinquency on a regular basis (DEFINE REGULAR).	Delinquency was calculated as the quantity of the payment that was missed instead of the entire loan principle. No targets for delinquency control
Provision for loan losses	Must provision 35% of total loan value if the loan has been delinquent for less than 12 months; a credit union is to provision 100% of total loan value if the loan has been delinquent for less than 12 months	Non-existent
Loan charge-offs	Loans that are delinquent for more than 12 months must be removed off of the balance sheet. After this, legal collections continue	Non-existent
Capitalization	Must hold 10% of total assets in reserves.	Non-existent
Liquidity reserves	Must allocate 25% of withdrawable savings to liquidity reserves. This was increased to 30% during the banking crisis early 2001.	Non-existent
Control of Operating Costs	Must maintain operating costs less than 8% of total assets Must limit non-earning assets for 7% or less of total assets	No defined parameters

Asset-liability management?
As more financial products are offered, the practice of asset-liability management becomes an important component of savings management. INCLUDE IN SAVINGS MANAGEMENT SECTION

Controlling Delinquency

"We had calculated our delinquency at 20%. When we used WOCCU's calculation, we were at 50%. We had to charge off so many people, I though I would go under, "
-Integral

"We had calculated out delinquency to be approximately 17%, when we used RCUP's method it was approximately 89%; the latter is more transparent."-Económica

"The biggest obstacle for us to adopt WOCCU's calculation of delinquency was to explain to members that if they missed one payment, the collections officer was coming."-Iaguei

"In 1996 we had 20% delinquency, in 2000 we had 4.5%"-Avances

Meeting the capitalization discipline (10% of total assets in capital)

"It was more a matter of allocating funds to reserves than a matter of reducing operating costs." –Integral

"We had not capital, only shares."-Avances

"Before joining RCUP, we were not allocating finds to reserves because we focused only on lending. So all of our funds were placed in loans. In 1998 we managed to have 15% and in 2000 we raised this to 30% because of the banking crisis." -Iaguei

"We had gotten a US$50,000 donation and we used these funds to capitalize our credit union. This donation helped us a lot."-Económica

Provisioning for loan losses

"Once we understood why this is so important, we did it."-Integral

"We had approximately C$20,000 and we had to write off approximately C$7,000.

Controlling operating costs

"I first had to add costs because I had to recruit new staff in order to accomplish all the requirements to meet the disciplines."-Iaguei

Underlying Policies and Procedures

The underlying policies and procedures that had to be in place in order to be able to achieve the requisite financial disciplines are:

Accounting system

INSERT examples of before and after

Accounting systems had to be changed in order to record data associated with the financial disciplines.

"Adopting the new accounting system was really really difficult. It took about a year to accept it. Once we understood it, we agreed that it was better than our previous accounting system."

- RCUP CU Manager (Integral)

"Adopting the new accounting system was simple."-RCUP CU Manager (Iaguei)

Avances had received funding and from the Finish government and PAMIC. This funding, in part, gave this credit union an accounting software program and 2 computers. Participating in WOCCU required going back to manual accounting. Since they did not want to go backwards, they were hesitant to participate in WOCCU's accounting system. Their accounting system did not measure delinquency according to WOCCU's definition that includes the entire loan principal as the total amount considered delinquent. *"We were underreporting our financial status."*-RCUP CU Manager

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Stricter Loan Approval and Collections
INSERT LOAN APP. BEFORE&AFTER

"One of the biggest obstacles working with RCUP was managing the loan portfolio. And although we had an improved loan application, we had to explain to our members that the share leveraging days are over and that it was important that we build a solid financial institution. They had to understand that this was why we required a **factibilidad de pago** and their loan guarantee after their first payment was missed. We explained our new policies in our Annual General Meeting (AGM), which is attended by approximately 65% of members." –Economica

At each AGM the rights and responsibilities of the members are reviewed. Now we have a rule that only those who attend qualify to enter the credit union´s raffles.

The government during the 1980's allowed people to default on their loans. I was like a lawyer that had to make a case as to why it was crucial to have timely payback of loans. For those members that do not have a mortgage, we accept a contrato de prendas, a factura of their sewing machine (for tailors, a prenda del maquina. These receipts etc. are notarized and they are recorded in the Public Registry.

"We only had one loan officer who was also in charge of loan collections. We decided to educate our members about the importance of paying back loans. The loan officer would give speeches explaining our more thorough loan evaluation. At first members were taken aback by all of the questions we asked in the new lending methodology. But we kept explaining, to individuals that came to the credit union and at our annual general meetings, which is attended by approximately 20% of our members."-Integral

As an institution begins to mobilize savings, every bad loan places a risk on member savings. It is therefore imperative to maintain a healthy loan portfolio. As stipulated in the financial disciplines, RCUP CUs had to re-define delinquency and maintain delinquency at 5-10% of total loans. In order to curb loan delinquency, RCUP CUs' lending methodology changed from a loan-to-share practice to a risk-based credit methodology. The latter more accurately evaluates repayment capacity; loan eligibility is based on an individual's capacity to repay the loans, his/her repayment history and collateral. COMPLETE

Lending Methodology

RCUP	**Pre-RCUP**
Borrowers were evaluated according to their capability to repay the loan, by looking at his/her income stream and evaluating the risk associated with the activity or return associated with the member's investment.	Borrowers were evaluated according to the amount s/he held in his/her share account.

In addition to improving its lending methodology, RCUP CUs focused on diversifying their loan portfolios by economic sector, size and term structure. Furthermore, increased efforts were devoted to loan collections.

"*I was skeptical at first, but by 1998 I believed in WOCCU*"-Avances

Strengthening Institutional Image

The synergy between internal and external soundness transformed these small dependent credit-driven organizations into community financial intermediaries.

Concurrent with creating a strong internal framework by adopting financial disciplines and improving policies & procedures, RCUP CUs were engaged in a strategy to strengthen their external institutional image. As very small and oftentimes obscurely located credit unions housed in rundown buildings, this entailed moving to more visible locations as well as renovating physical infrastructure. Central to the upgrading of physical infrastructure was using a unified logo and color scheme that laid the foundation for a credit union system. The image of a sound system further creates public confidence and therefore supports savings mobilization initiatives.

Upgrading physical infrastructure was the first phase of RCUP CUs' marketing strategy and was wholly financed by RCUP for the first year, if and only if RCUP CU met all the requisite financial disciplines and was reforming policies and procedures accordingly. The simultaneous focus of internal and external strengthening allowed for an effective incentive system; those who improved internal operations visibly saw improvements in their credit union.

Fostering Professionalism

The renovated physical infrastructure contributed to fostering a professional attitude in RCUP CUs. Most credit unions introduced uniforms. Some RCUP CUs, such as Professional and Iaguei, chose uniforms to be blue and green, identical to the colors of the new logo and buildings. Others, such as Avances and Económica chose gray and black and white respectively, since these were perceived to be more professional colors. Professionalism was accompanied by an improvement in staff morale; all RCUP CUs surveyed noted that staff morale increased significantly during the period of internal and external strengthening.

"*We did a 364º turn. We became more professional, had more respect. The community had more confidence in us. At first they tested if we would really allow them to withdraw their savings.*"-*Económica*

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"Once you have the disciplines in place, it is easy to mobilize savings."-RCUP CU Manager

II. SAVINGS PRODUCTS

On average, credit unions spent the first 2 years preparing the institution to be able to mobilize voluntary savings. When the institutional preconditions have been met, the credit unions begun to offer savings products.

Section II will describe savings products, including pricing and promotion strategies. This section will include a general discussion as well as a case study presentation of 5 RCUP CUs that are representative of RCUP CUs both geographically and occupationally.

ELIGIBILITY AND REQUIREMENTS TO SAVE AT RCUP CUs

Eligibility

All Nicaraguan citizens above the age of 18 are eligible to become a member of any of the RCUP CUs. Any Nicaraguan citizen under the age of 18 can affiliate herself via a legal guardian who is a credit union member. This distinction has to be made because of legal constraints governing financial cooperatives; *it does not reflect a strategy.*

Paperwork requirements for membership are simple and are standardized for all RCUP CUs. All new members must fill out an application request (*Solicitud de Ingreso*, see Appendix A). This form requires one form of identification (national identity card, social security, drivers license or passport), and a brief description of personal information. The form also asks for one beneficiary to be identified.

This form must be signed. In cases of illiteracy a fingerprint may be used in lieu of a signature. There is always a staff member available to guide a new member through the application in cased there are any questions or in case of illiteracy.

"I was recently told by Juan that I shouldn't accept fingerprints. (by order of not DIGECOOP but a different legal entity)"
-Económica

BREAKING THE SHARE LEVERAGING TRADITION

RCUP CUs were in the habit of using member shares as a reference point of loan disbursement. In other words, members had to have a share account, which historically did not pay an interest rate. In effect, members faced an additional cost for borrowing and were disincentived to save.

One of the greatest obstacles to change this practice was convincing credit union leadership that reallocating share funds to voluntary savings accounts would not result in a decapitalization of the credit union. The strategy applied in Nicaragua was creating 3 fixed term deposits 1 year, 2 years, 3 years. One third of total shares were placed in the 1st year account, 1000 in 2nd year account, 1000 in 3rd year account. The goal was to mobilize at least the equivalent of 1/3 of total shares during the first year, another 1/3 the 2nd, and the third years. The objective of this was to give members ownership and control of their savings. The gamble was could they do this?

Membership Requirements

All RUCP CUs require members to purchase a share in the credit union. Shares are treated as any other savings account, thus it earns interest at the end of each month. In most cases it earns a higher interest rate than other accounts. The member can choose to which account s/he wants the interest earned on his/her shares to accrue. Some RCUP CUs may require a minimum amount to be held in a savings account. For example, at Iaguei members must place a minimum of C$50 in a savings product in addition to buying a share.

SAVINGS PRODUCTS AT 5 RCUP CUs (CASE STUDIES)

RCUP CU, RCUP CU Manager	Location: (dept., city)	Hours of Operation	Approximate No. of other local financial service providers	Unique Characteristic
Cooperativa Financiera Profesional Ms.Flor de M. Perez	Masaya, Masatepes	M-F 8:00-12:00, 1:00-4:30 Sat. 8:00-11:30		
Cooperativa Financiera Integral Ms. Clementina Escorcia	Matagalpa, Sébaco	M-F 7:30-5:30	5 commercial banks 8 micro-credit organizations	Most members are agricultural producers Sébaco is one of the regions that suffered tremendous damage due to Hurricane Mitch
Cooperativa Financiera Iaguei Ms. Rosa M. Alvilez	Chinandega, Corinto	INSERT M-F Sat.		Most members are female market vendors
Cooperativa Financiera Avances Mr. Enrique Vargas	Chontales, Sto. Tomas	INSERT M-F Sat.		Largest RCUP CU Region relatively more affected by the armed conflict between the Sandinistas and the US-backed Contras (1979-1989)
Cooperativa Financiera Económica Ms.Christiam Arauz	Madriz,Somoto	M-F 8:00-5:00 Sat. 8:00-11:00		Operating in one of the poorest regions of Nicaragua

***History of Financial Products and Services Offered*[ii]**

Financiera Profesional

Loans	Interest Rate	Commission	Start Date	Savings	Interest Rate	Start Date	Others	Interest Rate	Start Date
Yes	48%/year	2% flat	2/75	Yes	17-19%/year	11/98	1)Savings in US$ 2)Rent chairs 3)Make fotocopie	1)7-4%/year 2)C$.50/chair 3)C$.50/page	1)12/98 2)7/97 3)End of 1997

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							s		

Financiera Integral

Loans	Interest Rate	Commission	Start Date	Savings	Interest Rate	Start Date	Others	Interest Rate	Start Date
Yes	36.72%/year	None	6/75	Yes	19-21%/year	4/94	Savings in US$	10%/year	4/94

Note: Savings activity before 1996 was forced savings. In 1998 Integral began to mobilize savings through its voluntary savings products.

Before 1996 no voluntary savings products were offered at Integral. Instead savings were used as a means to determine the maximum size of a loan and act as a source of collateral. Integral's loan-share lending practice was 5:1. Since Integral entered into WOCCU's Rural Credit Union Program (RCUP) in x, the practice of forced savings and loan-share lending practices has been abandoned.

Savings mobilization did not occur immediately at Integral. They were stagnant for approximately 2 years. **How much of this was due to the fact that they still had to get their house in order? Were RCUP CU allowed to mobilize before disciplines were in place? The region in which Integral operates was one of the more severely affected by Hurricane Mitch (is there a causal relationship here?).**

Financiera Iaguei

Loans	Interest Rate	Commission	Start Date	Savings	Interest Rate	Start Date	Others	Interest Rate	Start Date
Yes	5%/month	1% flat	10/95	Yes	18-30%/year	9/95	1)Loans in US$ 2)Savings in US$	1)2%/year 2)4-6%/year	1)1998 2)1997and 1999

Had and still have a Christmas savings account.

Financiera Avances

Loans	Interest Rate	Commission	Start Date	Savings	Interest Rate	Start Date	Others	Interest Rate	Start Date
Yes	1 and 2.5% /month	1% flat	1975	Yes	12-14%/year	1996	1)Savings in US$ 2)Fidelity bonds	1) 7-9% /year 2).5%/month	1) 3/98 2) 3/98

Financiera Económica

Loans	Interest Rate	Commission	Start Date	Savings	Interest Rate	Start Date	Others	Interest Rate	Start Date
Yes	24-42%/year	2% flat	5/94	Yes	18 and 22%/year	5/2000	1)Savings in US$ 2)Fax&phonecalls 3)Fidelity bonds	1) 8%/year 2)the cost 3)2% flat	1) 5/00 2) 5/00 3) 9/00

Savings Products

All RCUP CUs have one required savings product and 3 types of voluntary savings products. It is important to note that the former does *not* fall into the same category as forced savings. Rather, members are required to purchase a share account in order to become a member. All RCUP CUs treat share accounts as any other savings product. RCUP CUs' voluntary withdrawable savings products can be categorized into fully and semi-liquid products. Fully liquid savings products are passbook savings and youth accounts; semi-liquid savings products are fixed-term deposits.

All savings products earn competitive interest rates that are on average one percentage point higher than commercial bank rates. The interest earned on all types of savings accounts is capitalized to the member's savings account at the end of each month, calculated on an average daily balance. A member can come in the first 15 days of each month and the teller will disclose how much the member has received interest payments.

Share Accounts

In addition to having to meet the eligibility requirements listed in SAVINGS PRODUCTS /ELIGIBILITY, all RCUP CUs require members to purchase a share in the credit union. Shares are treated as any other savings account; at the end of each month share accounts earn interest. In most cases share accounts earn a higher interest rate than other savings accounts.

The member can choose to which account s/he wants the interest earned on his/her shares to accrue to. The member receives a share certificate that assigns the new member his/her member number (see the first set of boxes in Appendix B). The share certificate allows the member to choose an account to which his/her interest payments are credited to (see second set of boxes in Appendix B). For example, a member can choose to have his/her interest earned on his/her savings to be credited to her passbook account.

RCUP CU	**Amount of Required Share Purchase**	**Interest Rate Earned**
Profesional	C$50	19%
Integral	C$70	19%
*Iaguei	C$50	18%
Avances	C$100	19%
Económica	C$100	18%

*Members can withdraw amounts that are in excess of the required minimum.

Withdrawable Savings Products

RCUP CUs offer two types of withdrawable savings products that are fully liquid: *passbook savings accounts* and *youth savings accounts*. *Passbook savings accounts* are the most commonly used savings product. *Youth savings accounts* offer the same interest rates as on non-youth accounts, even though the costs associated with this product tends to be higher since account balances tend to be lower. "The balances of youth savings accounts tend to be very low and this is relatively the most expensive savings product." However, since youth forms a crucial part of RCUP CUs' potential market RCUP CUs want to offer the most attractive rates to this market niche. Note that 40% of the Nicaraguan population is between 0-14 years old (CIA Factbook 2000) INSERT different source. As Profesional's Manager said, "We want this group to feel like they are treated equally in our credit union by paying them the same interest rate that adults receive on their savings accounts." She added "even though the youth accounts have a higher cost right now, once these accounts grow this will even out." In other words, young members do tend to have lower savings balances but, if they remain members throughout their lifecycle, these low balances are likely to grow into larger ones. Furthermore, as Económica's Manager commented, we would not want the parents to place their children's money in their account because they receive a better interest rate.

C.F. Profesional

	Passbook savings		Youth savings	
	C$	US$	C$	US$
Minimum deposit required to open account and to receive interest	50	20	5	5
What are the limits on withdrawals?	6/month		6/month	
*Annual Interest Rate	17.9%	7%	17.9%	7%

*Note: the interest rates includes the 6% monetary adjustment (deslizamiento).

C.F. Integral

	*Passbook savings		Youth savings
	C$	US$	C$
Minimum deposit required to open account and to Receive interest	100	10	5
*What are the limits on withdrawals?	No limits		No limits
Annual Interest Rate	19%	8%	19%

* *For those that want to make a large deposit, this rate is negotiable*

***For those members that make more than 3 withdrawals per week, they do not earn an interest rate, "they are using the account as a checking account".*

A formal limit on withdrawals has not been established at Integral because in general members do not make more than 6 withdrawals per month.

C.F. Iaguei

	Passbook savings		Youth savings	
	C$	US$	C$	US$

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Minimum deposit required to open account and to receive interest	100	20	10	5
What are the limits on withdrawals?	No limits		No limits	
*Annual Interest Rate	18%	4%	18%	4%

**They write the deslizamiento separately (+6%)*

Iaguei classisfies members according to stability in their savings accounts. Ahorro corriente can be used as a loan guarantee. Shares are not considered in loan evaluations.

If a member comes with an amount of 10,000 or larger s/he may negotiate to receive a higher interest rate, generally 5 basis points higher than the regular interest rate.

In addition to these two savings products, Iaguei offered a Christmas savings product before the project and still offers it today. However, they only have approximately 20 accounts.
They are currently focusing on increasing their youth savings accounts, and may consider focusing on increasing this product when they have completed this goal.

Christmas Savings		
	C$	US$
Minimum deposit required to open account and to receive interest	50	10
Term	6 mo.	
Annual Interest Rate	18%	4%

C.F. Avances

	Passbook savings		Youth savings	
	C$	US$	C$	US$
Minimum deposit required to open account and to receive interest	100	20	5	1
What are the limits on withdrawals?	10%/total savings		10%/total savings	
*Annual Interest Rate	18%	7%	18%	7%

* *Write the monetary correction separately for córdoba denominated accounts, i.e. 12%+6%*

Withdrawals significantly increased during the banking crisis.

C.F. Económica

	Passbook Savings		Youth Savings	
	C$	US$	C$	US$
Minimum deposit required to open account and to receive interest	100	20	50	10
*What are the limits on withdrawals?	6/mes	6/mes	6/mes	6/mes

*Annual Interest Rate	18%*	8%	18%*	8%

** If the member notifies the credit union one day prior to withdrawal, then the credit union allows unlimited savings withdrawals.*
***Note: the interest rates includes the 6% monetary adjustment (deslizamiento).*

The credit union has 4 cases of passbook accounts with less than the required minimum; all have reasons deemed justifiable by the credit union.

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In addition to the fully-liquid withdrawable savings products described above, RCUP CUs also offer semi-liquid withdrawable savings products: *fixed-term deposits*. All RCUP CUs prohibit members to withdraw before the maturity date of their fixed-term deposit. However, in cases of emergency, RCUP CU Managers may allow partial or full withdrawal before the maturity date.

Profesional

Term	3 months		6 months		9 months		12 months	
	C$	US$	C$	US$	C$	US$	C$	US$
Min. Balance	200	100	500	50	500	50	500	50
Annual Interest Rate	17.5%	10%	18%	12%	18.5%	13%	19%	14%

At Profesional, the 12-month fixed-term deposit accounts may be used as collateral.

Profesional is considering adding a fixed term deposit account with a term of 24 months. The Manager noted that fixed-term deposits offer a stable source of funds for the credit union.

Integral

Term	6 months		9 months		12 months		> 12 months	
	C$	US$	C$	US$	C$	US$	C$	US$
Min. Balance	500	50	500	50	500	50	500	50
*Annual Interest Rate	20%	9%	20%	9.5%	20%	10%	20%	10%

Includes the yearly currency adjustment (deslizamiento).

In cases of emergency the member may be allowed to withdraw their deposits held in a fixed term account at no fee. Integral has recently allowed this in the case of a member that needed a sudden operation.

Integral offers relatively longer terms, which is a response to its membership, of which a large portion agricultural producers.

Iaguei

Term	1 months		3 months		6 months		12 months	
	C$	US$	C$	US$	C$	US$	C$	US$
Min. Balance	500	50	500	50	500	50	500	50
*Annual Interest Rate	18%	4%	22%	4%	23%	4%	24%	4%

**The yearly currency adjustment (deslizamiento)is written separately, i.e. 12%+6%.*

Members can withdraw fixed-term savings prior to the maturity date, but they will not receive any interest on their fixed term account.

Iaguei offers relatively shorter-term fixed loans, which is a response to its membership, which are predominantly market vendors.

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Avances

Term	3 months		6 months		12 months		> 12 months	
	C$	US$	C$	US$	C$	US$	C$	US$
Min. Balance	500	100	500	100	500	100	500	100
*Annual Interest Rate	18.5%	8%	19%	9%	20%	10%	10%	10%

**The yearly currency adjustment (deslizamiento)is written separately, i.e.12.5%+6%*

There is currently no policy on withdrawing money from a fixed-term deposit before the maturity date; these rare cases are evaluated individually to determine whether a fee is necessary or not.

For exceptional savers, interest rates are negotiable. Avances has one case where a member saved in large quantities of dollars, and was permitted to earn 10.5%.

All types of savings can be used as a form of a guaranty for a loan, given that no withdrawals are made on the savings account that is to be used as the guarantee. In the cases that savings are used as a form of collateral, it is mostly fixed-term deposits.

C.F. Económica

Term	3 months		6 months		12 months	
	C$	US$	C$	US$	C$	US$
Min. Balance	500	Nt*	500	Nt	500	
*Annual Interest rate	20%	7%	21%	7.5%	22%	8%

**The yearly currency adjustment (deslizamiento) is included.*

In case of withdrawing before the maturity date, the member has to pay 2% of his/her account balance.

Pricing Savings Products

Interest Rates

The primary tool used by RCUP CUs to determine their interest rates is the RCUP business plan. This is the tool that considers costs associated with savings products (such as marketing and administrative costs), as well as local variables (such as local bank rates and the national inflation rate). The business plan allows one to set an interest rate for savings products and project the effects that this will have on other products as well as overall operations. For example, for Profesional this year's interest rate on savings was 19%, which they used as the base for their fixed-term deposit rates. Currently RCUP CUs are working on developing a method to differentiate interest rate on different savings products (see APPENDIX F).

Most RCUP CUs monitor local bank rates monthly. Interest rates in the Nicaraguan banking sector have been relatively stable. Therefore, a monthly monitoring has been proven to be sufficient. Integral monitors interest rate movement at local financial institutions every six months. As every RCUP CU manager explained, "interest rates are relatively stable in Nicaragua." Iaguei is the only RCUP CU in our case study sample that monitors local banks' interest rates daily, although an adjustment in interest rates has never been necessary.

In cases of emergency, RUCP CU Managers can adjust interest rates in a timely manner. The Manager does need to get approval from the BOD. All RCUP Managers explained that they were considered the experts and the BOD generally would accept their suggestions, given that they could give a sound explanation justifying their choices.

Other factors considered when determining interest rates
The local competition's interest rates are the determining factor for RCUP CU interest rates. For example, Economica monitors the following financial service providers daily: BDF?, 2 NGOs, (FUNDENUSE) and (ACODEP).

RCUP CU Managers monitor 2 monthly publications in order to keep informed of national trends in the financial sector: the Central Banks monthly newsletter and the monthly newsletter published by La Fundación Internacional para el Desafío Económico Global , titled *El Observador Económico*. At this nascent stage of savings mobilization, costs associated with a specific savings product are not considered in interest rate determination. INSERT elaboration

Promoting Savings Products

Marketing Strategies
Effective marketing strategies have been the cornerstone of savings mobilization in RCUP CUs. RCUP CUs' marketing efforts can be summarized into three phases:
Phase I: Improving institutional image according to a unified image to convey a credit union system
Phase II: promoting savings services
Phase III: segmenting markets

During the first year of affiliation to RCUP, 100% of RCUP CUs' marketing expenditures were financed by RCUP, the second year this became a shared cost at 50/50, the third year 75% of marketing efforts were financed by RCUP CUs, compared to 25% financed by RCUP.

Phase I: Improving institutional image according to a unified image to convey a credit union system

RCUP CU	Name before RCUP	Location before RCUP	Location after RCUP
Profesional	Masatepe	Obscure and derelict	Visible
Integral	La Hermanidad	Obscure and derelict	High-transit
Avances	Avances	Did not move, had a derelict building.	Did not move
Iaguei	Iaguei	Obscure (in the back of a ferretería) and derelict	Own office
Económica	Comulmad	Obscure and derelict	Visible

Integral is one of the many RCUP CUs that moved from an obscure location to one of constant transit. The increased visibility and the successful completion of the upgrading of physical infrastructure was the first milestone to foster trust in the public.

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Económica was located in a small derelict wooden house. In 1994 Económica serviced 131 members. " *I always had hard times and was operating at a loss. In terms of savings, all of our savings were forced and served as loan collateral for the borrowers and as institutional capital for us. It was just Fransisco (?) and myself but I was determined, it was a personal and a professional mission.*

When RCUP came along, I wanted to see what they thought we were doing wrong. And if I really was doing something wrong, I wanted to know how I could fix it. For example we analyzed RCUP's suggestions about how to improve our accounting system and they were right, we were inflating our capital. In other cases we needed more convincing; for example RCUP's method of screening borrowers, of calculating delinquency, of provisioning for loan losses. After 3 years of seminars and workshops we were convinced...But I never thought that people here in Somoto [one of the poorer regions in Nicaragua] *could save.*"

Económica entered RCUP in 1997 engaging in internal and external institutional strengthening; current membership is 354 members. Assuming equally proportionate annual growth, this reflects a 90% annual growth in membership.
Growth came after our inauguration. The community had more confidence in us. People recognized our new appearance; they had seen the credit union in Sébaco [which is on the route to Somoto]. This also helped to foster confidence.

Phase II: promoting savings services

Marketing Strategy targeting Youth
In addition to marketing savings services to the public, RCUP CUs targeted children under 18 in order to promote their youth savings product.
RCUP assisted RCUP CUs with their marketing strategy targeted to Nicaraguan youth.
RCUP CUs explained to school principals and directors that they would like to present students with a brief summary about the importance of saving and how a credit union can help one achieve this. RCUP CUs tailored its message to a young audience by delivering its message via a series of skits performed by a clown. The clown explained the importance of savings to one's future, the ability to use savings as a means to plan one's future and the role of the credit union in helping all people save.

Marketing Tools
RCUP CUs' standard marketing tool for the public includes a brochure that describes the credit union and its products and services available to the community (see appendix H). Shirts and caps are also used as promotional tools.

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RCUP CU	Marketing Strategies	Marketing Channels	Budget for the year 7/2000-7/2001
Profesional	Raffles	Loudspeaker Local newspaper &radio	
	Presentations to youth (children up to 18 years)	Local primary and secondary school system	
Integral * This marketing strategy was abandoned after the Peace Corps volunteer left, since there was not sufficient labor power to continue this strategy.	Raffles	Pass out flyers when collecting loans, maximizing his time in the field (see Appendix).	C$6,000
	*Conducted workshops, together with a peace corps volunteer, gave workshops giving examples of a borrower and saver as a client that went to a bank vs. to a credit union.	Neighboring rural communities	
	Seek acknowledgement from local tv and radio.	Attend key community events.	

Iaguei	Raffles	Loudspeaker	C$ 35,000
	Awareness of financial services offered	t.v. radio during baseball games banners in the streets	
	Awareness of savings services tailored to the youth (children up to 18 years)	Primary and secondary schools	
	General Assembly	Loudspeaker	
Avances	Awareness of financial services offered	Local radio, esp. during sports events loudspeaker Attend sports events and pass out shirts and brochures Banners in the streets Are trying to get a commercial on t.v.	
	Awareness of savings services tailored to the youth (children up to 18 years)	Went to 7 schools	
Económica	Raffles	Loudspeaker Local radio Local television: an advertisement that appears at the bottom (cinta publicitaria) Banners in the street Attend community events (fiesta patronales). Attend sports events.	C$ 10,000
	Awareness of financial services offered	Loudspeaker Local radio Local television: an advertisement that	

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		appears at the bottom (cinta publicitaria) Banners in the street	
	Awareness of savings services tailored to the youth (children up to 18 years)	Went to all local schools except for 2. *In the pipeline: holding a raffle tailored to youth(with a bike as the main prize).*	
	Facilitating access to products and services.	Direct visits to households with deposit/withdrawal slips. The marketing staff takes the filled out and signed slips and the libreta, processes the transactions and returns it to the member.	

Note that loudspeakers reach all people, regardless of whether s/he can read, has a radio or a television. Baseball is the national sport. Usually raffles are held around Christmas time and Mothers Day, two influential holidays in Nicaragua.

In addition to marketing strategies, credit unions often give a small incentive to new members, such as a shirt, a cap or a raffle ticket.

"Our first raffle had a loss; people saved very small amounts. But now we have a lot of very small amounts [of savings]. For example, one month after our raffle held on 12/30/00, we closed with C$468,880. One month after this raffle, we closed with 476,517 [a 1.63% increase in this month]."*-Económica*

"Door to door visits are very important to attract new members. It is expensive but gives personalized attention to potential members and is very effective."-Económica

Marketing tailored to local conditions and institutional parameters

Integral
At Integral the credit official and collections agency absorbs most of the responsibilities of marketing. He explains that it took a long time for the community to develop enough trust in the credit union; savings mobilization has begun over the last 2 years. The loan officer spends 80% of his time out of the office with members. In addition to visiting members with delinquent loans, Pedro discusses the savings services offered at Integral. As the physical infrastructure improved, it became easier to conjure trust in community members. The credit union's affiliation with WOCCU, an international apex organization of credit unions also fosters confidence in the community that Integral is an institution capable of safeguarding community deposits.

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Raffles are very successful. A raffle/adult C$200, raffle/kid C$50. The products that are raffled off are expensive (T.v.), but they have covered their costs so far. Withdrawals after the raffles are minimal.

Iaguei
The Manager and another staff member do the loudspeaker advertisements. They also go directly to the households of potential members. At this point they have to travel to find more microentrepreneurs; all the microentrepreneurs located directly in Corinto are all members of Iaguei. In addition to microentrepreneurs, Iaguei considers the aduana a potential target group. Their marketing strategy targeting youth (see table) is regarded as attracting feasible group of potential members, despite that youth typically saves in small amounts. This reflects the attitude that mobilizing a lot of small accounts iw a feasible strategy.

Avances
We give the message that "we are here a great alternative to the banks."

Phase III: Segmenting Markets
Phase III of RCUP CU marketing strategy is to segment markets in order to sharpen their knowledge about their current and potential markets, which will allow for better marketing strategies and product development. Phase III has started in 2001.

Conceptual framework of current and potential market
Profesional
Currently Profesional's primary market is the community in Masatepe, where it is located. Flor defines this local market as being made up of various economically active sectors, salaried workers, entrepreneurs engaged in commercial activities of which virtually all are self-employed, and a small group of artisans. Visits have been made to neighboring communities, namely Nandome and Piadose but expanding outreach to other communties has not yet taken place on a significant scale. They are planning to target the more rural neighboring communities. The marketing approach in these neighboring communities is a house-to-house strategy, where Profesional staff approach households and provide those that are interested with the credit union brochure (see Appendix H) and answer any questions. Loudspeakers have also been used to promote awareness of the credit union and its financial services accessible to all. These house-to-house visits are carried out during business hours, which excludes those that work away from their house. Do we want recommendations here? Probably not

Integral
Integral has defined several niches in their local market, defined by occupation. Their strategy is to target strategic loci of the economically active population, whereby the limited marketing resources can result in a wide outreach. In the pipeline: speak with the Human Resources departments of the maquiladora sector.

Económica
Económica has defined several niches in their local market, defined by occupation and age:
Self-employed entrepreneurs engaged in commerce (comerciantes)
Coffee producers
Youth

Institutional incentives/Other Financial Services Offered
In addition to offering access, financial institutions can offer clients incentives to save.
Most RCUP credit unions offer members a savings life insurance, the remainder of RCUP CUs are in the process of implementing this product. If a credit union member dies before the age of 55,

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his/her beneficiary will receive 3 times the amount of his/her savings. If the credit union member is 55 years or older, his/her beneficiary will receive the amount equivalent to his/her balance at the time of death. Technical assistance to design and implement the life insurance product was given by RCUP, who received technical assistance from ICAA/MIS.

Observations of Members' Usage of Financial Services

Profesional
When asked to summarize member's usage of savings accounts, Flor summarized her credit union's members as a majority of savers with small balances and a minority of borrowers with little savings.

Integral
Members prefer withdrawable savings even though they are not withdrawing much. Deposits > withdrawals. Generally savers are savers and borrowers are borrowers. There are few borrowers and a lot of savers. They don't save a lot [quantity], but they save.

Miscellaneous Comments
Isabel, the President of the BOD at Integral is working with a group of indigenous women (they form an occupational collective); they have recently become members at Integral.

III. PRUDENTIAL SAVINGS MANAGEMENT

LIQUIDITY MANAGEMENT

RCUP CUs base their liquidity reserves on their daily cash follow, which they review on a monthly basis. RCUP CUs hold 15-20% of withdrawable savings as liquidity reserves. [During the Hurricane Mitch Crisis,]. During the bankruptcy of Banco de Café, they increased their liquidity reserves to 30% as proposed by RCUP.

> When the banks went bankrupt, we had a lot of withdrawals. For 15 days we did not make loans, only to members with a AA rating. -Iaguei

Integral holds 15% of withdrawable savings as liquidity reserves.
Due to distrust in the commercial banks, Iaguei holds only 15% of its liquidity reserves in the bank and 10% in its vault. These funds will be allocated more efficiently (i.e. interest-bearing) once the credit unions have formed a second tier institution. *EXPAND*

Deposits & Withdrawals

A member can withdraw from and/or deposit into his/her passbook and/or youth savings account during business hours. The member must have his/her passbook.

In order to make a withdrawal or a deposit, the member must fill out a deposit/withdrawal slip (see Appendix C). There are three copies of the deposit/withdrawal slip, one for the member, one for the teller and another for accounting. The teller marks the deposit or withdrawal in pen and then again with a typewriter. The teller then places her signature in the right margin of the transaction

Member Privacy
In order to ensure member privacy, RCUP CUs have rules that stipulate under which conditions third parties can withdraw and/or deposit from a member account.

	Conditions under which third parties request members' account information	Conditions under which third parties make withdrawals from a member's account.	Conditions under which a third parties make deposits to a member's account.
Profesional	None		
Integral	None		
Iaguei	None	When they come in with a signed deposit/withdrawal slip.	When they come in with a signed deposit/withdrawal slip.
Avances	None		
Economica	None	None	When they come in with a signed deposit/withdrawal slip.

Note that all cases in which a third party makes a transaction on behalf of a member are subject to signature verifications. In other words the third party is required to have a signed deposit/withdrawal slip, whose signature is verified by credit union staff. *(For further discussion, see Member Security)*

Restrictions on Delinquent Members

Profesional
In the case of delinquency, a member will not receive interest payments on their savings accounts, but will be able to make withdrawals from their account.
Integral
If the member is delinquent, then they still receive interest but they are not allowed to withdraw their savings.
Iaguei
If the member is delinquent s/he is not allowed to withdraw savings. The implementing process is as follows: If a member is delinquent, a sticker is placed on his/her member card. When the member comes in to withdraw money, the teller sees his/her delinquent status and refuses a withdrawal.
Avances
If the member is delinquent s/he will receive interest on his-her savings account(s). The member is only permitted to make a withdrawal if s/he is using the withdrawal to pay off his/her loan.

Económica
If a member is delinquent, s/he does not receive interest payments on his/her account. S/he is permitted to

Monitoring the Exchange Rate
[16/18 check] RCUP CUs that allows deposits in both local currency and US dollars, including Profesional, Integral, Iaguei

Profesional and Iaguei use the official exchange rate and monitor the exchange rate daily at their local bank. Integral uses the parallel market rate, which is lower than the official rate 13C$/US$ as of [ ]. When capitalizing interest, the daily rate is used to calculate the daily balance, and the rate of the last day of the month is used to capitalize the member's account at the end of the month.

withdraw from his/her savings account given that these funds are used to pay off the delinquent loan.

How is delinquency tracked so that the credit union knows when to refuse a withdrawal and/or decline interest payments? In Iaguei a tracking sheet is used (see Appendix). The tellers are quickly able to identify which members are delinquent, since orange stickers are placed on the member's ledger card if s/he is delinquent. In contrast, in a relatively smaller credit union such as Economica the manager knows which members are delinquent.

ACCOUNT MANAGEMENT

Inactive Accounts

Profesional does not charge fees on inactive accounts.

Integral: Accounts that have been inactive for more than 12 months are cancelled and placed into a cuenta por pagar. Then they are transferred into *other income* for the credit union. In all cases these accounts are of very small amounts.

Iaguei: We visit the member and explain our financial services. If that does not have an effect or if we do not find them, then we charge the balance to *other income.*

Avances: Dormant accounts are discussed at the AGM. Avances is interested in using the WOCCU manual and writing cards to members with inactive accounts. If the member corresponding to the inactive account is not located or does not respond, the account balance is placed in other income.

Económica: Here there are many people who have to travel far to get to the credit union. They can't come and return home in one day. So I cannot easily classify accounts as inactive.
In general our youth accounts are inactive. After one month we visit the child's household and give a general speech and/or a shirt.

Closing an account

Integral
When closing an account, the passbook is kept at the credit union and becomes a part of the verification documentation.
Iaguei
They use a close-out form (DO NOT HAVE THIS)

CASH MANAGEMENT

Since all RCUP CUs are legally unable to process checks, all withdrawals are paid out in cash.

Cash Drawer Management

	Starting Balance of the Cash Drawer	Determining Factor	In case of more demand or demand for dollars	Daily verification of cash drawer
Profesional	C$5,000	Experience	Manger accesses the strong box	
Integral	C$15,000	Experience		Yes
Iaguei	C$10,000	Changes by	Manger accesses	Yes

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		season, use the hoja de entrega as a reference	the strong box	
Avances				
Economica	C$3,000	Experience	Manager or Vice Gerente accesses the strong box.	Yes

a. Cash flow and cash reconciliation-
[Describe cash flow diagram and cite as Appendix]

At the end of the day the teller balances all transactions. S/he divides all cash and coins by nominations, ie. All C$25 are placed together, all US$5 are placed together etc. S/he also separates all of the minutes into deposits, withdrawals and loan payments. After the teller balances all transactions, the accountant does the cash reconciliation. *Include a text box of project policy? This is very detailed, I have all the forms involved as well as instructions.*

Excess Funds
Excess cash is transferred from the cash drawer to the vault or strongbox (most RCUP CUs have the latter). Only the Manager handles the strongbox or vault transactions, with the exception of Económica where Fransisco (short guy who works with her, is he the accountant?) also has access to this.

At Profesional excess money is deposited in the bank the next day. Excess meaning anything over the C$5,000 that is kept in the teller's drawer, and the [?%] that is kept in the caja fuerte.

At Integral, Manager deposits extra cash at the local bank at 4 pm daily, which is 3 doors from the credit union.

INFORMATION MANAGEMENT
RCUP CUs are not computerized. Member information is therefore limited to hard copies, which are stored in folders. One set of folders has member information (application and certificate of his/her share account); the second set of folders has member savings account materials separated by type of currency (C$ or US$) and type of account. In cases where there is no room for storing documentation, historical transactions are stored in plastic bags.

INTERNAL CONTROLS
Since RCUP do not fall under the purview of formal regulation, strong internal controls policy is essential for prudent savings management.

Employees Making Transactions
At Profesional, if the tellers want to make deposit or withdraw funds from their accounts, the Manager processes it.

At Integral and Iaguei the same rules apply to credit union employees as for members. The idea is that any inconsistencies will be identified at the end-of-day closeout. In other words, the end of day cash reconciliation is a form of internal controls for the credit union. Recall that the teller balances the transactions, the accountant processes and the Manager verifies and authorizes.
At Economica the size of the transaction determines who will process the transaction. For transactions below C$3,000 the same rules apply to credit union employees as for members; for transactions of C$3,000 and above the Manager processes the transaction.

"None of our staff's children can participate in our raffles."-Económica

Member Coding
Members are given a member identification code. Credit unions that have a branch identify to which location the member pertains in order to avoid the possibility of potential duplicate withdrawals by including an additional digit in the member identification number.

Handling funds
Profesional
Only the manager handles the funds stored in the caja fuerte; she is the only one with a copy of the key.

Member Security

TRUTH IN SAVINGS
All interest rates are displayed above the teller area. A member can come in the first 15 days of each month and the teller will disclose how much the member has received interest payments.

Since Profesional offers variable interest rates for its fixed term deposits, members can also obtain a copy of a sheet that displays the interest rates per type of fixed term deposit.

PRIVACY
Account information is not passed onto any other person other than the member. If the member cannot be physically present to withdraw or deposit funds, s/he has to send a different person with a signed deposit/withdrawal slip.

TRUTHFUL HANDLING OF ACCOUNTS

Death of a Member
In the event of a credit union member death, the beneficiary assigned by the member upon entry to the credit union will receive all savings. This beneficiary must show proper identification paperwork. If the beneficiary cannot furnish adequate paperwork, s/he must prove his/her legal identity via a lawyer.
For a discussion on Life Insurance, see *Other Services Offered*
Profesional is in the process/has completed of offering the savings life insurance..

Losing a Passbook
Integral: When a member loses his/her passbook, s/he has to write a letter stating the loss. S/he is then given another passbook with the same account number. The credit union looks at the member sub-ledger to verify what the member's current account balance is.
Iaguei: Charge C$5 and note this in the auxiliary. The member is then given a new passbook.

Economica: When a member loses his/her passbook, s/he has to wait at least three days before reporting the loss in writing to the credit union. The credit union closes the account and changes the number on the libreta. The member must pay C$10.

Institutional Security

RCUP CU	Excess cash is stored in:	Number of Security Guards	Distance to Banks where excess funds are stored
Profesional	Strong box	1	3 blocks away from the credit union
Integral	Strong box	1 since 1/99	
Iaguei	Strong box and vault	2 (1 during the day, 1 during the night)	
Avances	Strong box	0, but at night a public security guard monitors the credit union.	
Económica	Strong box	1 (24 hours)	

RCUP CUs are very standardized in terms of policies procedures and products. In this case study sample of 5 RCUP CUs, Iaguei was the only one with 2 unique practices: the internal delinquency sheet and the official cancellation sheet.

All credit union managers felt that in general members can be classified as either savers or borrowers.

When asking Celmentina if she would be interested in introducing shorter-term accounts (weeks) she said these would be better placed as passbook savings.

FURTHER POINTS TO INCLUDE:

OUTREACH/IMPACT

Entry into RCUP
Savings Growth over time: 1996-2000 per month
# of savings accounts by type of product
Volume of savings by product
# of accounts by gender per product
volume by gender per product

Current figures for savers/borrowers

DATA ON EXTERNAL CREDIT
DIFFERENCE B/w savings SERVICE vs. savings PRODUCT
Profesional/Liquidity reserves

I have most recent census data for each region of each of the 5 RCUP CUs
I have recent savings outreach information, more detailed than in RCUP report.

COMPARATIVE ANALYSIS WITH GTZ/CGAP CASE STUDIES (see lit. review)

Case of RCUP CU is more applicable to NGOs, for some of the same reasons as mentioned by Schmidt&Zeitinger (do not have unique characteristics such as government guarantee systems that may contribute to their success). I.e. The evolution of RCUP CUs as small rudimentary institutions in 1996 provide a more relevant experience to NGOs than the GTZ/CGAP case studies

[1] Hairston, James (2000), "Assessment of RCUP CU Products and Services". October.

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World Council of Credit Unions, Inc.
Savings Best Practices

Attachment 6

Savings Best Practices: Observations of Ecuador MIP Credit Unions

Some Observations about Savings Operations in four Credit Unions participating in WOCCU-Ecuador's Microenterprise Innovation Project

Savings Best Practices, WOCCU
N. Gons
DRAFT # 1: April 2001

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I. COUNTRY BACKGROUND INFORMATION

Table 1: General Country Data

Population (2000)	12,650,000
Women	6,300,000
Men	6,350,000
*Annual growth rate 1990-98	2.2 %

Sources: Banco Central del Ecuador, Informacion Estadistica Mensual; Centro Latinoamerico de Demografia (Celade), cited from EIU2000.
*IMF2000

GDP growth rates have been very low since 1995. In fact, the annual population growth rate of 2.2% exceeds national income growth throughout most of 1995-2000, suggesting a deteriorating in national living standards (refer to Table 1 and 2).

MACROECONOMIC CRISIS

In 1998 Ecuador's GDP stagnated; in 1999 GDP declined by an estimated 7.5%. This marked one of the worst macroeconomic crises Ecuador has faced in the last decades. Concurrently, inflation increased by 25-30% annually from 1996-1997, jumping up to 61% annually in 1999 (IMF2000). During 1998 and 1999 the real effective exchange rate depreciated by a total of almost 50%.

The **El Niño climatic pattern** in late 1997 brought excess rainfall and flooding which devastated key export crops on the coast, destroyed infrastructure (approximately 2,500 km of roads and 19 bridges) and left thousands homeless until the early months of 1998. According to the Economic Commission for Latin America and the Caribbean the estimated total economic damage of El Niño was approximately US$ 2.6 billion (or 13% of 1998 GDP) [EIU 1998/99, IMF 2000].

Underlying Ecuador's macroeconomic crisis was an overall weak macroeconomic structure. External debt was 77% of GDP at the end of 1997. Various external shocks during 1997-98 exacerbated this weak macroeconomic structure, including declining oil prices in 1997-99, the overall loss of confidence in emerging markets sparked by the Russian and Asian crises the late 1990s and losses incurred by el Niño.

Table 2: General Macroeconomic Indicators (annual percentage changes)

	1994	1995	1996	1997	1998	1999	2000(a)
GDP US$ bn	16.6	17.9	19.0	19.8	19.7	13.8	12.8
GDP per capita						US$ 1,130	
annual percentage changes							
Real GDP	4.3	2.3	2.0	3.4	0.4	-7.3	1.9*
Real GDP per capita			-.1	1.3	-1.7	-9.2	-3.3**
Consumer price index (period average)			24.4	30.6	36.1	52.2	96.4*
Unemployment rate			10.4	9.3	11.8	15.1	16.1**

Sources: Banco Central de Ecuador, Informacion Estadistica Mensual, IMF International Financial Statistics cited from EIU 2000; IMF 2000; *cited from EUI 2000 and 2001; **Preliminary data from 1st quarter 2000, IMF 2000

THE LABOR MARKET

The repercussions in the labor force of the economic stagnation in 1998 and the subsequent contraction in 1999 when GDP contracted by 7.3% are reflected in high unemployment and underemployment rates. Underemployment is a situation in which persons are working less than they would like to work, either daily, weekly, monthly or seasonally (Todaro 1997). Unemployment increased from 9.2 of the economically active population (EAP) in 1997 to approximately 16% by 2000. Due to the lack of formal job-creation, a significant proportion of the economically active population enters an economic activity in the informal sector.

Quarterly indicators for 2001 show a decreasing unemployment rate. However, this large-scale emigration among the working age population appears to have brought about a greater reduction in unemployment than job creation.

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Quarterly Indicators, EIU *2001*

	2000			
	1 Qtr	2 Qtr	3 Qtr	4 Qtr
Employment, wages and prices				
Unemployment Quito, Guayaquil, Cuenca (% of the labour force)	16.6	14.9	13.1	11.7
Underemployment (% of the labor force)	46.5	53.3	57.9	55.4

Labor force

(urban; % unless otherwise indicated)

	1992	1993	1994	1995	1996	1997*	1998	1999	2000
Economically active population ('000)	2,957	2,892	2,904	3,104	3,223	3,373.8	3,560.5*	3,769.6**	
% Male	59.5	60.3	60.8	60.5	60.5	60.9			
% Female	40.5	39.7	39.2	39.5	39.5	39.1			
% Unemployed	8.9	8.3	7.1	6.9	n/a	9.2	11.5	15	15.7
%Underemployed	47.9	47.2	45.2	45.9	n/a	40.4	46.6	52.3	41.8
By sector									
Agriculture	17.7	18	17.3	15.2	n/a	n/a			
Industry	8.2	10.1	7.4	9.7	n/a	n/a			
Services	45.3	41.8	46.1	44.0	n/a	n/a			

Sources: Banco Central del Ecuador, Boletin de Precios, Salarios y Empleo; Boletin Anuario; INEC, Encuesta Urbana de Empleo, Subempleo y Desempleo. Cited from EUI 1998/99
* Source: INEC, Encuesta Urbana de Empleo, Subempleo y Desempleo.cited from EIU 1999/2000
**Source: INEC, Encuesta Urbana de Empleo, Subempleo y Desempleo, www.inec.gov.ec and EIU 2000

According to the World Bank, in 1998 the highest 10% of income earners accounted for 37.6% of total consumption, while the lowest 20% of income earners accounted for just 5.4%. (IMF 2000)

Banking Sector Crisis

In 1994 the *Ley General de Instituciones del Sistema Financiero Nacional* (the Financial Institutions Law) deregulated the Ecuadorian financial sector. The subsequent increase in the number of financial institutions and the scope of their services occurred without the necessary institutional reform in the sector's regulatory authorities. In 1999 Ecuador had over 300 financial institutions of which 90% of assets were held by only ten institutions (EIU 1998/99). The banking superintendency's slow reform has permitted the spread of deficiencies in banking sector regulation and supervision. This has been one of the main causes of the successive banking crises since 1995 (EIU, 1999/2000).

At the onset of the macroeconomic crisis, some of the largest banks in Ecuador had eroded capital bases (IMF2000). A lot of commercial bank lending was US dollar-denominated, which left banks especially vulnerable a recession or a devaluation of the sucre (EIU 2000). Recall that during 1998 and 1999 the real effective exchange rate depreciated by a total of almost 50%.

CHRONOLOGY OF THE BANKING SECTOR COLLAPSE, 1998-99

September 1998: The medium-sized Banco de Prestamos failed to provide sufficient guarantees to secure liquidity loans from the Banco Central del Ecuador (BCE, the Central Bank). It closes.
December 1998: The Central Bank provides US$167m in liquidity loans to Filanbanco, the country's largest bank, but these are insufficient to save it from collapse. By mid-December control of the bank transfers to the newly created Agencia de Garantia de Depositos (AGD, the Deposit Guarantee Agency) so that it remains open under state management; in the same month the Banco Tunguragua is deemed insolvent and closes, following a massive deposit run on its offshore branch; a small savings and loan institution also closes.
January 1999: Banco del Azuay, unable to meet depositors demands, closes voluntarily. Two savings and loans thrifts, Financorp and Finagro, fail.
February 1999: A third savings and loans thrift, Financiera America, fails.
March 1999: Banco del Occidente closes. The government imposes a five-day bank holiday, followed by a year-long deposit freeze, which affects around 70% of total deposits-50% of sucre-denominated current- and savings-account deposits, all foreign currency deposits and all term deposits-in an effort to prevent further collapses. On March 23rd, Banco del Progreso, the largest bank in terms of deposits, closes voluntarily. Yielding to political pressure, the government refrains from intervening and instead the bank is given a two-month grace period in which to recapitalise.
However, with the Central Bank refusing to extend it credit, the bank closes at the end of the grace period, having failed to secure sufficient funds for recapitalisation. Subsequent audits reveal a massive capital deficit.
April 1999: Bancomex closes voluntarily.
May 1999: Independent foreign firms audit all 35 remaining banks.
July 1999: Banco Union, Solbanco and Banco de Credito close as a result of audit. The government intervenes to support Banco del Pacifico, Banco Popular, Previsora and Cofiec. New liquidity loans from the Central Bank allow them to continue to operate, despite significantly low capital-adequacy ratios.
September 1999: Banco Popular collapses following a run on deposits by nervous investors when a lawsuit is brought in the US by Colombia on account of problems with its sister bank, Banco Andino de Colombia. The US court ruling, which freezes the bank's Miami operations, is subsequently reversed, but only after a run on deposits in Ecuador forces the bank to close.
October 1999: La Previsora surrenders to the AGD by means of a proposed acquisition by Filanbanco. The merger is expected to be completed by the end of 2000. Banco del Pacifico and Banco Continental are also expected to undergo similar mergers.

-EIU2000

Liquidity in the system fell throughout 1998 (access to external interbank lines had been cut). The rate of deposit growth declined from an annual average of 26% in real terms in 1992-96 to just 3.3% in 1998 and to 1.5% in 1999, which mark the years of stagnation and recession respectfully. Loan losses increased as a result of the overall economic stagnation as well as losses incurred by el Nino.

The banking system entered a solvency and liquidity crisis. In December 1998 liquidity loans from the government, totalling $350m, were not able to save Filanbanco, the largest bank in the country, which was transferred to state control. By the end of 1998 four financial institutions, including the country's largest bank, had collapsed. In October 1999 over 70% of the banking system was under state control.

By 2000 only 26 banks remained of 42 that were operating in 1998, with four of the largest five having failed. The level of non-performing loans had reached 45% of loans outstanding. According to the Ministry of Finance domestic debt had risen from US$700 million end 1997 to US$3 billion end 1999 with the total cost of the banking crisis estimated at 20 % of GDP (EIU 2000, IMF 2000).

In December 1998, the Agencia de Garantia de Depositos (AGD) was created as part of a new banking-sector support scheme. The AGD was charged with restructuring and cleaning up the banking system, yet it lacked capital and provided for unlimited deposit insurance.

An international audit, carried out in mid-1999, categorized the remaining 35 banks under three broad headings: viable institutions, which met the minimum capital adequacy requirement of 9% capital to risk-weighted assets; banks whose capital-adequacy ratio was between 0% and 9%, which were given one year to increase their capitalization; and banks with negative capital deemed unviable, which then passed into the hands of the AGD.

SELECTED RECENT DEVELOPMENTS IN ECONOMIC POLICY: IMPLICATIONS FOR THE FINANCIAL SERVICES SECTOR

1998: In November a deposit guarantee agency (AGD) is created and charged with overseeing the clean-up of the financial system. During the subsequent nine months, $1.5bn in government bonds are issued to the ailing financial sector and 70% of the banking system is brought under state control

1999: Income and corporate taxes are suspended in January in favor of a new 1% tax on the circulation of capital.

2000: The economy is dollarized. Interest rate caps introduced under the *Ley de Transformación Económica*. A political demand for lower rates forced a reduction in the cap from 24% to 20% in May 2000. As a result, real interest rates became negative, which has given rise to severe credit rationing, as well as the application of distortionary commissions and fees by banks to compensate for economic losses (EIU2001).

> *The fragility of the banks is likely to hamper the financial system's effectiveness as a channel of credit to the private sector for years to come. Even if the government is successful in selling the remaining state-held banking assets to foreign investors,* ***this is unlikely to improve the problem of credit access for small and medium- sized businesses.***
>
> -EIU 2000

Current labor market trends (lack of formal job creation, burgeoning un and under-employment) push the EAP into the informal sector. The banking system's fragility will not only hamper access to financial services for small and medium businesses, but also for microentrepreneurs and the remainder of Ecuadorian residents.

II. THE CREDIT UNION SECTOR

Currently there are an estimated 350 credit unions operating in Ecuador, of which 26 are regulated by the Superintendency of Banks and hold approximately 80% of assets (CHECK mijn kladblok). WOCCU-Ecuador's Microenterprise Innovation project provides technical assistance to 23 credit unions, hereinafter referred to as *MIP CUs*.

Recent developments in Ecuador's banking sector not only underscore the importance of the credit union sector in Ecuador; it reveals the safety and soundness of the credit union system. *What happened to non-MIP credit unions?*

Throughout Ecuador's macroeconomic and banking crisis, all MIP CUs stayed afloat. Noteworthy is the tremendous growth in institutional capital that took place before, during and after the crisis.

Institutional capital/total assets

1995	2.73%
1996	4.66%
1997	7.99%
1998	11.13%
1999	21.14%
2000	26.13%

-and grew in membership

Growth in MIP CU Membership& other Clients

	Membership			Other Clients			TOTAL
	Total	Women	Men	Total	Youth	*Terceros*	
1996	522,001	199,242	277,236	8,617	8,617	0	**530,618**
1997	541,720	204,307	286,775	25,479	16,831	8,648	**567,199**
1998	631,947	227,051	353,026	89,146	38,090	51,056	**721,093**
1999	655,596	252,759	402,837	104,145	42,820	61,325	**759,741**
2000	700,428	268,736	431,692	112,150	42,213	69,937	**812,578**

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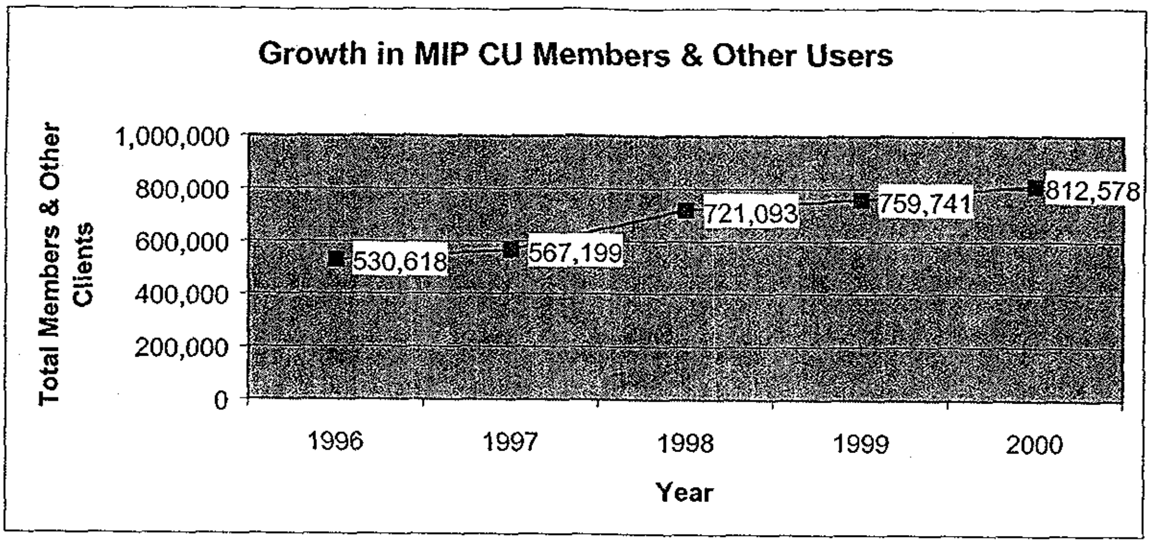


When evaluating volume of total savings in terms of US dollars, the decrease during 1998-99 is tremendous. Recall that the real effective exchange rate depreciated by a total of almost 50% during 1998 and 1999.

Growth in Savings (S3)

1996	23.19%
1997	47.55%
1998	-32.85%
1999	-50.54%
2000	**93.70%**

Noteworthy is the nearly 95% growth in savings in the year 2000. Growth in total savings for commercial banks increased by 26.8%. Note that over half of this growth comes from demand deposits, which is a service that credit unions are not offering. SUMMARIZE WHY

Bank deposits (in US$ m)

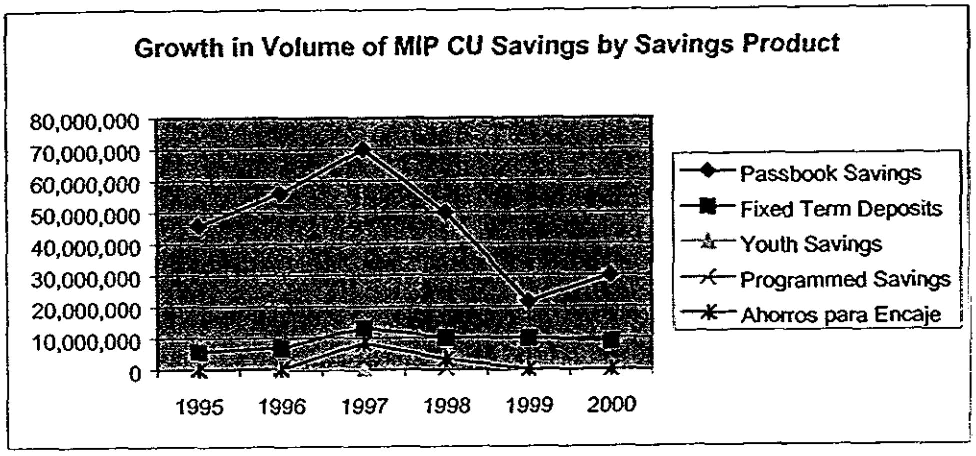
	demand deposits	%change	Term & savings deposits	%change	total savings	%change
Dec. 1999	696.6	-16.4	2,498.90	5.1	3,195.50	1.5
Dec.2000	1152	7.1	2,901.10	1	4,053.10	2.7
Increase	455.4	65.4%	402.2	16.1%	857.6	26.8%

Source: Banco Central del Ecuador, Información Estadística Mensual, cited from EIU2001

Total Savings as of September 2000

	Commercial Banks	Regulated Credit Unions
Total Volume	1,660,488,750	55,400,770
As % of GDP (2000)	12.9726%	0.4328%

INSERT: DATA OVER TIME



Growth In Savings Volume (in US$) as of March 2000

	1995	1996	1997	1998	1999	2000
Passbook Savings	45,703,373	56,069,151	70,048,742	49,972,861	21,638,338	29,943,937
Fixed Term Deposits	5,765,710	6,982,178	13,165,656	9,993,517	9,861,583	8,908,767
Youth Savings	0	0	307,882	0	0	0
Programmed Savings	683,678	1,020,233	2,936,272	483,206	0	0
Ahorros para Encaje	0	205,585	8,382,695	3,237,266	0	3,120
TOTAL	52,152,761	64,277,147	94,841,246	63,686,849	31,499,920	38,859,719

WOCCU-Ecuador PEARLS, March 2000

¿?Youth accounts show a value of 0 1998-2000 in PEARLS March 2000, however during this same time period, the number of youth clients increased from 38,090 to 42,213.

MISSING: # of ACCOUNTS

EFFECTS OF ECONOMIC POLICY ON CREDIT UNIONS

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Effects of Dollarization on Savings Products

COOPROGRESO: Our *Reepos* and *Profuturo* products were very popular in the past. At this time they are not doing very well at this time and need to be redesigned or terminated. One contributing factor is dollarization: before dollarization we paid 33% interest on the these products. Now we pay approximately 5%, which is *perceived* as yielding a lower net gain by many clients. The effect of dollarization is mainly psychological.

Another constraining policy governing credit unions in 2000 is that they were not allowed to pay dividends in the year 2000, so they went back to requiring saving in shares as a loan requirement. Another

Other examples of economic policy that produced negative effects in the financial services sector include the 1% tax on financial transactions (see Selected recent developments in Economic Policy). In order to avoid this tax, people withdrew their funds from domestic financial institutions.

The effects of dollarization are noted by credit union staff as having hampered savings mobilization. The effect of dollarization is a psychological one; interest rates dropped significantly in terms of the dollar denominated currency which is interpreted by many clients as yielding a lower net gain.

MIP CUs: A Closer Look

In February 2001 WOCCU carried out interviews with credit union management and staff at 4 MIP credit unions as part of WOCCU's Savings Best Practices project.

Note: MIP CUs are relatively more differentiated than for example RCUP CUs, which are relatively more standardized. The 2 main categories are *regulated* and *non-regulated* CUS which, in general, are synonymous with large and small credit unions respectfully. Almost all MIP CUs are regulated.

CU	Location	Status	Savings Products	Marketing
Riobamba	Riobamba	Regulated	Few savings products	Recently added a marketing dept.
La Merced	Ambato	Non-regulated	---	None
COOP Progresso		Regulated	Redesigning	Plan & Budget
29 de Octubre	Quito	Regulated	A slight decrease/increase	Plan & budget

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Savings Mobilization Strategies

None of these credit unions followed aggressive marketing strategies. Instead, one can say these CUs have an *implicit marketing strategy*, which is offering high quality products and services. All 4 credit unions mentioned "high quality service", which is characterized by personalized and attentive service, as a main reason for attracting and retaining clients. All credit unions have a Client Service staff (Servicio al Cliente). High quality service also involves offering high quality services. All credit unions offer a life insurance, INSERT ALL INSURANCE PRODUCTS

Most MIP CUs also offer remittance services through Western Union.

Some/Most offer free services doctor, orthodontist and funeral services.

Recently 4 credit unions joined into one network, known as MEGARED. This marks a new phase of intra-sectoral cooperation that will only improve the credit union's capacity to effectively deliver financial services.

Case Study in Marketing: La Merced

"We always wanted to mobilize voluntary savings- we needed technical assistance from WOCCU to do it."

Four years ago we began to redesign our savings products.

Using WOCCU tools was not that difficult since the cu staff are mainly professionals with financial background.

Marketing strategy focus included reactivating inactive clients and promoting new savings products introduced by WOCCU-Ecuador, including youth accounts and a series of programmed savings accounts including education, retirement and housing accounts. Offering qaulity products is interlinked with reatviating inactive clients.

Ads in the local newspapers, brochures, local radio stations.

The CU director would visit microentrepreneurs, since this niche is perceived as having a lot of savings potential.

Cu had a goal of growing by 150 new members/month. A main strategy used were personal visits by credit union staff to microentrepreneurs, residential areas, local institutions and schools. The CU segmented into local market into the following niches: informal sector/microenterepreneurs, commerce, residential, educational institutions, labor unions and associations. At schools the credit union marketed its youth accounts. It offered credit union banners and other decorative materials to the school and gave a speech using overheads that summarized the savings product. School directors allowed 30 minute speeches.

When marketing the other sectors, the credit union staff summarized all savings products. People then chose which product(s) were of most interest and focused on explaining the terms and conditions for those products. *Note: manager used to be a salesman.*

The word-of mouth effect was also effective.
Other factors contributing to success is that all withdrawals are given in cash.

Case Study in Marketing: COOPROGRESO, Marcos Garcia

COOPROGRESO has grouped their market into the following broad categories:
Age: age ranges that are defined according to one's savings/spending cycle, ie. 18-25 spend a lot save a little (FIND technical definition)
Socioeconomic groups: lower-middle, middle, microentrepreneurs and professionals
Geographical: they started in Atahualpa and want to cover the periphery of Pichincha.
In the future they may consider youth accounts.

Instead of defining their comparative advantage as offering higher interest rates, they want to promote their institutional soundness (solido, solvents y seguro) in their marketing initiatives. Given the recent banking crisis this promises to be a powerful marketing approach.

Marketing budget for 2001 is US$120,000. A main part of marketing initives will focus on promoting the credit union as an institutionally sound financial institution with quality financial products. This will be done through radio, newspaper and television. Brochures have been developed and will be disseminated at schools, universities, public places and events. The latter is outsourced by season. The slogan on these brochures is "Thinking about the future of my family".

Challenges: marketing can make suggestions to management but this does not mean that management will react. Every month there is a meeting in which department heads discuss what's happening.

COMMENTS:
A main reason why we are growing is due to our sound image that became very apparent during the banking crisis. *Member satisfaction surveys for existing and potential surveys are an important step in making high quality products a driving force of credit union growth.*

Case Study in Service Innovation: Cooperativa 29 de Octubre

Since 1995 this credit union has a mobile agency (agencia movil) that consists of a truck that travels to wherever the credit union's members need services. The concept stems from its mobile clientele, which historically have been military employees that have had to work in various locations for extended time periods.

The MA provides all the services that the credit union central office does, from deposits and withdrawals to new membership requests.

Currently the ma is utilized mainly by occupational employers whose employees are CU members as well as members in the military sector. The credit union is contacted and the MA goest to where the demand is. During the border conflict with Peru in the early 1990s, the MA went to the conflict areas to provide financial services to the army.

The truck is *in cognito*, in other words does not have a conspicuous credit union logo, instead it is relatively dirty. It is equipped with 2 firearms.

29 de Octubre offers debit cards which a member can use all over the world. MIP project staff have successfully used the debit card in South Africa.

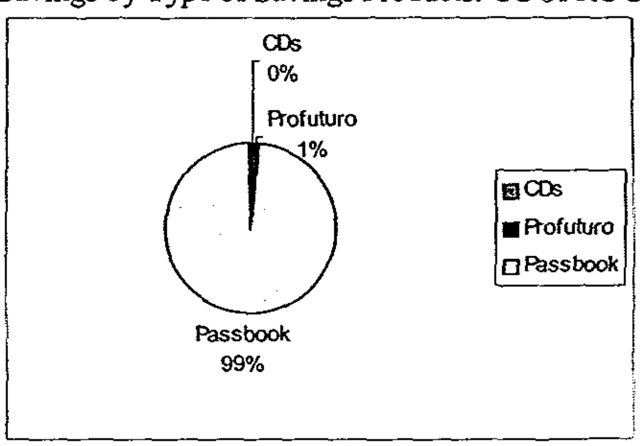
In the very near future- credit cards

Savings Products

WOCCU MIP savings product manual includes the following products:

Of the 4 MIP CUs surveyed, passbook savings and term deposits were the main products used and offered.

Savings by Type of Savings Products: COOPROGRESO



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Savings by Type of Savings Products and Gender : COOPROGRESO

Certificates of Deposit by Gender and Deposit Term (in days)

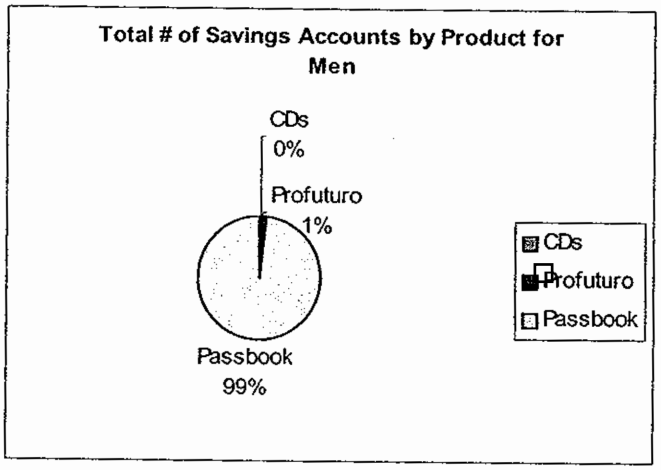
	30-90		91-180		181-270		271-360		361 +	
	Number	Volume	Number	Volume	Number	Volume	Number	Volume	Number	Volume
Men	99	254,488	28	24,111	11	7,801	6	1,446	12	3,409
Women	107	129,410	66	40,134	5	17,743	3	1,223	15	3,261
TOTAL	206	383,898	94	64,245	16	25,544	9	2,669	27	6,670

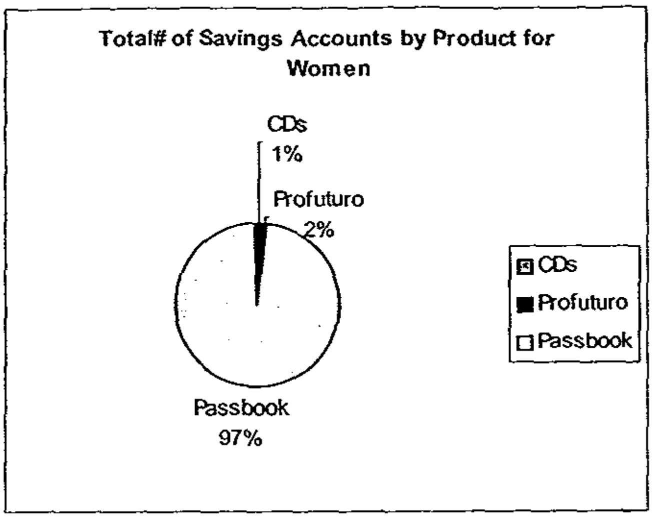
PROFUTURO

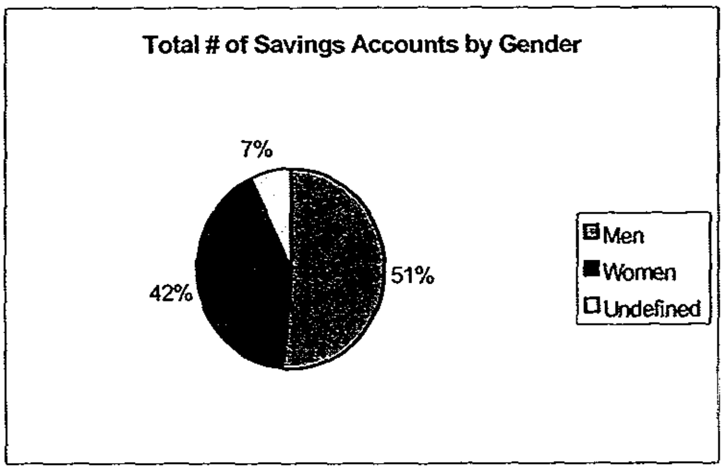
	Number	Volume
Men	508	22,910
Women	502	21,850
TOTAL	1,010	44,760

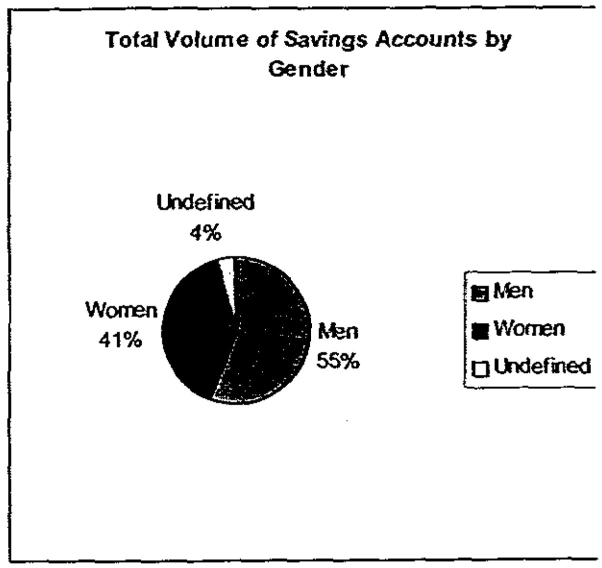
Passbook Savings by Gender

	Number	Volume
Men	35,659	3,106,475
Women	28,681	2,293,840
Undefined	4,801	256,336
TOTAL	69,141	5,656,651









INSERT Savings products by CU

Case Study in Information Management: COOPROGRESO

Client information is kept in envelopes, which is sent by all departments to the *Departamento de Archivo* on a monthly basis. This department, comprised of 2 people, store information in carton boxes by dates. Loan payment contracts are kept in *Custodia de Valores*, i.e. are saved in metal boxes with keys.

Member coding

A member code has 12 digits, for example: 401110235614

The 1st three digits identify the agency: 401110235614

The next two digits classify the type of account: 401110235614

The remaining 7 digits classify the client: 401110235614

Case Study in Cash Management: COOPPROGRESO

Head Teller, David Peralta

All tellers arrive at the credit union 15 minutes before opening. In order to access their cash box and daily cash amount, they all have to enter the vault. In order to enter the vault, each teller must print and sign his/her name . The head teller has the central key to the metal cash boxes and the tellers all have a personal key that is unique to their individual cash box. Hence both the teller and head teller have to be present in the process of accessing the initial daily cash amount.

During the day a teller may have too much or too little cash, in which case she may deposit or access more cash from the head teller. These transactions are documented by Intercambio de Efectivo slip. This credit union is insured for handling US$10,000-15,000 in the teller area, which is kept in a strong box in the head teller's office. If cash demand exceeds these funds, the head teller will access the vault. The total amount of cash in the credit union is US$33,000. The head teller's office has an automatic lock that must be unlocked from the inside.

How is the daily starting cash amount determined such that the head teller can minimize accessing the vault throughout the day? He projects the next day's cash demand by discussing with the credit department and the department in charge of certificates of deposits. Generally tellers start with US$1,500. The credit union is insured up to US$2,000/teller.

At the end of the day the teller divides her daily transactions by type of transaction (withdrawal, deposit) and denomination, which are stored on the bottom and top of the teller's cash box respectively.

The head teller processes all teller reports that summarize all transactions made throughout the day. He enters this into the computer, which can generate a "Cuadre de Boveda" (vault reconciliation report).

Banks collect credit union deposits daily with a security car.

Marketing Slogans

COOPROGRESO

General: COOPROGRESO ESTA PREPARADO PARA EL SIGLO XXI CON TECNOLOGIA DE PUNTA. Estamos controlados por la Superintendencia de bancos y Respaldados por la AGD.

This year's brochures: Thinking about your Family's future

Interest Rate Monitoring

La Merced-yearly

In Ambato there are over 20 banks, over 22 credit unions as well as financieras and mutualistas. We monitor our interest rates yearly. Interest rates are displayed outside.

COOPROGRESO-weekly monitoring of banks and credit unions, use the Central bank's website as a benchmark as well as local competition (see table).

"AGD insures credit unions for lower interest rates than banks: banks can pay up to 8%, banks up to 10%." -Jefe de Ahorros y Inversiones, COOPROGRESO

Observations

According to the Manager of La Merced: The fact that a lot of our accounts have low balances is not really a problem because we have a lot of them. Also, people with low balances tend to leave their money.

World Council of Credit Unions, Inc.
Savings Best Practices

Attachment 7

Supervision Best Practices in Peru, Bolivia and Ecuador
(Mejores Prácticas en la Supervisión de las Cooperativas de Ahorro y Crédito)

ALCANCE DE TRABAJO

Supervisón

Objetivo:

1. Documentar las practicas y instrumentos usados por todos involucrados en el proceso de supervision de las CAC.
2. Identificar los obstaculos en la implementación de la legislación y normativas de la supervisión (son estructurales, politicas, falta de recursos, falta de conocimiento, etc.?)
3. Entregar un informe de un *analisis comparativo* de las practicas y instrumentos de la supervision de las CAC en Perú, Ecuador y Bolivia. La discusión tiene que incluir como están las prácticas en ***teoria*** y como están en la ***realidad***, es decir, como se implimentan la legislación y normativas de la supervisión.

Antecedentes

¿Cuantas cooperativas están supervisadas? (en teoria, y en la practica)

¿Desde cuando?

Contenido de la(s) ley(es) y normativa(s)

- Como es el contenido de la(s) ley(es) y normativa(s):
  1. ¿existe pautas básicas para las operaciones prudentes de la CAC?
  2. ¿requisitos y pautas de auditoría?
  3. ¿normas de calidad de crédito?
  4. ¿los parametros de la creacion de estimaciones para prestamos incobrables?
  5. ¿normas de inversión?

  6. ¿Como funciona en la practica?

Ventajas y desventajas de supervision delegada y supervision directa:

- ¿Hay caracteristicas locales que hacen una estructura más adecuada que el otro?

- ¿Hay obstaculos inherente en cada estructura?
    1. ¿Cómo es la transferencia de información entre las CAC y las entidades que las supervisan?

    2. En su analisis, detalle casos especificos.

Papeles y responsabilidades

- Describe los papeles y responsabilidades de cada actor principal (la Superintendencia, Federacion, CAC) en el proceso de supervisar las CAC. Compárelos con los que pertenecen a los bancos y otras instituciones financieras no-bancarias.

- ¿La asignacion de los papeles y responsabilidades es efectivo para el enforzmiento de y el cumplimiento para las normas prudentiales ?

- ¿Como funciona en la practica?
    1. ¿Ejecutan sus responsabilidades y sus poderes estipulados en las leyes y reglamientos?
    2. Si no los ejecutan, identifica algunos razones porque no.
    3. En su analisis, detalle casos especificos.

Poderes de sancionar a las CAC

- Describa la estructura de responsabilidad y la implementación de hacer sanciones.
    1. Describe las practicas y procedimientos de sancionar CAC que no cumplen con las normas legales y/o prudentes, p.e. cartas de entendimiento, multas, orden de cesación por práctica desleal, separación de funcionarios, conservaduría y liquidación o fusión obligada.
    2. ¿Existe metodos alternativas de sanciones? ¿En que casos los usan?
    3. Dar casos pasados y detalle problemas, si existe, de implementación en la practica.

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La practica de auditoria (desde los punto de vistas de los reguladores y las CAC).

- Explique los estanderes de realizar la auditoria
    1. ¿Que instrumentos se usan para realizarlo?
- Explique los estanderes de verificar la auditoria
- ¿Quien(es) es/(son) responsable(s) para que parte del proceso?
- ¿Con que frecuencia lo hacen en la practica?

La practica de inspecciones (desde los punto de vistas de los reguladores y las CAC).

- ¿Cómo compara la politica de auditoria con la de las inspecciones de las CAC?
- Explique los estanderes que se usan para realizar las inspecciones.
    1. ¿Que instrumentos se usan para realizarlo?
- Explique los estanderes que se usan para verificar las inspecciones.
- ¿Quien(es) es/(son) responsable(s) para que parte del proceso?
- ¿Con que frecuencia se hace en la practica?

Comparacion de PERLAS y Alerta Temprana

Como podemos incorporar estas dos herramientas en el seminario *Mejores Practicas de Supervision* en una manera en que no compiten.

Anexo: ANTECEDENTES

PAIS	# de CAC	# de SOCIOS	ACTIVOS (US$)	AHORROS (US$)	PRESTAMOS (US$)
Peru	132	259,295	237,896,243	181,770,054	148,942,125
Bolivia	19	326,775	181,813,183	146,649,003	143,797,442
*Ecuador	23	844,058[1]	110,725,300	76,482,300	78,424,900

[1] 669,914 socios más 174,144 usuarios

Fuente: Informe Estadístico 1999;
*PERLAS2000, Note that during 1998 and 1999 the real effective exchange rate depreciated by a total of almost 50%.

MEJORES PRÁCTICAS

EN LA SUPERVISIÓN DE LAS

COOPERATIVAS DE AHORRO Y CRÉDITO

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I. Introducción

El objetivo de este trabajo es presentar las mejores prácticas en la supervisión de las operaciones financieras de las Cooperativas de Ahorro y Crédito (CAC's) en América Latina[1].

La documentación se fundamenta en una investigación (field study) realizada por un equipo mixto de expertos[2] de la Confederación Alemana de Cooperativas (DGRV) y del Consejo Mundial de Cooperativas de Ahorro y Crédito (WOCCU) entre el 7 y el 18 de mayo del año 2001.
En esa oportunidad se evaluó el cimiento normativo y las prácticas ejecutadas en la supervisión de las cooperativas de ahorro y crédito en Bolivia, Ecuador y Perú.

En cuanto a sus conclusiones y recomendaciones el autor adicionalmente remonta a las experiencias y prácticas de las Cooperativas Financieras de la Comunidad Europea (en particular al caso de Alemania), las cuales están sujetas a la regulación y fiscalización bancaria en sus respectivos países.

II. La trascendencia de las Cooperativas de Ahorro y Crédito para el desarrollo económico de una sociedad equitativa

Tradicionalmente los analistas miden la importancia de un sector financiero a través de una comparación de sus totales de activos acumulados dentro de la industria bancaria. El impacto del sector de las Cooperativas de Ahorro y Crédito, sin embargo, no radica en este factor sino en el número de sus cuentas y personas atendidas.

En este sentido las Cooperativas de Ahorro y Crédito reflejan el mismo fenómeno que su clientela. En Chile, por ejemplo, los micro- y pequeños empresarios cuyas ventas ascienden solamente a aproximadamente un 17% del total, pero que al mismo tiempo generan un 80% del empleo y las CAC's representan ni siquiera el 1% del mercado financiero pero atienden a más del 10% de la población económicamente activa.

Las Cooperativas de Ahorro y Crédito han desempeñado tradicionalmente y continúan haciendo el papel de "Banco de los Pobres" en las zonas urbanas y rurales de América Latina, atendiendo a familias de menores ingresos (y algunas de medianos ingresos) y empresas más pequeñas que los bancos no han atendido en forma tan adecuada.

[1] El autor agradece al Sr. Nelson Jofré, gerente de FECRECOOP/Chile, por su valiosa colaboración en la redacción del texto.
[2] Jesus Chávez y Oswaldo Oliva (WOCCU), Helmut Pabst (DGRV)

Las CAC's constituyen también el principal proveedor de crédito a microempresas en América Latina: "Aunque las ONG's y los Bancos comerciales proveen aproximadamente US$ 200 millones a los microempresarios, las Cooperativas de Ahorro y Crédito otorgan préstamos cuyos montos oscilan entre US$ 2.000 y 4.000 millones"[3].

"La modernización y la supervisión de CAC's ofrece la posibilidad de incrementar la cantidad y la calidad de los servicios de crédito y de depósitos provistos a las familias de menores ingresos, reduciendo así la desigualdad de los ingresos"[4].

La estabilidad de una sociedad humana depende principalmente de la participación equitativa de sus ciudadanos en las oportunidades económicas del país, esto es, que todas las personas tengan accesos a los mercados en igualdad de condiciones y que, por lo tanto, gocen de los mismos mecanismos e instrumentos para participar en el desarrollo.

El desequilibrio económico exhibido por medio de la polarización de niveles de ingresos y la posesión de capitales que generan estratos o "clases" claramente marcadas o diferenciadas en la población, provoca constantemente roces sociales inherentes. Estas distorsiones sociales que mantienen a amplios sectores de la población en la pobreza, culminan periódicamente en conflictos sociales que perjudican el crecimiento de los países respectivos y que –en definitiva- ponen en riesgo la sustentabilidad de los procesos de desarrollo de países emergentes, toda vez que se acentúa la incapacidad de generar instrumentos que materialicen una verdadera democracia económica.

Una de las causas más relevantes de esa falencia radica en la mayoría de los países Latinoamericanos, en el hecho que importantes estratos de la población no disponen en igualdad de derechos del acceso a prestaciones de servicios financieros por parte del mercado financiero formal. A este fenómeno se suman medidas insatisfactorias e incompletas de regulación y supervisión de la intermediación financiera.
La inestabilidad social y los defectos formales y materiales referente a la fiscalización de los mercados financieros tienen efectos permanentemente tangibles sobre la solidez de esta área de las economías. Entre los indicadores negativos figuran: un amplio mercado financiero informal, tasas de interés desfavorables, la devaluación de las monedas, etc.

Las Cooperativas de Ahorro y Crédito son intermediarios financieros que operan exitosamente gracias a una especialización particular que fortalece sus operaciones en el riesgoso ámbito de las microfinanzas. A continuación,

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[3] Banco Interamericano de Desarrollo (BID), *II Foro Interamericano de la Microempresa*, Buenos Aires, Argentina, 24-26. Junio 1999.

[4] Banco Interamericano de Desarrollo (BID), *Políticas financieras para reducir la desigualdad*, 1999, pág. 193.

presentamos los aspectos más destacados que caracterizan la intermediación financiera del sector cooperativo:

- Intermediación con igualdad de oportunidades
  Las CAC's no aplican barreras de entrada ni montos mínimos para recibir ahorros o conceder créditos.

- Localidad
  La mayor parte de las personas que solicitan créditos en las CAC no pueden ofrecer garantías, tampoco están en condiciones de entregar informaciones certificadas de sus ingresos y egresos o de su situación económica. Las CAC's compensan esas carencias a través de un sistema de información que se alimenta de los conocimientos personales que tienen los directores y funcionarios de la clientela perteneciendo a estratos sociales bajos hasta medios bajos.

- Nivel operativo adaptado a la clientela
  Las CAC's operan con una gran flexibilidad en las operaciones cotidianas en cuanto a prestaciones de servicios sin mantener una amplia red de sucursales y estructura burocrática. Las decisiones son rápidas a causa de la pequeña magnitud del intermediario. Los esfuerzos en pos a profesionalizar la gestión de las CAC's no deben llevar a convertirlas en entidades excesivamente burocratizadas de estructuras y procedimientos semejantes a los de la banca tradicional.

- Rentabilidad / Solvencia
  Las CAC's recaudan ahorros de hormiga y canalizan estos recursos a través de una cartera de créditos atomizada. Pese a costos elevados que causan las transacciones de microfinanzas, sus sistemas operativos adaptados permiten generar una rentabilidad sostenible.
  En los tres países analizados, los sectores exhiben –considerando como base patrimonial solamente sus reservas- un coeficiente de solvencia satisfactorio. En promedio, ese índice supera la exigencia del 8% del Acuerdo de Basilea.

- Aporte a la política de descentralización
  Las CAC's son los únicos intermediarios financieros descentralizados que restan en los mercados financieros de América Latina, últimamente muy propensos a un proceso acelerado de fusiones bancarias. Las CAC's realizan una atención intensiva en la concentración de operaciones y penetración de mercados locales, generando así un circuito local de intermediación, gracias a una dedicación determinada a una zona geográfica claramente definida.

III. Fundamentos para la regulación y la supervisión de las operaciones financieras de las Cooperativas de Ahorro y Crédito

1. Rol del Mercado Financiero

La política en los diversos ámbitos internacionales ha reconocido que la consolidación de los sectores financieros por medio de mecanismos de regulación y supervisión y su democratización son requisitos imprescindibles para el desarrollo de los restantes ámbitos de la economía nacional.

La envergadura extraordinaria de los mercados financieros deriva de su rol clave para el desarrollo de toda índole de industria y comercio –incluyendo la artesanía y la agricultura– y también para el porvenir económico de las personas naturales.

El funcionamiento de los sistemas financieros sin distorsiones o averías estructurales derivados de la insolvencia de instituciones financieras, es el fundamento del desarrollo de cada macroeconomía.

Los requisitos más relevantes para que el mercado pueda funcionar debidamente, son los que se esbozarán a continuación:

a) Una normativa actualizada y eficaz que regule la actividad de intermediación financiera (en vez de regular la gestión de los intermediarios financieros por sector; "Ley de Intermediación Financiera" versus "Ley de Bancos");
b) Una supervisión eficiente y firme de todos los agentes de la intermediación financiera;
c) Una aplicación total y uniforme de la normativa bancaria y de las labores de la supervisión para todos los intermediarios financieros;
d) Igualdad de acceso a servicios financieros para todos los ciudadanos por medio de una cobertura completa de las distintas demandas. Este afán resulta realizable con la constitución de sectores especializados (Bancos Comerciales, Financieras, Cooperativas de Ahorro y Crédito, Mutuales de Vivienda, Cajas Municipales, etc.)

1. El Acuerdo de Basilea

Conforme a los criterios del Concordato de Basilea, la intermediación financiera es toda aquella actividad habitual que consiste en la captación -bajo cualquier modalidad- de recursos redimibles del público para destinarlos a colocaciones. Por consiguiente, aquellas entidades que realizan dicha actividad son intermediarios financieros.

Las Cooperativas de Ahorro y Crédito movilizan recursos redimibles sea por vía de captaciones en el pasivo o por medio de aportes registrados en el patrimonio. Sin embargo, los aportes de las CAC's mientras no estén sujetos a restricciones de su devolución, exhiben características de un ahorro y no de un capital de riesgo, debido a su alta volatilidad. Por ende, mientras permanezca la posibilidad de libre rescate de las aportaciones, el capital social no puede ser considerado en calidad de elemento para el cálculo del coeficiente de solvencia.

2. La Fe Pública

Las CAC's trabajan, en cuanto a la recaudación de las captaciones, con la misma fe pública que los bancos comerciales. Es incomprensible que los recursos de ahorrantes, quienes en su gran mayoría pertenecen a estratos económicamente más débiles y menos experimentados, en la materia de evaluación de la solvencia de instituciones financieras, deben estar excluidos o menos considerados de mecanismos de supervisión en la materia financiera.

IV. Distintas opciones de regulación

1. Cimientos legales superiores
   Existen cinco opciones acerca de la regulación de la intermediación financiera de las Cooperativas de Ahorro y Crédito:

a) Regulación en la **Ley Bancaria/Ley de Instituciones Financieras** sea en forma general o en un capítulo particular para el sector cooperativo.
   ↳ best practice**

   Sin embargo, en la práctica existe la figura, que la regulación no tiene cobertura completa y rige solamente para una determinada cantidad o grupo de cooperativas financieras (casos de Bolivia y Ecuador). Los criterios para seleccionar un grupo adecuado para la supervisión consisten, entre otros, en el volumen de activos o el modo de operaciones (p.e. captación de terceros).

b) Regulación en una **Ley especial de las Cooperativas de Ahorro y Crédito**
   ↳ Best practice*

   Alternativa para el caso, que resulta imposible o difícil incorporar a corto/mediano plazo las CAC's en la ley bancaria. La desventaja de la opción consiste en una legislación paralela para las CAC's. Resulta preferible tener un marco normativo único para todos los integrantes del mismo mercado.

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c) Disposiciones sobre la intermediación financiera en un capítulo de la **Ley General de Cooperativas**
↳ Alternativa inadecuada

Se puede tolerar esta modalidad solamente para un período transitorio, con el fin de tener un mínimo de fundamento legal. Las operaciones financieras son tan específicas, que resulta imposible regularlas debidamente en una ley general. Las CAC's y su gestión quedarían en este caso, separadas de las pautas establecidas por la legislación bancaria, que rige para los demás intermediarios.

d) **Autorregulación** en los estatutos o convenios (p.e. de la Federación)

↳ La autorregulación comprende medidas de prudencia financiera del propio sector cooperativo:

a) Con el propósito de complementar un marco normativo adecuado existente pero no exhaustivo o,

b) En una fase inicial o de piloto antes de que rija por primera vez una normativa, que regula la intermediación de las CAC's. Es una alternativa para visualizar la viabilidad de la supervisión bancaria en CAC's ante el legislador, respectivamente las autoridades. También resulta oportuno el modelo para preparar el sector para la supervisión especializada. En este caso es necesario que con posterioridad se promulgue una regulación apta y que se implemente luego definitivamente la supervisión.

La autorregulación puede ser ejecutada y controlada por una Federación y/o por una Caja Central Sectorial. Los principales componentes de la autorregulación consisten en:

- la constitución de un FONDO DE PROTECCION DE DEPOSITOS,
- el encaje en una CAJA CENTRAL o FONDO DE LIQUIDEZ,
- la estipulación de PRINCIPIOS (p.e. la regionalidad, la subsidiaridad) en los estatutos de la federación,
- la redacción y difusión de un ESTATUTO MODELO para las CAC's,
- la implementación de un SISTEMA DE INFORMACION GERENCIAL en las CAC,
- el MONITOREO DE INDICADORES por parte de una división de la Federación.

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Con estas medidas el agente puede conceder a las CAC's asociadas un sello de calidad y realizar un ranking para que las autoridades, los socios y el público fácilmente puedan visualizar la solvencia de las cooperativas individuales.

- Sin embargo, la autorregulación por sí y sin respaldo normativo es insuficiente para implementar un régimen de disciplina financiera. Principalmente porque el modelo carece de la facultad de imponer sanciones, además, la adhesión de las CAC's es voluntaria.

e) **Ninguna regulación** de las operaciones financieras de las CAC's

- Situación que vulnera claramente las exigencias del Acuerdo de Basilea y discrimina los intereses y derechos de los más vulnerables ahorrantes del mercado financiero.

2. Normativa detallada

Los cimientos principales de la regulación están estipulados en una ley pertinente, mientras que las pautas protectoras y preventivas están establecidas en un nivel subordinado a la ley y esbozadas en una normativa aparte:

a) reglamento o recopilación de pautas
b) resoluciones sobre límites e impedimentos
c) cartas circulares
d) plan único de cuentas
e) estatuto modelo o exigencias mínimas ante el contenido de los estatutos

V. Modelos de Supervisión

Básicamente, se puede distinguir entre cinco modelos de supervisión de las operaciones financieras:

1. Supervisión directa → Regulación del Estado
→ Supervisión Superintendencia (SB)

En este caso la Superintendencia ejecuta la supervisión on-site y off-site , exclusivamente por medio de su personal propio (p.e. Bolivia, Costa Rica, Ecuador).

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2. Supervisión auxiliar → Regulación del Estado
→ Supervisión ⇒ SB

Off-site
Intervención
Sanción
⇒ SB

On-site
⇒ agente privado

En el modelo de la supervisión auxiliar, la Superintendencia queda con todas las facultades y funciones del modelo de la supervisión directa. La SB encarga algunas labores auxiliares a agentes privados. Básicamente, se trata de las visitas en terreno; ello con el propósito de alcanzar una cobertura completa referente a las inspecciones in situ. Sin embargo, en este modelo quedan reservadas las principales atribuciones de una supervisión (intervención, sanción) para la SB. La Superintendencia controla permanentemente la idoneidad del agente privado y la calidad de sus trabajos (caso de Alemania).

3. Supervisión delegada → Regulación del Estado
→ Supervisión agente privado

La supervisión delegada implica que todas las funciones del fiscalizador se trasladen a un agente privado incluyendo la supervisión off-site, on-site, la intervención y las sanciones (p.e. Brasil).

4. Supervisión híbrida → Regulación del Estado
→ Supervisión de CAC's grupo A de importancia económica ⇒ SB
→ Supervisión de CAC's grupo B medianas y pequeñas ⇒ agente privado

La supervisión híbrida es un modelo mixto entre la supervisión directa y la supervisión delegada (p.e. Perú). Dos o más instancias concurren en la fiscalización. Las CAC's del sector están repartidos entre los diferentes agentes a raíz de criterios (criterios: CAC's abiertas, cerradas, volumen de operaciones, regiones, etc.). La Superintendencia controla permanentemente la idoneidad del agente privado y la calidad de sus trabajos.

5. Autorregulación → Regulación voluntaria del sector
→ Supervisión agente privado

Se trata de un modelo alternativo más bien teórico, ya que se desconocen ejemplos puros de este caso. Los ejemplos de Chile y Guatemala son los más asimilados.

VI. Pautas principales de la supervisión

Una regulación reglamentaria para el sector de las Cooperativas de Ahorro y Crédito implica la existencia de un marco legal con reglas y parámetros de prudencia. De esta manera el legislador facilita a los agentes de la supervisión evaluar la idoneidad de la gestión y la situación financiera. A continuación, se distingue entre las medidas protectoras y preventivas y se esbozan las pautas principales también aplicables para las CAC's:

1. Medidas Protectoras

- Garantizar la liquidez del sector a través del prestamista de última instancia (Caja Central Sectorial, Banco Central)
- Protección de depósitos (fondo de protección)
- Información sobre la solvencia de prestatarios (Central de Riesgo)

2. Medidas preventivas

2.1. Normas preventivas cuantitativas

2.1.1 Exigencias y Límites

- **Capital mínimo** en monto efectivo. Resulta apropiada la implementación de una matriz escalonada que segmente las CAC's en categorías. Los criterios de la escalonidad radican en diferentes exigencias de capital mínimo que permite el desarrollo de CAC's ya operando igual que la constitución de nuevas en función a su desarrollo y su solvencia. La categoría más alta debe pretender a las CAC's el mismo nivel de exigencia con capital como para los bancos y al otro lado facultarlas para ofrecer los mismos servicios. El monto mínimo para la categoría más baja no debe ser demasiado exigente para no impedir la constitución de nuevas Cooperativas.

- **Coeficiente de solvencia** (mínimo 8%), calculado sobre activos ponderados por riesgo. El coeficiente será uniforme para todas las CAC. El porcentaje no debe diferir de lo establecido para la banca. La estabilidad patrimonial en las CAC se logra a través de una regulación de la estructura patrimonial y la suficiencia de recursos patrimoniales depende del capital mínimo, calibrado por medio de categorías escalonadas y no será resultado de un coeficiente que altera de la norma de los bancos.

- **Norma de estructura patrimonial.** Las reservas no deben ser menores que el capital social, expresados en aportes. Para prevenir que esta regla impida la fundación de nuevas CAC's, se debe establecer períodos transitorios para instituciones recientemente constituidas.

- **Restricción de devolución de aportaciones.** Con el objeto de atenuar la volatilidad del capital social, se debe establecer un plazo (mínimo tres meses) para la devolución de las aportaciones a los socios. En ningún caso se puede liquidar un aporte antes de la próxima asamblea general.

- **Indice de liquidez.** Monitoreo I: los fondos disponibles (caja, bancos) y las partidas del activo que vencen dentro de los próximos 30 días (cartera normal, inversiones financieras) no deben ser menores frente a las obligaciones con caducidad dentro de los próximos 30 días. Además, se debe monitorear la liquidez a mediano plazo a través del Monitoreo II: los componentes activos con un vencimiento hasta 90 días no deben ser inferiores que 75% de las obligaciones, que vencen dentro del mismo plazo.

- **Indice de cobertura del activo fijo.** Las inversiones en activo fijo físico y en inversiones permanentes no pueden exceder el total del patrimonio.

- El **límite crediticio.** El monto máximo de un crédito a un prestatario o grupo de prestatarios es de 15% del patrimonio.

- El **total de créditos vinculados** (dirigentes, gerentes, planta ejecutiva) no debe exceder 15% del capital institucional, compuesto por las reservas. La cooperativa debe notificar cada crédito concedido con sus características y condiciones al supervisor.

- **Causal de intervención.** La gerencia o el Consejo de la cooperativa debe notificar una pérdida de 25% del patrimonio al supervisor.

2.1.2 Normas de Disciplina Administrativa

- La habilitación para que el intermediario financiero desarrolle las operaciones, debe encontrarse sujeta al otorgamiento de una **licencia de funcionamiento.**

- **Reglas de idoneidad** para dirigentes (Consejo de administración y Junta de Vigilancia). En particular se debe impedir la concesión de condiciones privilegiadas a este grupo. Se debe regular la transparencia de compensaciones que reciben para su participación en la diligencia de la cooperativa.

- Se **suspende el cargo de Director o Gerente**, tendiendo una morosidad superior a 5 días o créditos reprogramados debido a la morosidad con la CAC. Igual se aplica la norma si la persona exhibe morosidad en otra entidad del sistema financiero.

- **Se prohibe el financiamiento de aportes** con créditos de la cooperativa.

- La **calificación de las colocaciones**. Se evalúa la cartera de préstamos clasificándola en cinco categorías de riesgo. Las colocaciones de las CAC's se caracterizan por una cartera atomizada de una gran cantidad de préstamos de montos pequeños. Para economizar el procedimiento de la evaluación el criterio de la clasificación debe ser la morosidad del prestatario.

Categoría	Estado	Morosidad	Otro criterio
A	Normal	0 – 5 días	
B	Riesgo potencial	6 – 30 días	
C	Deficiencia	30 – 120 días	1 reprogramación
D	Dudoso	120 – 180 días	2 reprogramaciones
E	Perdido	180 – días	3 o más reprogramaciones

- En virtud de la calificación realizada, las CAC's deben aplicar un **régimen de provisiones/previsiones** específicas. Del monto a provisionar, solamente las aportaciones prendadas y las garantías hipotecarias se pueden descontar.

Categoría	Estado	Provisiones
A	Normal	-
B	Riesgo potencial	5%
C	Deficiente	20%
D	Dudoso	40%
E	Irrecuperable	80%

- Las CAC's deben constituir una **provisión genérica** de 1% sobre la cartera normal.

- A partir de 360 días de morosidad, el crédito debe ser **castigado** en un 100% de su monto contable, descontando el valor de las garantías realizadas.

- Se aplica un **catálogo único de cuentas.**

2.2. Normas Preventivas Cualitativas

- **Auditoría externa** obligatoria. Las empresas de auditoría externa deben estar registradas y autorizadas por la SB, la cual determina el alcance de las labores y el contenido de los informes de los auditores. Las empresas deben adjuntar a los anexos de los estados financieros una información financiera suplementaria, donde los auditores se pronuncian sobre el cumplimiento de las normas por parte de las CAC's.

- Las CAC's están obligadas a instalar **un sistema de control interno** funcional. Excediendo determinados volúmenes (total de activos) la cooperativa debe instaurar una oficina de auditoría interna. El auditor interno debe depender jerárquicamente de la Junta de Vigilancia.

3. Normas Organizacionales

- La normativa debe establecer la cobertura y las modalidades del pago de los costos de la supervisión. Rige el "Principio de causantes", por ende el sector debe cubrir los costos. Se debe aplicar un régimen escalonado de aportes, calculados en función al total de activos.

- Remisiones periódicas obligatorias de datos e informaciones al supervisor, que permite un monitoreo a distancia del desarrollo de la CAC (la norma debe prescribir el formato, el contenido y la fecha de entrega de las remisiones).

VII. Procedimientos de la Supervisión

1. Procesos clásicos

1.1. supervisión a distancia (off-site, en gabinete)

- reporte mensual de los indicadores claves

- remisiones periódicas de datos suplementarios y estados financieros

El supervisor debe retroalimentar las CAC's de la evaluación off-site.

1.2. Supervisión in situ (on-site)

- Inspecciones regulares. La periodicidad de las visitas puede variar en virtud del volumen de operaciones del intermediario. En el caso de las cooperativas grandes se debe programar una visita por año.

- Visitas de seguimiento. La cobertura de las medianas y pequeñas cooperativas se alcanza con inspecciones regulares en forma aleatoria complementadas por visitas de seguimiento en vez de una inspección regular. En el último de los casos, se trata de una visita breve de entre 1 y 5 días.

2. Metodologías facilitadoras en microfinanzas.

   El instrumental de la supervisión, básicamente debería ser igual para el sector de las cooperativas de ahorro y crédito como para la banca tradicional. Sin embargo, el ámbito de las microfinanzas requiere de aplicaciones y una tecnología de supervisión adaptada a las realidades del sector. En particular, se refiere al problema del gran número de las CAC's y su dispersión geográfica, junto con un nivel menos desarrollado en la preparación técnica y finalmente en una cartera de créditos atomizados. Son los factores, los cuales obstaculizan una supervisión en terreno, con una cobertura completa en el sector cooperativo.

   A continuación, se presentan algunas medidas facilitadoras concretas:

- **Colaboración con auditores externos.**

Pre-requisito será, que el alcance de los auditores esta regulada en detalle. De particular interés resulta normar las actividades acerca de la revisión de la cartera de créditos y otros activos riesgosos. Los auditores deben entregar una información suplementaria financiera sobre el grado de cumplimiento de la empresa fiscalizada. A través de los auditores externos se puede verificar la calificación de las colocaciones y la confiabilidad de los indicadores e informaciones remitidos periódicamente. Esta metodología permite efectos de economía de escala y contribuye en disminuir la duración y preparar las visitas de los inspectores de la SB.

- **La escalonidad.**

Se debe establecer una escala gradual de conformidad con los servicios financieros autorizado vinculados proporcionalmente a niveles diferentes de capital mínimo. En función a ello, se trata de aplicar un mayor grado de intensidad y frecuencia de la supervisión in situ en cooperativas que pertenecen a las categorías superiores y, por consiguiente, en menos visitas para las CAC's clasificadas en categorías inferiores.

♦ **Adaptación de las exigencias de la clasificación de cartera.**

La escala de la clasificación por morosidad debe ser adaptada para el ámbito de las microfinanzas y, por ende, debe variar de la matriz aplicada en los bancos. La morosidad de la clientela de las cooperativas no representa el mismo grado de riesgo de irrecuperabilidad que en los bancos. La clientela es más informal y la estabilidad de sus ingresos depende de una mayor cantidad de variables que en el caso de la clientela en la banca tradicional (p.e. pequeños agricultores con pago post cosecha).
Pese a que se considera al ámbito de las microfinanzas como más riesgoso, en comparación con las colocaciones tradicionales de los bancos, se observa –sin embargo- un mayor nivel de lealtad en la relación socio-cooperativa, debido especialmente a la regionalidad o fuerte penetración local que exhiben las CAC's.

Los factores señalados justifican que por las particularidades del microcrédito, se amplíen los parámetros que definen las categorías de la clasificación de cartera y, consecuencialmente, del régimen de provisiones/previsiones.

♦ **Subsidios.**

En una fase inicial o de piloto durante la cual se pretende implementar la supervisión en CAC's, se justifica subsidiar el elevado costo de la supervisión, a través de recursos del Estado o de organismos internacionales. La meta es lograr una cobertura completa.

VIII. Herramientas de la Supervisión

1. Herramientas de la evaluación son:

a) El sistema de información gerencial (MANAGMENT INFORMATION SYSTEM/MIS). A través de un número amplio de indicadores el MIS pretende medir el grado de eficiencia de la gestión, enfocando básicamente la rentabilidad y las estructuras del activo y del pasivo.

b) El monitoreo de indicadores de riesgo a distancia (ver anexo VIII/1 indicadores). El enfoque del análisis comprende básicamente los riesgos de las colocaciones (nivel de provisiones/previsiones, la cartera vencida, concentraciones, índices de expansión) y la solvencia. Resulta importante recalcar, se sugiera utilizar para el monitoreo de los factores de riesgo una cantidad bastante reducida de indicadores. Esto, con el motivo de facilitar al analista encargado de la supervisión un diagnóstico rápido. En cuanto al número de indicadores y su alcance, circunscrito a los elementos

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potencialmente riesgosos de una entidad financiera, el monitoreo se distingue del sistema de información gerencial (MIS).

c) Los informes de los inspectores del supervisor

d) Los dictámenes e informes de los auditores externos

e) Los informes de los auditores internos

2. Sanciones

Con frecuencia hay que constatar, que la regulación y las herramientas de la evaluación están bien desarrolladas y cercanas de los niveles de los países industrializados. Sin embargo, el tema de hacer respetar las normas a través de sanciones y multas todavía parece ser el talón de Aquiles.

3. La Intervención

a) Cursar amonestaciones con observaciones y advertencias
b) Aplicar multas
c) La suspensión transitoria de operaciones
d) La suspensión o cesación en el cargo de directores, gerentes o personal ejecutivo
e) Colocar un interventor o un liquidador

IX. El conflicto de la oportunidad

El conflicto surge de la meta de cumplir con dos pretensiones extremas:

a) Conceder el máximo de protección a los clientes y en particular a los depositantes y ahorrantes del intermediario financiero. La asimetría de informaciones entre la dirección de las entidades financieras y sus ahorrantes en cuanto a la solvencia y la liquidez de la institución requiere que las autoridades estatales supervisen eficazmente la gestión del intermediario. De tal modo, la Superintendencia protege también la estabilidad macroeconómica del país.

b) La prevención de la injerencia estatal en los mercados con énfasis a una libre competencia. Los mecanismos de un libre mercado deben autorregular su configuración, o sea la eliminación de intermediarios insolventes a través de fusiones y liquidaciones.

En síntesis, el legislador y las Superintendencias tienen que estudiar detenidamente cuales son los conceptos de la regulación y las medidas de la supervisión para calibrar prudentemente entre la gestión libre de los integrantes del mercado y la necesidad de proteger los ahorrantes individuales y la estabilidad de la macroeconomía.

Los parámetros para medir si se logró alcanzar la más justa conformidad de supervisión es el grado de autonomía que les queda a los intermediarios financieros, y el nivel de la protección de los depositantes y otros acreedores de los intermediarios.
El desafío en este aspecto radica en aplicar un instrumental eficaz de supervisión integral entre las inspecciones in situ y el monitoreo a distancia y prevenir intervenciones innecesarias y la construcción de un aparato burocrático.

X. Observaciones y recomendaciones derivadas de los casos investigados

1. La cobertura de la supervisión con visitas en terreno no es suficiente ni satisface en el caso de los modelos de supervisión directa. Se debe incrementar el nivel de inspecciones in situ. Por tal motivo, se debe estudiar la factibilidad de aplicar mecanismos mecanismos de supervisión auxiliar. Esto depende, en cada país, de la presencia de agentes privados idóneos capaces para colaborar en la supervisión.

2. Establecer una norma sobre la estructura del patrimonio es de recalcada trascendencia. Se debe estipular que los aportes en el capital social no excedan un 100% de las reservas legales.

3. La regulación vigente aplica una restricción débil para la devolución de aportes, lo cual permite al capital social de las Cooperativas ser un elemento muy volátil dentro del patrimonio. Por ende, se debe regular la devolución de los aportes y lograr la obligatoriedad de que el socio notifique el retiro de su capital social con una anticipación de a lo menos tres meses.

4. En el caso de la supervisión auxiliar o delegada, la atribución de imponer sanciones y multas debe ser privativa de la Superintendencia. Ambas facultades son propias y exclusivas de la autoridad y exceden de las facultades y tareas auxiliares de un ente privado. Se deben separar las tareas técnicas delegadas al agente privado, de las sanciones que son propias del Estado, así, evitar que el agente privado (Federaciones, etc.) incurra en conflictos de juez y parte.

5. La norma de prohibir la concesión de créditos vinculados a directores y ejecutivos es vulnerable a través de operaciones simuladas por inter pósita persona (palos blancos). Se recomienda reemplazar la prohibición por la obligación de notificar todos los créditos vinculados a la Superintendencia.

XI. Resumen de mejores prácticas

Area	Best practice
Regulación	a) Ley Bancaria *** b) Ley especial para CAC**
Modelo	a) Supervisión auxiliar*** b) Supervisión híbrida/delegada** c) Supervisión directa* Condición: las opciones o alternativas a) o b) sólo pueden resultar como modelos exitosos exclusivamente cuando exista un agente suficientemente idóneo para involucrarlo en la ejecución de la supervisión.
Procedimientos	Supervisión off-site y Supervisión on-site Se aplican conceptos de gradualidad y escalonidad
Pautas	Capital mínimo, coeficiente de solvencia, norma de estructura patrimonial, restricciones a la devolución de aportaciones, índice de liquidez, índice de cobertura de activo fijo, límites crediticios, límites y remisiones para créditos vinculados, reglas de idoneidad, calificación y clasificación de colocaciones, régimen de provisiones específicos y genéricos, castigos, catálogo de cuentas.
Herramientas	Management Information System Monitoreo de indicadores de riesgo a distancia (off-site) Informes de inspección in situ Dictamen e informes de auditores externos Informes auditores internos Sanciones Intervención

XII. Las implicancias de una regulación y supervisión incompleta o deficiente de los mercados financieros

La supervisión bancaria implementada en el sector cooperativo no implica automáticamente una mejoría en la calidad de la gestión de las CAC's. Sin perjuicio de ello, sin esta fiscalización especializada, habrá menos protección para los depósitos de ahorrantes de Cooperativas de Ahorro y Crédito.

La falta de una supervisión significa una discriminación que puede llegar a impedir el acceso a los servicios financieros para los estratos de bajos y medios ingresos a través de la limitación y/o la regulación negativa de la gestión de las Cooperativas de Ahorro y Crédito (se privilegia a la población de altos ingresos, vía selección de la clientela de bancos comerciales).

Una regulación y supervisión incompletas de la actividad financiera en términos que no se regule de igual manera y en base a los mismos criterios a todos aquellos entes que participan en este mercado, pone en serio riesgo la estabilidad de los sistemas financieros, lo que constituye una debilidad estructural indudable de cualquier sistema económico.

Por otra parte, al no incorporarse a todos los intermediarios financieros en la regulación y supervisión especializada en la materia financiera, la autoridad está –indirectamente– interviniendo y debilitando más aún la condición socioeconómica de gran cantidad de ciudadanos. Al mismo tiempo se impide el acceso de la población más pobre a servicios financieros en condiciones equitativas, y por otro lado se está dejando indefensos a amplios sectores sociales al no someterse a las entidades que administran sus recursos a una supervisión especializada. En definitiva, el Estado –de alguna manera– deja de asumir su responsabilidad social respecto de quienes más lo necesitan pareciendo restringir el bien común sólo a los sectores económicos altos.

Conforme con lo anterior, un aporte decisivo en el camino del desarrollo sostenible de los países, es la regulación y supervisión completa e integral de los mercados financieros, en razón de la especial naturaleza de dicha actividad, incorporando a todos los agentes, sin discriminación ni proteccionismo.

Sólo de esa forma se permite que todas las personas cuenten efectivamente con los mismos instrumentos para generar crecimiento, pudiendo ser partícipes del proceso de desarrollo y gozando al mismo tiempo de sus beneficios; y no – por el contrario – contribuyendo a aumentar las grandes diferencias económicas y sociales generadas por una desigual distribución del ingreso, cuestión que parece ser el capítulo negro y no superado aún de las economías en vías de desarrollo y emergentes.

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Indicadores Financieros para CAC

A. Indicadores de riesgo de las colocaciones

1. Indice de morosidad

$$\frac{\text{colocaciones categorías B,B-,C,D}}{\text{total colocaciones}^{1*}} \times 100$$

explicación: muestra el porcentaje de los créditos vencidos
meta: inferior al promedio del sector

2. Indice de riesgo

$$\frac{\text{provisiones sobre colocaciones (4205)}}{\text{total colocación}} \times 100$$

explicación: estimación de la cartera de créditos, considerados como irrecuperables
meta: no establecer meta

[1]* colocaciones: cartera de créditos

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3. Indice I de carga de riesgo sobre la rentabilidad

$$\frac{{}^{3*}\text{provisiones sobre colocaciones (6110,6120) + castigos directos (6270) – recuperación de colocaciones castigadas (8105)}}{\text{excedente del ejercicio + provisiones (6110, 6120)}} \times 100$$

explicación: el índice muestra el deterioro que sufre la rentabilidad de la CAC durante un ejercicio, derivado del riesgo de la cartera de créditos
meta: no superior a 5 %

4. Indice II de carga de riesgo

$$\frac{{}^{3*}\text{provisiones sobre colocaciones (6110,6120) + castigos directos (6270) – recuperación de coloc. castigadas (8105)}}{\text{total de activos}} \times 100$$

explicación: el índice permite comparar dentro del sector el nivel del deterioro proviniendo del riesgo de las colocaciones
meta: inferior al promedio del sector

[3*] cuenta de egresos

5. Indice de la expansión crediticia

$$\frac{\text{colocaciones fin de ejercicio – coloc. comienzo ejerc.}}{\text{colocaciones comienzo del ejercicio}} \times 100$$

explicación: el índice sirve para detectar una excesiva politica de expansión
meta: crecimiento no más allá de un 50 % del promedio del sector

B. Indicadores patrimoniales

6. Indice de patrimonio efectivo

$$\frac{\text{Patrimonio}^{4*}}{\text{activos ponderados de riesgo}^{4*}} \times 100$$

explicación: el índice mide la solvencia en base a las directrices del Acuerdo de Basilea.
meta: igual o superior a 8 %.

4* componentes ver Circular S.B.I.F. N° 2.916/1.211 del 22.01.1998 sobre patrimonio para efectos legales y reglamentarios.

7. Indice de solvencia

$$\frac{\text{reservas (4310, 4315, 4320) + provisiones voluntarias (4245)}}{\text{activos ponderados de riesgo}} \times 100$$

explicación: el índice mide la solvencia a través de la última partida, que sirve para absorber pérdidas de la gestión antes de recurrir al capital social
meta: igual o superior a 4 % (la mitad de la exigencia del Acuerdo de Basilea)

8. Indice de la estructura patrimonial

$$\frac{\text{reservas (4310, 4315, 4320)}}{\text{patrimonio}} \times 100$$

explicación: indica la relación entre las reservas y los demás componentes del capital propio
meta: reservas superior a 50 %

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9. Indice de financiamiento del activo no circulante

$$\frac{\text{activo fijo físico (2305) + inversiones en sociedades (2320)}}{\text{capital pagado y reservas (4305, 4310, 4315, 4320)}} \times 100$$

explicación: el índice reporta el grado de autofinanciamiento del activo fijo
meta: cobertura 100 %

C. *Indicadores de rentabilidad*

10. Indice de rentabilidad operativa

$$\frac{\text{excedente + provisiones sobre colocaciones (6110, 6120) + castigos directos (6270)}}{\text{promedio * total de activo}} \times 100$$

$$\text{calculo: total de activo } \frac{(01.01. + 31.03. + 30.06. + 30.09. + 31.12.)}{5}$$

explicación: muestra el nivel de la rentabilidad operativa y sin cargas derivadas del riesgo de las colocaciones
meta: superior al promedio

11. Indice de rentabilidad neta

$$\frac{\text{excedente}}{\text{promedio total de activo}} \times 100$$

explicación: muestra la rentabilidad de la gestión
meta: superior al promedio

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12. Indice del gasto personal

$$\frac{\text{gastos del personal y directorio (6205...)}}{\text{Promedio total del activo}} \times 100$$

explicación: índice que analiza las variaciones internas entre ejercicios; adicionalmente apto para comparar el nivel de este costo con el sector
meta: inferior al promedio

13. Indice de gastos administrativos

$$\frac{\text{gastos de administración (6230...)}}{\text{promedio total de activo}} \times 100$$

explicación: índice que analiza las variaciones internas entre ejercicios; apto para comparar el nivel de este costo con el sector
meta: inferior al promedio del sector

D. *Indicadores de Liquidez*

14. Indice I de relación entre operaciones activas y pasivas

$$\frac{\text{pasivos}^{7*}\text{ con vencimiento hasta 30 días}}{\text{activos}^{7*}\text{ con flujo de capital hasta 30 días}} \times 100$$

explicación: demuestra la capacidad de enfrentar compromisos de pagos a plazo inmediato
meta: 100 %

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15. Indice II de relación entre operaciones activas y pasivas

$$\frac{\text{pasivos}^{7*}\text{ con vencimiento hasta 90 días}}{\text{activos}^{7*}\text{ con flujo de capital hasta 90 días}} \times 100$$

explicación: Indice de monitoréo de la capacidad de pago a mediano plazo
meta: 100 %

16. Indice de la estructura de operaciones activas y pasivas a largo plazo

$$\frac{\text{colocaciones con vencimiento} > 12\text{ meses + activo no circulante (2305,2320)}}{\text{partidas pasivas}^{8*}\text{ de largo plazo + capital y reservas}} \times 100$$

explicación: Indice de equilibrio de montos y de apalancamiento de plazos entre las partidas del financiamiento y de la colocación. Se aplican cálculos de contingencia para determinar las partidas pasivas pertinentes
meta: no superior a 100 %

[7*] componentes activos y pasivos por motivo del cálculo del calce de operaciones activas y pasivas determinadas en la circular n° 3.001/Bancos de la S.B.I.F.

[8*] partidas pasivas para el cálculo:
- capital y reservas (4305, 4310, 4315, 4320) 100 %
- captaciones con vencimiento > 12 meses 100 %
- partidas contingentes
  captaciones y prestamos con vencimiento > 30 hasta 90 días 10 %
  captaciones y prestamos con vencimiento > 90 días hasta 360 días 30 %
  ahorros 40 %

E. *Indicadores de la estructura*

17. Indice del activo improductivo

$$\frac{\text{otras cuentas del activo (2110,2115,2120) + activo fijo físico (2305) + inversiones en sociedades }^{9*}\text{ (2320)}}{\text{total de activos}} \times 100$$

explicación: índice que pretende limitar las inversiones improductivas
meta: inferior a 6 %.

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Mejoras Prácticas en Supervisión – Sinópsis del diagnóstico de los casos Bolivia – Ecuador - Perú

Criterios	Bolivia[1]	Ecuador[2]	Perú
A. **Datos sectoriales**[3]			
- Cantidad total de CAC's	113	350	201
- Federación	Las CACs se afiliaron a diversas instituciones gremiales.	Las CACs están afiliadas a diversas instituciones gremiales.	Si
- Caja Central	No	Si, FINANCOOP (48 CACs afiliadas)	Si, se encuentra en la fase inicial
- Sistema informático único sectorial	No, pero básicamente concentrado en dos sistemas	No, pero básicamente concentrado en dos sistemas	No
- Central de riesgo	Si, pero acceso solamente para las 30 CACs supervisadas	Si, pero acceso solamente para las 27 CACs supervisadas	Si, las CACs tienen acceso
- Protección de depósitos	No para los ahorrantes de las CACs Para la banca existe un Fondo de Protección de Depósitos	Si, para los ahorrantes de las CACs supervisadas	No para ahorrantes de las CACs Para la banca existe un fondo de seguro de depósitos
- Número de socios del sector	368.396[4]	1.500.000	331.277
- Número de socios v/s población económicamente activa	11,9% (3.093 mil)	18,8% (8.000 mil)	3,3% (10.038 mil)
- Total de activos	299 Mio US$	158 Mio US$	245 Mio US$
B. Regulación			
- Regulación de las operaciones financieras de las CAC's	a) Para cooperativas que captan de sus socios o de terceros, mediante cuentas del pasivo, rige la Ley de Bancos e Instituciones Financieras. b) Cooperativas que sólo realizan operaciones de intermediación financiera de ahorro y crédito entre sus socios, quedan excluidas de la Ley y en consecuencia, carecen de regulación.	a) Para las cooperativas calificadas ante los criterios de la SB, como CAC DE INTERMEDIACION FINANCIERA CON EL PUBLICO. b) Las cooperativas que no obtienen esta licencia quedan excluidas de la Ley y en consecuencia, carecen de una regulación de sus operaciones.	Ley General del Sistema Financiero y de Seguros y Orgánica de la Superintendencia de Bancos y Seguros – SBS.
- Cobertura de la regulación	30 de 113 CACs = 26,5% del total del sector (24 CACs con Licencia de CAC abierta además, 6 CACs en trámite de reconocimiento, a las cuales ya se aplica	27 de 350 CACs = 7,7% del total del sector (100% urbanas, ninguna rural) estimación: 65% de cobertura del total de activos del sector	100% de las CACs del sector Peruano

[1] En base a 50 de las 113 Cooperativas
[2] En base a 50 de las 350 Cooperativas
[3] Al 31.12.2000
[4] En el caso de Bolivia se presenta la cantidad de cuentas, puesto que no existe una estadística sobre el total de los socios.

	la normativa)		
- Normativa detallada	– Decreto Supremo N°24.439: Definición de CAC abierta y sujeta a supervisión – Recopilación de Normas para Bancos y Entidades financieras de la SBEF	– Codificaciones de resoluciones de la SB y del Banco Central – Decreto ejecutivo N°1.227 de N°1.998 Reglamento de la Ley General de Instituciones Financieras para Cooperativas de Ahorro y Crédito – Catalogo único de cuentas de la SB (rige para las 27 CACs supervisadas)	- Reglamento de CACs; resolución N°0540 de la SBS 16.06.1999 - Resoluciones complementarias de la SBS - Circulares de las SBS - Cartas Circulares de FENACREP
- Pautas principales	1. Licencia de funcionamiento 2. Exigencia de capital mínimo (CACs segmentadas por categorías) 3. Coeficiente patrimonial (exigencias varían en función a la categoría) 4. Prohibido otorgar créditos a Directores o Ejecutivos y todos quienes pudiesen comprometer a la institución bajo su sola firma 5. Créditos a una sola entidad financiera; máx. 20% 6. Créditos al personal, en conjunto, hasta 1,5% patrimonio neto (PN) 7. Créditos individuales al personal hasta 0,15 del PN 8. Créditos con garantía personal a un prestatario/grupo hasta el 3% del PN 9. Créditos con garantía personal a un prestatario/grupo hasta el 1% del PN 10. Calificación y clasificación de cartera de créditos en 5 categorías 11. Régimen de provisiones en función de la calificación: 12. Directores no pueden tener deudas morosas en el sistema financiero 13. Directores no pueden ser socios de otras CACs 14. Obligaciones subordinadas, como parte del patrimonio neto, hasta 50% del capital pagado	1. Reglas de idoneidad para Gerentes y Directivos 2. Licencia de funcionamiento 3. Capital mínimo: US$ 750.000.- 4. Coeficiente patrimonial: 9%, calculado sobre activos ponderados por riesgo 5. Norma de estructura patrimonial (reservas no menor al equivalente de 50 % del capital social); las CACs deben asignar como mínimo un 10% de sus excedentes a las reservas. 6. Monto mínimo de aportes: US$ 0,40 7. El plazo de liquidación de un aporte es de 30 días, en caso de retiro de un socio 8. Coeficiente de liquidez (en partidas liquidas hasta 30 días; deben tener mínimo 14% del monto en obligaciones vencidas dentro de 30 días) 9. El total de los créditos vinculados no debe exceder 10% del patrimonio técnico; el crédito a un sólo Director no debe superar individualmente 2% del patrimonio técnico. 10. Clasificación contable de la cartera 11. Calificación y clasificación de la cartera de créditos en 5 categorías 12. Régimen de provisiones en función	1. Reglas de idoneidad, impedimentos, responsabilidades para Gerentes y Directivos (p.e. las dietas para dirigentes, después de 120 días en morosidad, suspensión del cargo). 2. Contenido y formato del informe trimestral de la Gerencia a los Consejos 3. Coeficiente de solvencia (el monto de los activos y créditos contingentes, ponderados por riesgo, no pueden exceder de 11 veces su patrimonio efectivo (= 9,1 %). 4. Norma de estructura patrimonial (reservas no menor al equivalente de 35 % del capital social) 5. Monto mínimo de aportes 6. Límite crediticio (monto total máximo a un prestatario: 5% del patrimonio efectivo) 7. Límites de financiamiento de activo fijo e inversiones (activo fijo físico no podrá exceder 40% del patrimonio efectivo; inversiones permanentes no podrán exceder 15% del patrimonio efectivo; créditos/inversiones en cooperativas o empresas de apoyo al giro no pueden exceder 20%). 8. Causales de la intervención (la pérdida de 50% del patrimonio

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	15. Devolución de aportaciones, prohibido en caso de incumplimiento de límites legales o pérdidas Acumuladas o de gestión 16. Inversiones en activos fijos no mayor al PN 17. Inversiones permanentes en sociedades, sólo en aquellas en las que sea requisito indispensable la Asociación para recibir el servicio 18. Créditos de otras entidades financieras hasta 1 vez el PN 19. Bienes adjudicados para recuperación de créditos deben s vendidos en el plazo de 1 año (mueble o 2 Años (inmuebles) 20. Auditor interno obligatorio (depende de la Junta de Vigilancia)	de la calificación: 13. El monto máximo de un crédito a un prestatario o grupo de prestatarios es de 10% del patrimonio técnico (20% créditos con garantías). 14. Se suspende el cargo de Director o Gerente teniendo deudas en morosidad superior a 60 días en el *sistema financiero* 15. Inversiones en activos fijos: No mayor al patrimonio técnico 16. Remisión de datos e informaciones a la SB. 17. *Auditoría externa: Obligatoria para* las CACs supervisadas; el reglamento para los auditores externos establece que, solamente empresas registradas y autorizadas por la SB pueden realizar *la auditoría* de los Estados Financieros en CACs. 18. Auditoría interna: Obligatoria para las CACs supervisadas. 19. Manual de Cuentas Uniforme: Del sistema *financiero rige* obligatoriamente para las 27 CACs supervisadas.	efectivo) y los procedimientos 9. *Prohibición de conceder créditos* para el financiamiento de aportes en la misma CAC. 10. La distribución de facultades y tareas para la regulación (SBS) y *Supervisión* (FENACREP); las atribuciones de la Federación, las modalidades de la inspección. 11. La fiscalización de la supervisión delegada 12. Sanciones y multas 13. Fondo de Contingencia 14. Auditoría interna (remisión obligatoria del informe anual a la Federación); en CACs de menor tamaño se permite outsourcing de la *auditoría interna.* 15. Auditoría externa obligatoria para todas las CACs de categoría I[5] (74 CACs con un total de activos superior a 800.700 soles = 225 mil US$; las empresas tienen que estar registrados y autorizados; se establecieron exigencias mínimas del contenido y de la estructura de los Informes). 16. Contenido, formato y periodicidad de las remisiones a la Federación 17. La distribución de remanentes 18. El costo de la supervisión
C. Modelo de supervisión			
- Supervisión directa	30 CACs están autorizadas de captar, vía pasivos, de socios y no socios	27 CAC's	Para todas las CACs, *que captan de no* socios Actualmente ninguna CAC
- Supervisión híbrida/delegada	No procede	No procede	Todas las otras CACs, las cuales captan de sus socios por vía pasivo o aportes, 181 del total de las 201 CACs del sector

[5] Segmentación del sector en categoría I

- Autorregulación	No procede	No procede	No procede
- Sin Supervisión especializada	83 CACs calificadas como "cerradas"	323 CAC's	No procede
D. Procesos de supervisión			
- CAC's supervisadas	30 del total de las 113 del sector	27 del total de las 350 del sector	181 del total de las 201 del sector
- Instancia a cargo de la supervisión	Superintendencia de Bancos e Instituciones Financieras SBEF Intendencia no bancaria División "Cooperativas de Ahorro y Crédito"	Superintendencia de Bancos (SB)	Unidad de Supervisión de FENACREP
- Personal de la Supervisión	Total: 8 ejecutivos fijos más 3 colaboradores a tiempo parcial 1 jefe de división 7 supervisores (2 en la sucursal Santa Cruz) 3 analistas de sistemas (personal para tareas puntuales)	Total 9 ejecutivos fijos más 3 analistas a tiempo parcial: 1 jefe de la unidad de inspección 8 inspectores (en 4 sedes) 3 analistas a cargo de la recaudación de las informaciones extra-situ	Total 11 ejecutivos: 1 jefe de la unidad de control 1 secretaria 4 analistas 3 inspectores fijos 2 inspectores contratados a honorario
- Costos de la supervisión	Aporte anual 0,1 % calculado sobre total de activos, cobranza semestralmente.	Aporte anual 0,095% calculado sobre total de activos	A cargo de las CACs; ellas pagan 0,2% sobre su total de activos a FENACREP.
- Supervisión off-site	Sí	Sí	Sí
- Mecanismos de monitoreo	Las CACs reportan mensualmente	1. Las CACs reportan mensualmente 2. Los auditores externos entregan para cada CAC, anualmente, un informe de información financiera complementaria sobre el cumplimiento de las pautas bancarias establecidas. 3. Los auditores internos remiten trimestralmente sus informes	Las CACs reportan mensualmente
- Número de CAC's monitoreadas	30	27	181
- Informe de retroalimentación	Carta de resumen de la evaluación trimestral (incluye el informe de la situación financiera y patrimonial)	Ficha de análisis por cada CAC (indicadores macro diseñados sobre CAMEL)	Trimestralmente información financiera
- Supervisión in situ (on-site)	Sí	Sí	Sí
- Plan de inspección	Anual, cronograma GANTT	Plan anual, elaborado por jefe de inspectores	Anual
- Número de inspecciones anuales	13 CACs: Programadas de visitas ordinarias 17 CACs: Visitas de seguimiento	12 CACs programadas de visitas ordinarias 15 CACs, visitas de seguimiento	37 CAC's programadas 10 CACs al aleatorio
- Cobertura con visitas anuales	11,5 % del sector (13 sobre 113 CACs)	7,7% del sector (27 sobre 350 CACs)	26 % del sector (sobre 181 CACs que

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			reportan)
- Duración de inspecciones	10 días, *mínimo (incluye 5 días para el* informe) 18 días, máximo (incluye 3 días para el informe)	40 días mínimo (incluye 5 días para el informe) 60 días máximo (incluye 3 días para el informe)	4 días, mínimo 18 días, máximo
- Criterio del cálculo de duración	Tamaño y complejidad de la CAC	Tamaño y complejidad de la CAC	Tamaño y complejidad de la CAC
- Planificación de las visitas	Si, con memorándum de visita, *emitida* por el encargado de cada CAC	*Si, con memorándum* de visita, emitido por el encargado de cada CAC	Si, con memorándum de visita, emitido por el jefe de unidad
- Modalidades	Equipo de trabajo	Equipo de trabajo	Un inspector o equipo
- Aviso de la visita de inspección	Si, con 5 días de anticipación.	Si, con 14 días de anticipación (carta del primer día).	Si, con 3 *días de anticipación.*
- Alcance de la inspección	Gestión, administración, gobernabilidad Cartera de créditos Contabi*lidad*	*Evaluación de la gestión administrativa* Calificación de activos de riesgo Principales cuentas del balance Contabilidad Ingresos y gastos Cumplimiento de *observaciones* de inspecciones o auditorías (internas y externas) anteriores	Gestión del Consejo de Administración y de Gerencia Sistema de control interno Auditoría interna Gestión administrativa y contable Solvencia, liquidez, estructuras de financiamiento Procesos de administración de cartera de créditos Carpetas de crédito
- Instrucciones y papeles de trabajo	Para contabilidad Para control interno Para administración Para créditos (hallazgo general, hallazgo *específico)*	No hay formularios estándares, *los* inspectores aplican formatos individuales, autodiseñados por ellos	*Manual* de control interno e inspección (versión mayo 2001) Manual de procedimientos de inspección (versión abril 2001) Hoja de revisión de créditos
- Informe escrito de la inspección	Sí	Sí	*Sí*
- *Contenido informe* de inspección	- Conclusiones de la evaluación financiera (PERLAS) - Cálculo del patrimonio neto - *Dirección y administración* - Auditoría interna - Cartera de créditos (tamaño de muestra de créditos, alcance de la revisión de la muestra de cartera) - *Contabilidad* - Sistemas de información - Observaciones - Evaluación de consistencia de previsión	1. Capítulo I: Información introducida 2. *Capítulo II:* Seguimiento de recomendaciones 3. Capítulo III: Rubros y áreas examinadas (gestión del Consejo de Administración, del Consejo de *Vigilancia, de Gerencia* General y de auditoría interna, fondos disponibles, - evaluación de la calificación de activos de riesgo: a) inversiones; b) cartera de créditos; c) cuentas por cobrar; d) *otros activos* – control de garantías, garantías bancarias,	1. Resumen ejecutivo Antecedentes Principales observaciones 2. Contenido del informe: *Riesgo de liquidez,* Riesgo crediticio Otros activos sujetos a riesgo Aspectos contables Grado de implementación del informe *de visita anterior* Auditoría interna Auditoría externa Suficiencia patrimonial

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	- Conclusiones y recomendaciones	cuentas de resultados.	Grado de cumplimiento de normas legales
- Informe verbal	Sí	Sí	Sí

MEJORES PRACTICAS EN SUPERVISION
Diagnóstico del caso de
B O L I V I A

A. Datos sectoriales[1]

Cantidad total de CACs	113
Federación o Asociación Gremial	No existe un vocero o interlocutor único del sector. Las CACs se afiliaron a diversas instituciones gremiales: FENACRE (en proceso de liquidación) FEBOCAC (*nueva Federación, recién constituida*) ASOCAF, Asociación que reúne la mayoría de las CACs sujetas a la SBEF ASOFIN, Asociación de Financieras y algunas CACs Federaciones departamentales
CACs afiliadas	A FEBOCAC solamente Federaciones Departamentales ASOCAF 20 CACs ASOFIN 2 CACs
Afiliación obligatoria	No
Caja Central	No
Sistema informático único sectorial	No, pero básicamente concentrado en dos sistemas
Central de riesgo	Si, pero acceso solamente para las 30 CACs supervisadas
Protección de depósitos	No para los ahorristas de las CACs Para la banca existe un Fondo de Protección de Depósitos
Número de cuentas de ahorro	368.396
Número de socios v/s población económicamente activa (3.093 mil)	11,9%
Total de activos	299 MioUS$[2]
Colocaciones v/s total activos	76,0%
Cartera vencida[3] v/s colocaciones	17,3 %

[1] Cifras al 31.12.2000 de 50 CACs económicamente más relevantes; Fuente: UNDESCOOP
[2] Estadística sobre socios es incompleta
[3] Cartera vencida a partir del primer día y cartera en ejecución

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Indice de riesgo[4]	8,0 %
Activo fijo+inversiones permanentes v/s reservas + ajustes	112,9 %
Captaciones v/s total activos	75,7 %
Endeudamiento bancario[5]	7,1 %
Coeficiente de solvencia[6]	2,96%
Rentabilidad neta[7]	-1,23%

B. Regulación

Regulación de las operaciones financieras de las CACs	a) Para cooperativas que captan de sus socios o de terceros, mediante cuentas del pasivo, rige la Ley de Bancos e Instituciones Financieras (Ley N°1.488). b) Cooperativas que sólo realizan operaciones de intermediación financiera de ahorro y crédito entre sus socios, quedan excluidas de la Ley y en consecuencia, carecen de regulación (Artículo N°70 Ley de Bancos e Instituciones Financieras).
Cobertura de la regulación	30 de 113 CACs = 26,5% del total del sector (24 CACs con Licencia de CAC abierta además, 6 CACs en trámite de reconocimiento, a las cuales ya se aplica la normativa)
Normativa detallada	A. Decreto Supremo N°24.439: Definición de CAC abierta y sujeta a supervisión B. Recopilación de Normas para Bancos y Entidades financieras de la SBEF Título I: Autorizaciones - Capítulo 1: Constitución y funcionamiento; sección 2 para CACs - Capítulo 2 : Sucursales y Agencias Título II: Transparencia de información - Capítulo 1: Informes periódicos de la SBEF - Capítulo 2: Manual de cuentas - Capítulo 3: Informes y Balances Semestrales requeridos

[4] Indice de riesgo: Provisiones v/s total de colocaciones; para el sector rige la obligatoriedad de generar 1 % de provisiones genéricas además, de las provisiones específicas.
[5] Endeudamiento bancario: Préstamos bancarios v/s total activos
[6] Reservas v/s total de activos
[7] Remanente v/s total de activos

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- Capítulo 4: Reporte de tasas de interés
- Capítulo 5: Reporte de estratificación de depósitos
- Capítulo 6: Reporte de calce de plazos
- Capítulo 7: Información sobre deuda externa
- Capítulo 8: Información de comisiones por servicio
- Capítulo 9: Memoria anual de las Entidades financieras
- Capítulo10: Publicidad

Título III: Auditores externos
Título IV: Síndicos o Comisiones fiscalizadoras, auditores internos y peritos evaluadores
Título V: Cartera de créditos

- Capítulo 1: Evaluación y calificación de la cartera de créditos (evaluación y calificación, régimen de provisiones, responsabilidades, acciones judiciales, castigo de créditos y registro de cuentas de orden, garantías, evaluación de garantías, información y documentación mínima).
- Capítulo 2: Operaciones de microcrédito debidamente garantizadas
- Capítulo 3: Operaciones de consumo debidamente garantizadas

Título VI :Central de información de riesgo
Título VII : Inversiones
Título VIII: Obligaciones
Título IX: Control y supervisión

- Capítulo 1: Visitas de inspección
- Capítulo 2: Control de encaje legal
- Capítulo 7: Activos fijos
- Capítulo 8: Reglamento de control de suficiencia patrimonial y ponderación de activos

Título X : Normas generales
Título XI : Responsabilidades de Directores y Gerentes
Titulo XII : Fusión, transformación, disolución y liquidación forzosa
Titulo XIII : Multas y sanciones

Pautas Principales

1. Licencia de funcionamiento
2. Exigencia de capital mínimo (CACs segmentadas por categorías)

Categoría I	150.000 DEG	–	195.000 US$
Categoría II	250.000 DEG	–	325.000 US$
Categoría III	630.000 DEG	–	819.000 US$
Categoría IV	5.500.000 DEG	–	7.150.000 US$

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3. Coeficiente patrimonial (exigencias varían en función a la categoría)
   05 CAC en Categoría I coeficiente 20%
   13 CAC en Categoría II coeficiente 15%
   11 CAC en Categoría III coeficiente 10%
   01 CAC en Categoría IV coeficiente 10%
4. Prohibido otorgar créditos a Directores o Ejecutivos y todos quienes pudiesen comprometer a la institución bajo su sola firma
5. Créditos a una sola entidad financiera; máx. 20%
6. Créditos al personal, en conjunto, hasta 1,5% patrimonio neto (PN)
7. Créditos individuales al personal hasta 0,15 del PN
8. Créditos con garantía personal a un prestatario/grupo hasta el 3% del PN
9. Créditos con garantía personal a un prestatario/grupo hasta el 1% del PN
10. Calificación y clasificación de cartera de créditos en 5 categorías

Categoría I: Créditos normales hasta 5 días morosidad
Categoría II: Créditos con problemas potenciales de 6 – 30 días
Categoría III: Créditos deficientes de 31 – 60 días o 1ª. Reprogramación
Categoría IV: Créditos dudosos de 61 – 90 días o 2ª. Reprogramación
Categoría V: Créditos perdidos de 91 en adelante o 3ª. ó más Reprogramaciones

Nota: La cartera de créditos esta segmentada en 4 tipos de créditos: microcréditos, comercio, consumo, hipotecario; en el caso de los créditos hipotecarios y de comercio, la clasificación varía insignificativamente de acuerdo a la matrix, arriba esbozada.

11. Régimen de provisiones en función de la calificación:

a) Créditos normales : 1% previsión genérica
b) Créditos con problemas potenciales: 5% previsión específica
c) Créditos deficientes: 20%
d) Créditos dudosos : 50%
e) Créditos perdidos :100%

12. Directores no pueden tener deudas morosas en el sistema financiero
13. Directores no pueden ser socios de otras CACs
14. Obligaciones subordinadas, como parte del patrimonio neto, hasta 50% del capital pagado
15. Devolución de aportaciones, prohibido en caso de incumplimiento de límites legales o pérdidas Acumuladas o de gestión

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16. Inversiones en activos fijos no mayor al PN
17. Inversiones permanentes en sociedades, sólo en aquellas en las que sea requisito indispensable la Asociación para recibir el servicio
18. Créditos de otras entidades financieras hasta 1 vez el PN
19. Bienes adjudicados para la recuperación de créditos deben ser vendidos en el plazo de 1 año (muebles) o 2 Años (inmuebles)
20. Auditor interno obligatorio (depende de la Junta de Vigilancia)

C. Modelo de supervisión

Supervisión directa	30 CACs están autorizadas de captar, vía pasivos, de socios y no socios
Supervisión delegada/auxiliar	No procede
Autorregulación	No procede
Sin supervisión especializada	83 CACs calificadas como "cerradas"

D. Procesos de supervisión

CACs supervisadas	30 del total de las 113 del sector
Ente a cargo de la supervisión	Superintendencia de Bancos e Instituciones Financieras SBEF Intendencia no bancaria División "Cooperativas de Ahorro y Crédito"
Personal División SBEF	Total: 8 ejecutivos fijos más 3 colaboradores a tiempo parcial 1 jefe de división 7 supervisores (2 en la sucursal Santa Cruz) 3 analistas de sistemas (personal para tareas puntuales)
Organización	*Los supervisores emprenden la supervisión en gabinete y in-situ; cada ejecutivo tiene adjudicado una cantidad* de CACs (entre 3 y 5)
<u>Supervisión off-site</u>	Si
Mecanismos de monitoreo	Las CACs reportan mensualmente
Número de CACs monitoreadas	30
Evaluación	- Informe de la situación financiera y patrimonial I. Introducción

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II. Situación Financiera: 1) protección 2) estructura financiera 3) rendimiento y costos 4) liquidez 5) activos improductivos 6) señales expansivas
III. Plan empresarial, protecciones financieras, plan de acción
IV. Límites y prohibiciones
V. Conclusiones y recomendaciones
VI. Anexo PERLAS
VII. Balance General
VIII. Estado de resultados
IX. Revisión de cumplimiento de limites legales

- Informe Sistema Cooperativo Consolidado, semestral

Retroalimentación a las CAC	Carta de resumen de la evaluación trimestral (incluye el informe de la situación financiera y patrimonial)
<u>Supervisión in-situ (on-site)</u>	Si
Plan de inspección	Anual, cronograma GANTT
Número de inspecciones anuales	13 CACs: Programadas de visitas ordinarias 17 CACs: Visitas de seguimiento
Cobertura	11,5 % del sector (13 sobre 113 CACs)
Duración de inspecciones[8]	10 días, mínimo (incluye 5 días para el informe) 18 días, máximo (incluye 3 días para el informe)
Criterio de cálculo de duración	Tamaño y complejidad de la CAC
Duración de visitas de seguimiento	1 – 2 días
Planificación	Si, con memorándum de visita, emitida por el encargado de cada CAC
Configuración personal	Equipo de trabajo
Aviso de inspección	Si, con 5 días de anticipación Causa: las CACs tienen que preparar la información requerida por los inspectores; no existe un sistema electrónico único para el sector al cual los inspectores tengan acceso.
Alcance de la inspección	Gestión, administración, gobernabilidad Cartera de créditos Contabilidad
Instrucciones y papeles de trabajo	- Para contabilidad - Para control interno - Para administración - Para créditos (hallazgo general, hallazgo específico)

[8] En circunstancias normales y sin que la CAC exhiba índices mayores de riesgo o deficiencias

Informe por escrito de la inspección: Si

Contenido del informe de inspección:
- Conclusiones de la evaluación financiera (PERLAS)
- Cálculo del patrimonio neto
- Dirección y administración
- Auditoría interna
- Cartera de créditos (tamaño de muestra de créditos, alcance de la revisión de la muestra de cartera)
- Contabilidad
- Sistemas de información
- Observaciones
- Evaluación de consistencia de previsión
- Conclusiones y recomendaciones

Informe oral: Si

Veredicto ejecutivo:

1. Las CACs de Bolivia están insertas solamente en forma parcial en la regulación bancaria. La Ley N°1.844 de Marzo 1993 distingue entre CACs abiertas y cerradas. Para el último grupo no rige la normativa bancaria.
2. El sector carece todavía del reconocimiento completo como parte del sistema financiero nacional.
3. La intermediación de no más del 26% de las CACs que operan en el país, está supervisada a través de monitoreo off-site e inspecciones in-situ. Las técnicas aplicadas por parte de las SBEF son profesionales, con una tendencia a exagerar la parte de exigencias formales y trabajos en gabinete.
4. El modelo implementado por la legislación Boliviana es la Supervisión Directa de un grupo seleccionado de CAC. La regulación no estableció ninguna modalidad aparte para la supervisión de las CACs cerradas, que representan 74% de los que integran el sector.
5. El modelo de la supervisión directa ejecutado a través de la SBEF es técnicamente viable. La SBEF cumple con el rol definido en la normativa.
6. En general las pautas y límites establecidas, igual que las técnicas aplicadas, permiten prevenir una debida gestión en las 30 CACs sujetas a la fiscalización e inspiran suficiente seguridad para los depositantes/ahorristas. Con el propósito de perfeccionar las técnicas de Supervisión Directa y enmendar la normativa en pos a una cobertura completa de regulación y supervisión de todas las CACs del sector, se agrega a continuación un módulo con observaciones y recomendaciones.
7. Con la modalidad de circunscribir la regulación y supervisión de la intermediación financiera de las CACs, a un grupo reducido de CACs abiertas, Bolivia cumple todavía solamente en forma parcial con las exigencias del Acuerdo de Basilea, emitidas por el Comité de Supervisión del Banco de Pagos Internacionales.

Observaciones y recomendaciones	↬ Todavía no existe en Bolivia un interlocutor único y reconocido que pueda negociar los intereses del sector con el legislador y las autoridades. Las Federaciones o Asociaciones no han calificado en pos a esa misión. ↬ No hay en este momento un ente sectorial idóneo, al cual se puede delegar facultades y tareas de un supervisor auxiliar. ↬ La interpretación de la SBEF acerca de las CACs cerradas, está cuestionada por algunas CACs individuales. Ellas interponen, aunque captan por cuentas del pasivo, mientras suscriban sus operaciones a sus socios deben estar exentas de disposiciones de la Ley Bancaria. ↬ La norma de prohibir la concesión de créditos, vinculados a Directores y Ejecutivos, es vulnerable a esquivaciones (palos blancos). Se recomienda reemplazar la prohibición por la obligación de notificar todos los créditos vinculados a la SBEF. ↬ La cobertura de la supervisión con visitas en terreno aún, no es suficiente ni satisface. Se debe incrementar el nivel de inspecciones in-situ a un 50 % anual. ↬No existe una norma sobre la estructura del patrimonio; se debe estipular que las aportaciones no sobrepasen 100% de las reservas. ↬ Se debe regular la devolución de las aportaciones; el objetivo es atenuar su volatilidad; lograr la obligatoriedad que el socio avise el retiro de su capital social en un plazo de a lo menos 3 meses.

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E C U A D O R

A. Datos sectoriales[1]

Cantidad total de CACs	350
Federación o Asociación Gremial	Las CACs están afiliadas a diversas instituciones gremiales. Ninguno de ellos representa al sector. FECOAC Asociación de CACs bajo supervisión
CACs afiliadas	FECOAC (20 CACs activas) Asociación (21 CACs)
Afiliación obligatoria	Si (no se cumple)
Caja Central	Si, FINANCOOP (48 CACs afiliadas)
Sistema informático único sectorial	No, pero básicamente concentrado en dos sistemas
Central de Riesgo	Si, pero acceso solamente para las 27 CACs supervisadas
Protección de depósitos	Si, para los ahorristas de las CACs supervisadas El aporte se calcula sobre el promedio de los activos de un intermediario durante 12 meses y computa a 0,1%; cobertura máxima de protección 8.000 US$ por persona.
Fondo de liquidez[2]	Aporte anual 6,7% de los depósitos captados
Estadística sectorial	No, una base de datos existe solamente referente de las CACs supervisadas y las CACs afiliadas a la Caja Central
Número de socios del sector	1.500.000
Número de socios v/s población económicamente activa (8.000 mil)	18,8%
Total de activos	158 MioUS$
Colocaciones v/s total activos	70,5%
Cartera vencida[3] v/s colocaciones	3,4% (cartera que no devenga intereses)
Indice de riesgo[4]	2,4%

[1] Cifras de 60 CACs, las que representan aproximadamente 70% del sector al 31.12.2000
[2] Prestamista de última instancia estatal
[3] Cartera vencida a partir del noventa días
[4] Indice de riesgo: provisiones v/s total de colocaciones; para el sector rige la obligatoriedad

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Activo fijo+inversiones permanentes v/s reservas	58,5%
Captaciones v/s total activos	63,9%
Endeudamiento bancario[5]	1,1%
Coeficiente de solvencia[6]	20,5%
Rentabilidad neta[7]	1,2%

B. Regulación

Regulación de las operaciones financieras de las CACs

a) Para las cooperativas calificadas ante los criterios de la SB, como CAC DE INTERMEDIACION FINANCIERA CON EL PUBLICO, rigen las disposiciones de la Ley General de Instituciones Financieras (1994, ultima redacción 01/2001).

b) Las cooperativas que no obtienen esta licencia quedan excluidas de la Ley y en consecuencia, carecen de una regulación de sus operaciones. Deben adquirir posteriormente la licencia, fusionarse, disolverse o convertirse en CACs gremiales cerradas.

Cobertura de la regulación

27 de 350 CACs = 7,7% del total del sector (100% urbanas, ninguna rural)
estimación: 65% de cobertura del total de activos del sector

Normativa detallada

1. Codificaciones de resoluciones de la SB y del Banco Central
   - De la constitución y organización (apertura y cierre de oficinas, fusiones, aprobación o denegación de denominaciones)
   - Del Gobierno y de la administración (nombramiento de Directores, representantes legales y auditores)
   - Patrimonio (capitalización, conformación del patrimonio técnico, de la relación del patrimonio técnico frente a los activos ponderados por riesgo).
   - Operaciones y funcionamiento
   - Grupos financieros
   - Activos y los límites de crédito (castigo de activos, calificación de activos y constitución de provisiones, vinculación, garantias, límites de crédito, riesgo de mercado).
   - Contabilidad, información y publicidad
   - Procedimientos (bienes adjudicados etc.)
   - Limitaciones, prohibiciones y sanciones

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de generar 1 % de provisiones genéricas además, de las provisiones especificas.

[5] Endeudamiento bancario: préstamos bancarios v/s total activos

[6] Reservas v/s total de activos

[7] Remanente v/s total de activos

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- Liquidación de Instituciones Financieras
- De la superintendencia de bancos (intervención, calificadoras de riesgo, tarifas)

2. Decreto ejecutivo N°1.227 de N°1.998 Reglamento de la Ley General de Instituciones Financieras para Cooperativas de Ahorro y Crédito
   - Ambito de aplicación y control
   - De la constitución y organización de las CACs
   - Del Gobierno y administración (Asamblea General, Consejo de Administración, del Presidente, Consejo de Vigilancia, Gerente, régimen económico, de las operaciones, de la contabilidad, información financiera y auditoria, de la regulación de las CACs con problemas, de la disolución y liquidación).
3. Catalogo único de cuentas de la SB (rige para las 27 CACs supervisadas)

Pautas principales

1. Reglas de idoneidad para Gerentes y Directivos
2. Licencia de funcionamiento
3. Capital mínimo: US$ 750.000.-
4. Coeficiente patrimonial: 9%, calculado sobre activos ponderados por riesgo
5. Norma de estructura patrimonial (reservas no menor al equivalente de 50 % del capital social); las CACs deben asignar como mínimo un 10% de sus excedentes a las reservas.
6. Monto mínimo de aportes: US$ 0,40
7. El plazo de liquidación de un aporte es de 30 días, en caso de retiro de un socio
8. Coeficiente de liquidez (en partidas líquidas hasta 30 días; deben tener mínimo 14% del monto en obligaciones vencidas dentro de 30 días)
9. El total de los créditos vinculados no debe exceder 10% del patrimonio técnico; el crédito a un sólo Director no debe superar individualmente 2% del patrimonio técnico.
10. Clasificación contable de la cartera
    - Cartera por vencer (normal)
    - Cartera vencida (mayor a 30 días; hasta 90 días se registran las cuotas pendientes; a partir de 90 días el capital del crédito es transferido a esta subcuenta)
    - Cartera no devenga intereses (cartera vencida superior a 90 días)
11. Calificación y clasificación de la cartera de créditos en 5 categorías
    Categoría I : Créditos normales hasta 30 días de morosidad
    Categoría II : Créditos con problemas potenciales de 31 – 90 días
    Categoría III : Créditos deficientes de 91 – 180 días
    Categoría IV : Créditos dudosos de 181 – 270 días
    Categoría V : Créditos perdidos de 271 días en adelante
    Nota: La cartera de créditos esta segmentada en 3 tipos de créditos: de comercio, de consumo y de

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vivienda; en el caso de los créditos de vivienda y de comercio, la clasificación varía insignificativamente de la matrix arriba esbozada.

12. Régimen de provisiones en función de la calificación:
    a) Créditos normales: 1% previsión genérica
    b) Créditos con problemas potenciales: 3% provisión especifica
    c) Créditos deficientes: 20%
    d) Créditos dudosos: 80%
    e) Créditos perdidos: 100%
13. El monto máximo de un crédito a un prestatario o grupo de prestatarios es de 10% del patrimonio técnico (20% créditos con garantías).
14. Se suspende el cargo de Director o Gerente teniendo deudas en morosidad superior a 60 días en el sistema financiero
15. Inversiones en activos fijos: No mayor al patrimonio técnico
16. Remisión de datos e informaciones a la SB.
17. Auditoría externa: Obligatoria para las CACs supervisadas; el reglamento para los auditores externos establece que, solamente empresas registradas y autorizadas por la SB pueden realizar la auditoría de los Estados Financieros en CACs. Se normó el contenido de los informes y anexos igual al alcance de las labores de los auditores. Además, se pretende que los auditores externos proporcionen a la SB una información financiera complementaria. En este anexo, los auditores deben pronunciarse sobre el cumplimiento de las normas bancarias.
18. Auditoría interna: Obligatoria para las CACs supervisadas.
19. Manual de Cuentas Uniforme: Del sistema financiero rige obligatoriamente para las 27 CACs supervisadas.

C. Modelo de supervisión

Supervisión directa	27 CACs
Supervisión delegada/auxiliar	No procede
Autorregulación	No procede
Sin supervisión especializada	323 CACs

D. Procesos de supervisión

CACs supervisadas	27 del total de las 350 del sector

Ente a cargo de la supervisión	Superintendencia de Bancos (SB)
Personal a cargo de las CACs en la SB	Total 9 ejecutivos fijos más 3 analistas a tiempo parcial: 1 jefe de la unidad de inspección 8 inspectores (en 4 sedes) 3 analistas a cargo de la recaudación de las informaciones extra-situ
Organización	Después de una reforma organizacional, en el año 2000, se disolvió la Intendencia para las CACs, la nueva Dirección de la SB quiere volver a la estructura anterior, segmentada en intendencias por sectores de intermediarios (bancos privados, mutuales, sociedades financieras privadas, CACs). Si, existe una unidad de inspección in-situ; la supervisión extra-situ desempeña en este momento una unidad centralizada, recaudando los datos de todos los sectores.
Costo de la supervisión	Aporte anual 0,095% calculado sobre total de activos
<u>Supervisión off-site</u>	Si
Mecanismos de monitoreo	1. Las CACs reportan mensualmente 2. Los auditores externos entregan para cada CAC, anualmente, un informe de información financiera complementaria sobre el cumplimiento de las pautas bancarias establecidas. 3. Los auditores internos remiten trimestralmente sus informes
Número de CACs monitoreadas	27
Evaluación	Ficha de análisis por cada CAC (indicadores macro diseñados sobre CAMEL)
Retroalimentación a las CACs	Oficio de observaciones (datos remitidos en forma incorrecta, vulneración de límites)
<u>Supervisión in-situ (on- site)</u>	Si
Plan de inspección	Plan anual, elaborado por jefe de inspectores
Número de inspecciones anuales	12 CACs programadas de visitas ordinarias 15 CACs, visitas de seguimiento
Cobertura	7,7% del sector (27 sobre 350 CACs),
Duración de inspecciones[8]	40 días mínimo (incluye 5 días para el informe) 60 días máximo (incluye 3 días para el informe)
Criterio del cálculo de duración	Tamaño y complejidad de la CAC
Duración de visitas de seguimiento	20 días
Planificación	Si, con memorándum de visita, emitido por el encargado de cada CAC
Configuración del personal	Equipo de trabajo
Aviso de inspección	Si, con 14 días de anticipación (carta del primer día) Causa: las CACs tienen que preparar las informaciones requeridas por los inspectores; no existe un

[8] En circunstancias normales y sin que la CAC exhiba mayores índices de riesgo o deficiencias

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	sistema electrónico único para el sector, al cual los inspectores tengan acceso
Alcance de la inspección (ordinaria)	- Evaluación de la gestión administrativa - Calificación de activos de riesgo - Principales cuentas del balance - Contabilidad - Ingresos y gastos - Cumplimiento de observaciones de inspecciones o auditorías (internas y externas) anteriores.
Papeles de trabajo	No hay formularios estándares, los inspectores aplican formatos individuales, autodiseñados por ellos
Informe por escrito de la inspección	Si
Contenido del informe de inspección	1. Capítulo I: Información introducida (motivo de la inspección, objetivos de la inspección, alcance de la inspección, trabajo de campo, integrantes del equipo de visita, configuración de Consejos, Gerencia y planta ejecutiva, base legal) 2. Capítulo II: Seguimiento de recomendaciones 3. Capítulo III: Rubros y áreas examinadas (gestión del Consejo de Administración, del Consejo de Vigilancia, de Gerencia General y de auditoría interna, fondos disponibles, - evaluación de la calificación de activos de riesgo: a) inversiones; b) cartera de créditos; c) cuentas por cobrar; d) otros activos – control de garantías, garantías bancarias, cuentas de resultados.
Informe verbal	Si
Veredicto ejecutivo	1. La SB de Ecuador sufre de una inestabilidad perjudicial en su dirección debido a una alta rotación en el cargo del Superintendente. Los últimos 10 años cambiaron 14 veces el titular. Esto provoca incertidumbre en la planta ejecutiva de la institución y cambios permanentes en cuanto al nivel de Intendentes y Subintendentes además, de modificaciones aceleradas de las estructuras organizacionales internas. 2. La crisis bancaria de Ecuador no llegó al sector cooperativo financiero. Responsable de ello, en primera instancia, fue el alto grado de solvencia patrimonial basándose en las reservas acumuladas y una prudente política de liquidez del sector propio, mas que en la supervisión bancaria. 3. Existe un proyecto de agregar a la actual Ley General de Instituciones Financieras un capítulo especial que regulará debidamente la intermediación financiera de las CACs. Una vez promulgado este anexo, en la forma como fue presentado en el Congreso, la normativa Ecuadoriana se consideraria completa con respecto a este sector. 4. Actualmente las CACs de Ecuador están solamente insertas en forma parcial en la regulación bancaria. 323 CACs carecen de una regulación hasta que el capítulo anexo a la ley sea promulgado. Por ende, la intermediación de no más del 8% de las CACs, operando en el país, está supervisada a través de monitoreo off-site e inspecciones in-situ. 5. El modelo implementado por la legislación de Ecuador es la Supervisión Directa. En el capítulo anexo

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a la Ley Bancaria, se menciona la posibilidad de delegar funciones auxiliares a agentes privados.

6. Los procesos de la supervisión no son óptimos en las siguientes áreas:

- Falta de papeles de trabajo estándares (guía de inspección, lista de chequeos para control interno, formato para revisión de créditos, modelo de informe).
- Existe duplicidad de trabajos: los auditores internos reportan trimestralmente sus observaciones, los auditores externos se pronuncian anualmente en un anexo a sus informes sobre el cumplimiento de las normas establecidas, las CACs remiten mensualmente informaciones y datos, los inspectores de la SB efectúan visitas ordinarias y de seguimiento in-situ.

7. El modelo de Supervisión Directa, ejecutado a través de la SB, es técnicamente viable pero, requiere de procedimientos óptimos.
8. En general las pautas y límites establecidos, permiten prevenir una indebida gestión en las 27 CACs sujetas a la fiscalización. Con el propósito de perfeccionar las técnicas de la supervisión directa y enmendar la normativa, en pos a una cobertura completa de regulación y supervisión de todas las CACs del sector, se agrega a continuación un módulo con observaciones y recomendaciones.
9. La fiscalización por parte de la SB cubre todavía un pequeño grupo de CACs. De esta manera, la SB cumple solamente en forma parcial con las exigencias del Acuerdo de Basilea, emitidas por el Comité de Supervisión del Banco de Pagos Internacionales.

Observaciones y recomendaciones

↳Todavía no existe en Ecuador un interlocutor único y reconocido que pueda negociar los intereses del sector con el legislador y las autoridades. La Federación y Asociaciónes de CACs supervisadas no han calificado en pos de esa misión o no representan al total de los afectados.

↳ Se debe evaluar si hay, en este momento, un ente sectorial idóneo al cual se pueda delegar facultades y tareas de un supervisor auxiliar, con el fin de aumentar significativamente la cantidad de CACs supervisadas.

↳ La duración de las visitas de inspección es muy prolongada. Se deben optimizar los procedimientos técnicos con el propósito de ganar tiempo y cubrir una mayor cantidad de CACs.

↳ Se recomienda obligar a las CACs a notificar todos los créditos vinculados a la SB.

↳La regulación vigente aplica una restricción débil para la devolución de aportes, lo cual permite al capital social de las CACs ser un elemento muy volátil dentro del patrimonio. Sin las medidas previstas en el capítulo anexo a la Ley Bancaria el coeficiente patrimonial, por consiguiente, no refleja la solvencia real de una CAC.

↳ La estructura y organización de la SB no es óptima. La concentración de todas las funciones en una sola Intendencia General no es apropiada; producto de ello, no existe suficiente flujo de información y coordinación entre las instancias de inspección y el análisis extra-situ. Se recomienda volver a la estructura de Intendencias por sectores.

1.4 BUDGET

The following is the Agreement Budget, including local cost financing items, if authorized. Revisions to this budget shall be made in accordance with 22 CFR 226.25.

Cost Element	Amount	
Program	$328,092	(A)
Procurement	60,962	(B)
Training	232,885	(C)
Indirect Costs	178,061	(D)
Total USAID Cost	$800,000	
Total Recipient Contribution	10,000	
Other Contributions	150,000	
Total Grant Program	$960,000	

1.5 REPORTING AND EVALUATION

1.5.1 Financial Reporting

In accordance with 22 CFR 226.52 the SF 269 and 272 will be required on a quarterly basis. The recipient shall submit these forms in the following manner:

(a) The SF 272 and 272a (if necessary) will be submitted via electronic format to the U.S. Department of Health and Human Services (http://www.dpm.psc.gov). A copy of this form shall also be simultaneously submitted to the Agreement Officer and the Cognizant Technical Officer.

(b) The SF 269 or 269a (as appropriate) shall be submitted to the Cognizant Technical Officer with one copy to the Agreement Officer.

(c) In accordance with 22 CFR 226.70 – 72 the original and two copies of final financial reports shall be submitted as follows: M/FM, the Agreement Officer and the CTO. The electronic version of the final SF 272 or 272a shall be submitted to HHS in accordance with paragraph (a) above.

1.5.2 Monitoring and Reporting Program Performance

(a) Program Reporting

The Recipient shall submit an original and one copy of the performance report to the Project Officer and the Agreement Officer specified in the Cover Letter. The performance reports are required to be submitted annually and shall contain the information set forth in CFR 226.51(d).

(b) Final Report

The Recipient shall submit the original and one copy to the Cognizant Technical Officer and the Agreement Officer specified in the Cover Letter and one copy to USAID Development Experience Clearinghouse, ATTN: Document Acquisitions, 1611 N. Kent Street, Suite 200, Arlington, VA 22209-2111 (or e-mail: docsubmit@dec.cdie.org).

MEJORES PRACTICAS EN SUPERVISION

Diagnóstico del caso de

PERU

A. Datos sectoriales[1]

Cantidad total de CACs	201
Existe una Federación	Si
CACs afiliadas a la Federación	119
Federación	Federación Nacional de Cooperativas de Ahorro y Crédito del Perú, FENACREP
Afiliación obligatoria	No
Caja Central	Si, se encuentra en la fase inicial
Sistema informático único sectorial	No Un programa se encuentra en proceso de prueba en 5 CACs pilotos
Central de riesgo	Si, las CACs tienen acceso
Protección de depósitos	No para ahorristas de las CACs Para la banca existe un fondo de seguro de depósitos
Número de socios del sector	331.277
Número de socios v/s población económicamente activa (10.038 mil)	3,3 %
Total de activos	245 MioUS$
Colocaciones v/s total activos	62,1 %
Cartera vencida[2] v/s colocaciones	11,4 %
Indice de riesgo[3]	12,8
Crecimiento colocaciones	4,1 % (inflación 2000: 3,6 %)
Activo fijo+inversiones permanentes v/s reservas	121,9 %
Captaciones v/s total activos	55,2 %
Endeudamiento bancario[4]	1,8 %

[1] Cifras al 31.12.2000

[2] Cartera vencida: cuotas a partir de 8° día; capital a partir de 30 días (cartera comercial) y 90 días (créditos de consumo)

[3] Indice de riesgo: provisiones v/s total de colocaciones; para el sector rige la obligatoriedad de generar 3 % de provisiones genéricas además, de las provisiones específicas.

[4] Endeudamiento bancario: préstamos bancarios v/s total activos

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Coeficiente de solvencia[5]	7,5 %
Rentabilidad neta[6]	1,64 %

B. Regulación

Regulación de las operaciones financieras de las CACs.	Ley General del Sistema Financiero y de Seguros y Orgánica de la Superintendencia de Bancos y Seguros –SBS. Vigésima cuarta disposición final y complementaria
Cobertura de la regulación	100% de las CACs del sector Peruano
Normativa detallada	- Reglamento de CACs; resolución N°0540 de la SBS 16.06.1999 - Resoluciones complementarias de la SBS - Circulares de las SBS - Cartas Circulares de FENACREP
Pautas principales	- Reglas de idoneidad, impedimentos, responsabilidades para Gerentes y Directivos (p.e. las dietas para dirigentes, después de 120 días en morosidad, suspensión del cargo). - Contenido y formato del informe trimestral de la Gerencia a los Consejos - Coeficiente de solvencia (el monto de los activos y créditos contingentes, ponderados por riesgo, no pueden exceder de 11 veces su patrimonio efectivo (= 9,1 %). - Norma de estructura patrimonial (reservas no menor al equivalente de 35 % del capital social) - Monto mínimo de aportes - Límite crediticio (monto total máximo a un prestatario: 5% del patrimonio efectivo) - Límites de financiamiento de activo fijo e inversiones (activo fijo físico no podrá exceder 40% del patrimonio efectivo; inversiones permanentes no podrán exceder 15% del patrimonio efectivo; créditos/inversiones en cooperativas o empresas de apoyo al giro no pueden exceder 20%). - Causales de la intervención (la pérdida de 50% del patrimonio efectivo) y los procedimientos - Prohibición de conceder créditos para el financiamiento de aportes en la misma CAC. - La distribución de facultades y tareas para la regulación (SBS) y Supervisión (FENACREP); las atribuciones de la Federación, las modalidades de la inspección. - La fiscalización de la supervisión delegada - Sanciones y multas

[5] Reservas v/s total de activos
[6] Remanente v/s total de activos

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- Fondo de Contingencia
- Auditoría interna (remisión obligatoria del informe anual a la Federación); en CACs de menor tamaño se permite outsourcing de la auditoría interna.
- Auditoría externa obligatoria para todas las CACs de categoría I[7] (74 CACs con un total de activos superior a 800.700 soles = 225 mil US$; las empresas tienen que estar registrados y autorizados; se establecieron exigencias mínimas del contenido y de la estructura de los informes).
- Contenido, formato y periodicidad de las remisiones a la Federación
- La distribución de remanentes
- El costo de la supervisión

C. Modelo de supervisión

Supervisión directa	Para todas las CACs, que captan de no socios Actualmente ninguna CAC
Supervisión híbrida/delegada	Todas las otras CACs, las cuales captan de sus socios por vía pasivo o aportes, 181 del total de las 201 CACs del sector
Autorregulación	No procede
Sin supervisión especializada	No procede

D. Procesos de supervisión

CACs supervisadas	181 del total de las 201 del sector
Instancia a cargo de la supervisión	Unidad de Control de FENACREP
Personal de la Unidad de Supervisión	Total 11 ejecutivos: 1 jefe de la unidad de control 1 secretaria 4 analistas 3 inspectores fijos 2 inspectores contratados a honorario
Costo de la supervisión	A cargo de las CACs; ellas pagan 0,2% sobre su total de activos a FENACREP; se genero una matrix escalonada para los aportes individuales en función al tamaño.
Supervisión off-site	Si
Mecanismos de monitoreo	Las CACs reportan mensualmente

[7] Segmentación del sector en categoría I

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Número de CACs monitoreadas	181
Informe de retroalimentación	Trimestralmente información financiera
Supervisión in-situ (on-site)	Si
Plan de inspección	Anual
Número de inspecciones anuales	37 CACs programadas 10 CACs al aleatorio
Cobertura con visitas anuales	26 % del sector (sobre 181 CACs que reportan)
Duración de inspecciones[8]	4 días, mínimo 18 días, máximo
Criterio del cálculo de duración	Tamaño y complejidad de la CAC
Planificación de las visitas	Si, con memorándum de visita, emitido por el jefe de unidad
Modalidades	Un inspector o equipo
Aviso de la visita de inspección	Si, con 3 días de anticipación Causa: Las CACs tienen que preparar las informaciones requeridas por los inspectores ya que no existe un sistema electrónico único para el sector al cual los inspectores tengan acceso.
Alcance de la inspección	Gestión del Consejo de Administración y de Gerencia Sistema de control interno Auditoría interna Gestión administrativa y contable Solvencia, liquidez, estructuras de financiamiento Procesos de administración de cartera de créditos Carpetas de crédito
Instrucciones y papeles de trabajo	- Manual de control interno e inspección (versión mayo 2001) - Manual de procedimientos de inspección (versión abril 2001) - Hoja de revisión de créditos
Informe escrito de la inspección	Si
Contenido informe de inspección	1. Resumen ejecutivo 1.1 Antecedentes 1.2 Principales observaciones: Liquidez, créditos, bienes adjudicados, ingresos, asociativo, auditoría interna, situación patrimonial, sistema de información . 2. Contenido del informe: 2.1 Riesgo de liquidez, 2.1.2 Evolución de la liquidez 2.1.3 Manejo de liquidez

[8] en circunstancias normales sin que la CAC exhibe mayores índices de riesgo o deficiencias

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2.2 Riesgo crediticio
  2.2.1 Evolución de la cartera y morosidad
  2.2.2 Evaluación de la gestión de créditos
  2.2.3 Cuentas por cobrar
2.3 Otros activos sujetos a riesgo
  2.3.1 Bienes adjudicados
2.4 Aspectos contables
  2.4.1 Fondos disponibles
  2.4.2 Ingresos financieros
  2.4.3 Ingresos de préstamos refinanciados
2.5 Grado de implementación del informe de visita anterior
2.6 Auditoría interna
2.7 Auditoría externa
2.8 Suficiencia patrimonial
2.9 Grado de cumplimiento de normas legales

3. Anexos:
Balance y Estados de Resultados del día de inspección, relación de los Consejos y Comités, Directivos en situación de morosidad, evolución de las principales operaciones (colocaciones, provisiones, depósitos, patrimonio), resumen de evaluación y clasificación de cartera de créditos, muestra de la clasificación de cartera de créditos, anexo con el déficit estimado de provisiones de la clasificación de cartera de créditos, créditos otorgados con plazos de gracia y/o cancelaciones al vencimiento, créditos vencidos con más de 180 días de atraso sin acciones judiciales, créditos en exceso, otorgados a empresas vinculadas.

Informe verbal

Si

Veredicto ejecutivo

1. Las CACs se encuentran insertas en la regulación bancaria.
2. Por ende el sector de las CACs es reconocido plenamente como parte del sistema financiero nacional.
3. La intermediación de todas las CACs, operando en el país, está supervisada reglamentariamente a través de monitoreo off-site e inspecciones in-situ. Tomando en consideración que el modelo se aplica recién desde 1994 hay que resaltar que el nivel de desarrollo esta avanzando.
4. El modelo implementado por la legislación Peruana es la Supervisión híbrida, con delegación de funciones a la Federación. La regulación estipula que la supervisión en CACs, que captan también de no socios, debe ser ejecutada directamente por la SBS; y para las demás CACs, se realiza por medio de la Federación. De tal modo que todas las 181 CACs, las cuales operan en el

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país, están sujetas a las mismas normas y prácticas de supervisión.

5. El modelo de la supervisión híbrida/delegada, implementado a través de la Federación FENACREP, es viable. La Federación cumple básicamente el rol definido en la normativa.
6. En general las pautas y límites establecidos, igual que las modalidades y técnicas aplicadas, permiten prevenir una debida gestión en las CACs e inspiran una suficiente seguridad para los depositantes/ahorristas. Con el propósito de perfeccionar y complementar las prácticas del caso, se agrega a continuación un modulo con observaciones y recomendaciones.
7. Incorporando las CACs en la supervisión financiera, la SBS cumple con las exigencias estipuladas en el Acuerdo de Basilea emitidas por el Comité de Supervisión del Banco de Pagos Internacionales.

Observaciones y recomendaciones

🖎 La auditoría externa también debe ser obligatoria para la categoría II de las CACs y debe realizarse cada segundo año abarcando los últimos dos ejercicios.

🖎 La cobertura de la supervisión ,con visitas en terreno, aún no satisface. Se debe incrementar el nivel de inspecciones in-situ a un 50 % anual.

🖎 La norma sobre la estructura del patrimonio debe estipular que los aportes no sobrepasen 100% de las reservas.

🖎 Se debe regular la devolución de los aportes; el objetivo es atenuar su volatilidad fijando una obligatoriedad para el socio de avisar el retiro de su capital social en un plazo de a lo menos tres meses.

🖎 En cuanto a la pauta del patrimonio suficiente, se debe implementar la exigencia de un coeficiente de solvencia de 9 % calculado sobre los activos ponderados de riesgo siendo equivalente al actual límite de once (11) veces y debe ser reemplazado por la norma del coeficiente.

🖎 Los informes de inspección y las publicaciones periódicas de la Unidad de Control de FENACREP deben poner mas énfasis en el nivel de la solvencia de las CACs, como meta prioritaria entre las pautas.

🖎 La ejecución de las sanciones y la cobranza de multas debe efectuarse con mas puntualidad y eficacia.

🖎 La atribución de imponer sanciones y multas debe hacerse extensiva a la SBS. Ambas facultades son propias y exclusivas de la autoridad y exceden de las facultades y tareas auxiliares de un ente privado. Se deben separar las tareas técnicas, delegadas a la Federación, de las sanciones que son propias del Estado así, evitar que la Federación incurra en conflictos de juez y parte.

🖎 Para la realización de visitas de inspección sorpresivas se requiere de un sistema informático único para sector, que permite a los inspectores de la Federación el acceso previo a los datos de la CAC, previo al comienzo de sus labores in-situ.

🖎 Queda pendiente la constitución de un Fondo de Protección de Depósitos.

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World Council of Credit Unions, Inc.
Savings Best Practices

Attachment 8

Participant List from Savings Confrence, Managua, Nicaragua

Participantes en la Conferencia "Mejores Prácticas para la Movilización de Ahorros"
23 al 25 de abril de 2002
Managua, Nicaragua

Carlos Rafael Acuña Larios
Director de Mercadeo
Cooperativa Union Popular, R.L.
Guatemala

Saul Asdrúbal Acuña Olivas
Oficial de Crédito
CAC Dinámica
Nicaragua

Carlos Aguilar Olmedo
Gerencia de Acaprodusca de R.L.
Asociación Cooperativa de Ahorro y Crédito
Productores de Cuscatlan y Cabañas de Resp.
Ltda.
El Salvador

Jayme Aguilar Pérez
Asesor
Cooperativa La Esperanza de Las Sabanas
Nicaragua

Francisco Javier Alemán Pérez
Asesor de Crédito
Fundación 4i-2000
Nicaragua

Nelson Alexis Aldana
Director Ejecutivo
Agencia Calificadora de WOCCU
Guatemala

Juan Manuel Altamirano
Gerente General
Central de Cooperativas de Ahorro y Crédito
Financieras de Nicaragua
Nicaragua

Maria Ester Alvarado
Directivo
Cooperativa COANDES
El Salvador

Rafael Amador
Presidente, Consejo de Vigilancia
MEDICOOP
República Dominicana

Blanca Andara de Perdomo
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Las presentaciones de la conferencia estarán disponibles en la página web www.woccu.org apartir del 15 de mayo de 2002.

Attachment 9

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Attachment 10

Participant List from Supervision Best Practice Conference, Mexico City, Mexico

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No.	NOMBRE	INSTITUCIÓN	PUESTO	PAÍS
1	ACOSTA CHAN LIZBETH	UNIDAD OPERATIVA COMITÉ DE SUSPERVISIÓN MÉRIDA/SISTEMA COOPERA	GERENTE DE FEDERACIÓN	MÉXICO
2	ADAME GARDUÑO ROBERTO	MANCERA, ERNST & YOUNG	GERENTE	MÉXICO
3	AGUILAR ESPINOSA JOSÉ LUIS	UNIDAD OPERATIVA COMITÉ DE SUSPERVISIÓN MÉRIDA/SISTEMA COOPERA	INSPECTOR	MÉXICO
4	ALAMILLA RAMOS FELIPE	COMISIÓN NACIONAL BANCARIA Y DE VALORES	GERENTE	MÉXICO
5	ALCAZAR NADIA	VICEMINISTERIO DE ASUNTOS FINANCIEROS	ASESORA DEL VICEMINISTERIO DE ASUNTOS FINANCIEROS	BOLIVIA
6	ALEJOS ESPARZA JOSÉ ANTONIO	FEDERACIÓN CONFIANZA POPULAR, S.C.	DIRECTOR DE LA FEDERACIÓN	MÉXICO
7	ALMAGUER SIMENTAL GERARDO	DID-BANSEFI	CONSULTOR EXTERNO	MÉXICO
8	ALTAMIRANO JUAN	CENTRAL DE COOPERATIVAS DE AHORRO Y CRÉDITO FINANCIERAS DE NICARAGUA, R.L.	GERENTE GENERAL	NICARAGUA
9	ALVA ÁVILA DANIEL	FEDERACIÓN REGIONAL DE COOPERATIVAS DEL CENTRO	FINANCIERO	MÉXICO
10	ÁLVAREZ JUÁREZ RICARDO	COMISIÓN NACIONAL BANCARIA Y DE VALORES	SUPERVISOR	MÉXICO
11	ANGULO POUS ALEJANDRO	PRO-DESARROLLO SUPERVISIÓN, A.C.	PRESIDENTE DEL COMITÉ DE SUPERVISIÓN	MÉXICO
12	ARELLANO PONCE AGAPITO	FEDERACIÓN CONFIANZA POPULAR, S.C.	PRESIDENTE DEL CONSEJO DE ADMINISTRACIÓN	MÉXICO
13	ARIAS SILVIA	SUPERINTENDENCIA DEL SISTEMA FINANCIERO DE EL SALVADOR	JEFE INTERINO DE LA UNIDAD DE INTERMEDIARIOS FINANCIEROS NO BANCARIOS	EL SALVADOR
14	ARMELE FELIPE	COOMECIPAR, LTDA. DEL PARAGUAY	PRESIDENTE	PARAGUAY
15	BENÍTEZ GUSTAVO	SUPERINTENDENCIA DE BANCOS, BANCO CENTRAL DEL PARAGUAY	INTENDENTE DE ANÁLISIS FINANCIERO Y NORMAS	PARAGUAY
16	CALDERÓN DELGADO MARÍA DEL CARMEN	ASOCIACIÓN MEXICANA DE UNIONES DE CRÉDITO DEL SECTOR SOCIAL, A.C. AMUCSS	ENCARGADO DE ANÁLISIS FINANCIERO	MÉXICO
17	CAMPOS CORTÉS EDUARDO	INTEGRA SERVICIOS ADMINISTRATIVOS, S.C./FEDERACIÓN REGIONAL DE COOPERATIVAS DEL CENTRO, S.C. DE R.L.	DIRECTOR GENERAL	MÉXICO
18	CÁRDENAS FÉLIX JAVIER	FONAES	DIRECTOR DE CAJAS SOLIDARIAS	MÉXICO
19	CASTRO ROLDÁN JOSÉ SALVADOR	FEDERACIÓN REGIONAL DE COOPERATIVAS DEL CENTRO	AUDITOR	MÉXICO
20	CHIM CAB JOSÉ RAÚL	UNIDAD OPERATIVA COMITÉ DE SUSPERVISIÓN MÉRIDA/SISTEMA COOPERA	INSPECTOR	MÉXICO

PARTICIPANTS

No.	NOMBRE	INSTITUCIÓN	PUESTO	PAÍS
21	CHOLICO GARCÍA JOSÉ DE JESÚS	UNISAP DE OCCIDENTE, A.C.	AUDITOR DEL COMITÉ DE SUPERVISIÓN	MÉXICO
22	CIFUENTES SÍNCRITO	FEDERACIÓN NACIONAL DE COOPERATIVAS DE AHORRO Y CRÉDITO	GERENTE GENERAL	GUATEMALA
23	CONTRERAS MÁRQUEZ ADRIANA	COMISIÓN NACIONAL BANCARIA Y DE VALORES	INSPECTOR "A"	MÉXICO
24	COPELLO MARÍA MERCEDES	FOGACOOP	DIRECTOR	COLOMBIA
25	CÓRDOVA HÉCTOR DAVID	FEDERACIÓN DE ASOSCIACIONES COOPERATIVAS DE AHORRO Y CRÉDITO DE EL SALVADOR, R.L.	GERENTE CORPORATIVO	EL SALVADOR
26	CRUZ AGUILAR ANA CAROLINA	COMISIÓN NACIONAL BANCARIA Y DE VALORES	INSPECTOR	MÉXICO
27	CRUZ FURBER CRISTINA	INSTITUTO DE MICROFINANZAS DE LEÓN GUANAJUATO	DIRECTOR GENERAL	MÉXICO
28	DÁVALOS ESTRELLA CARLOS CÉSAR	COMISIÓN NACIONAL BANCARIA Y DE VALORES	INSPECTOR "A"	MÉXICO
29	DE LA LLAVE PALLARES MARIANA	COMISIÓN NACIONAL BANCARIA Y DE VALORES	INSPECTOR	MÉXICO
30	DE LA TORRE DE LA ROSA HOMERO	COMISIÓN NACIONAL BANCARIA Y DE VALORES	SUPERVISOR	MÉXICO
31	DEL POZO CARLOS	SUPERINTENDENCIA DE BANCOS Y SEGUROS DEL ECUADOR	ASESOR DEL SUPERINTENDENTE DE BANCOS Y SEGUROS	ECUADOR
32	DERGAL URANGA ANNEL	COMISIÓN NACIONAL BANCARIA Y DE VALORES	INSPECTOR "A"	MÉXICO
33	DÍAZ CASTILLO RAFAEL ALFONSO	COMISIÓN NACIONAL BANCARIA Y DE VALORES	INSPECTOR	MÉXICO
34	DÍAZ GONZÁLEZ CABRERA ERNESTO	COMISIÓN NACIONAL BANCARIA Y DE VALORES	SUBGERENTE	MÉXICO
35	DOS SANTOS OSVALDO CARLOS	CONFEDERACIÓN NACIONAL DE LAS COOPERATIVAS UNICRED	PRESIDENTE	BRASIL
36	DUARTE FLEMING	BANCO CENTRAL DE PARAGUAY	DIRECTOR DE UTEP	PARAGUAY
37	DUPONT CRUZ CLEMENCIA	SUPERINTENDENCIA DE LA ECONOMÍA SOLIDARIA	SUPERINTENDENTE DELEGADA	COLOMBIA
38	ESCOBAR ARVIZU JOSÉ ANGEL	COMISIÓN NACIONAL BANCARIA Y DE VALORES	VICEPRESIDENTE	MÉXICO
39	ESPITIA MELO FERNANDO	SUPERINTENDENCIA BANCARIA DE COLOMBIA	DIRECTOR TÉCNICO TRES C	COLOMBIA
40	FABELA VIÑAS JORGE	COMISIÓN NACIONAL BANCARIA Y DE VALORES	DIRECTOR GENERAL	MÉXICO

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No.	NOMBRE	INSTITUCIÓN	PUESTO	PAÍS
41	FERNÁNDEZ LABARDINI MARÍA TERESA	COMISIÓN NACIONAL BANCARIA Y DE VALORES	DIRECTOR GENERAL	MÉXICO
42	FIGUEROA RUÍZ FELIPE	COMACREP	VICEPRESIDENTE	MÉXICO
43	FLORES MEDINA IVONNE KARLA	COMISIÓN NACIONAL BANCARIA Y DE VALORES	INSPECTOR	MÉXICO
44	GALVÁN BARRIOS MARIO	SISTEMA ESTATAL DE FINANCIAMIENTO DE DESARROLLO/SEFIDE	DIRECTOR GENERAL DE ASISTENCIA TÉCNICA MULTIPLICA	MÉXICO
45	GARCIARIVAS REYES FABIÁN	COMISIÓN NACIONAL BANCARIA Y DE VALORES	INSPECTOR "A"	MÉXICO
46	GARDUÑO RODRÍGUEZ ENRIQUE ROBERTO	COMISIÓN NACIONAL BANCARIA Y DE VALORES	INSPECTOR "A"	MÉXICO
47	GARROCHTEGUI IGNACIO	FINCOOP	GERENTE GENERAL	VENEZUELA
48	GARZA CASTAÑEDA MIGUEL ANGEL	COMISIÓN NACIONAL BANCARIA Y DE VALORES	DIRECTOR GENERAL	MÉXICO
49	GÓMEZ ALCALÁ EDUARDO	COMISIÓN NACIONAL BANCARIA Y DE VALORES	DIRECTOR GENERAL	MÉXICO
50	GRANADOS RAMÍREZ LUIS ROLANDO	UNIDAD DE CONTROL INTEGRAL, S.C. UNICIM	DIRECTOR GENERAL	MÉXICO
51	GUERRERO POZAS GREGORIO	COMISIÓN NACIONAL BANCARIA Y DE VALORES	CONTRALOR INTERNO	MÉXICO
52	GURZA GONZÁLEZ ALFONSO	COMISIÓN NACIONAL BANCARIA Y DE VALORES	INSPECTOR "A"	MÉXICO
53	GUTIÉRREZ BOLIVAR ROSA MARÍA	FEDERACIÓN REGIONAL DE COOPERATIVAS DE AHORRO Y PRÉSTAMO CENTRO-SUR, S.C.L.	ASESOR CONTABLE	MÉXICO
54	GUTIÉRREZ DÍAZ PABLO ANTONIO	AMSAP	AMSAP	MÉXICO
55	HERNÁNDEZ CARRAZA LINCOLN GIOVANI	CALIFICADORA DE INSTITUCIONES WOCCU	ANALISTA DE RIESGOS	GUATEMALA
56	HERNÁNDEZ MORALES CARMEN LAURA	UNIDAD DE CONTROL INTEGRAL, S.C. UNICIM	ENCARGADO DE SUPERVISIÓN	MÉXICO
57	ILLANES DÍAZ RIVERA EMILIO MAXIMILIANO	FONAES	DIRECTOR GENERAL DE FONDOS Y MICROEMPRESAS	MÉXICO
58	IMPERIAL ZUÑIGA RAMÓN	COMACREP	PRESIDENTE	MÉXICO
59	JIMÉNEZ DE LA PEÑA JOSÉ ANTONIO	COMISIÓN NACIONAL BANCARIA Y DE VALORES	SUPERVISOR	MÉXICO
60	JOFRE ZAMORANO NELSON	FEDERACIÓN CHILENA DE COOPERATIVAS DE AHORRO Y CRÉDITO, LTDA. (FECRECOOP)	GERENTE GENERAL	CHILE

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No.	NOMBRE	INSTITUCIÓN	PUESTO	PAÍS
61	JUANCHI GÓMEZ DORIS	BANSEFI	SUBDIRECTORA DE COORDINACIÓN INTERNACIONAL	MÉXICO
62	LAFUENTE ANZOLEAGA ROLANDO	QUILLACOLLO, LTDA., ASOCIACIÓN TÉCNICA DE COOPERATIVAS DE BOLIVIA (ATC)	GERENTE	BOLIVIA
63	LIZÁRRAGA OBREGÓN LUIS FELIPE	PRO-DESARROLLO SUPERVISIÓN, A.C.	GERENTE DE PROYECTO	MÉXICO
64	LÓPEZ MARÍN CÉSAR	COMACREP	SECRETARIO EJECUTIVO	MÉXICO
65	LOZANO COVARRUBIAS GUILLERMO	FEDERACIÓN DE COOPERATIVAS DEL NOROESTE	PRESIDENTE	MÉXICO
66	MARISCAL MAGDALENO LUIS FELIPE	COMISIÓN NACIONAL BANCARIA Y DE VALORES	DIRECTOR GENERAL	MÉXICO
67	MÁRQUEZ ESTODANO MIGUEL	CAJA POPULAR MEXICANA/AMSAP	GERENTE DE AUDITORÍA CONTABLE E INFORMÁTICA	MÉXICO
68	MARTÍNEZ LLANAS JAVIER	COMISIÓN NACIONAL BANCARIA Y DE VALORES	INSPECTOR	MÉXICO
69	MARTÍNEZ RINCÓN ALBERTO	COMISIÓN NACIONAL BANCARIA Y DE VALORES	ASESOR DE VICEPRESIDENCIA	MÉXICO
70	MARTINICA PAULINO	MINISTERIO DEL TRABAJO	VICEMINISTRO	NICARAGUA
71	MEDINA GUZMÁN EMILIO	COMISIÓN NACIONAL BANCARIA Y DE VALORES	INSPECTOR "A"	MÉXICO
72	MEDINA PUGA RAFAEL	COMACREP	VICEPRESIDENTE	MÉXICO
73	MEJÍA ELVIA	SUPERINTENDENCIA DE LA ECONOMÍA SOLIDARIA	SUPERINTENDENTE	COLOMBIA
74	MENDOZA RÍOS MARÍA DE LA LUZ	FEDERACIÓN REGIONAL DE COOPERATIVAS DE AHORRO Y PRÉSTAMO CENTRO-SUR, S.C.L.	ASESOR CONTABLE	MÉXICO
75	MERCADO GUZMÁN ADRIANA	UNIÓN DE COOPERATIVAS PIONERAS DE OCCIDENTE, S.C. DE R.L.	ADMINISTRADORA	MÉXICO
76	MIER SAÍNZ-TRAPAGA JOSÉ FRANCISCO	COMISIÓN NACIONAL BANCARIA Y DE VALORES	SUPERVISOR EN JEFE	MÉXICO
77	MONDRAGÓN MINERO MARÍA DEL CARMEN	COMISIÓN NACIONAL BANCARIA Y DE VALORES	ESPECIALISTA	MÉXICO
78	MORA CÁRDENAS ARTURO	UNISAP DE OCCIDENTE, A.C.	GERENTE DE ASESORÍAS	MÉXICO
79	MORALES EDUARDO ALFONSON	FEDERACIÓN NACIONAL DE COOPERATIVAS DE AHORRO Y CRÉDITO	PRESIDENTE	GUATEMALA
80	MORALES LÓPEZ VERÓNICA	CONSEJO COORDINADOR NACIONAL DE CAJAS SOLIDARIAS	COMITÉ DE SUPERVISIÓN	MÉXICO

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No.	NOMBRE	INSTITUCIÓN	PUESTO	PAÍS
81	MORALES PÉREZ ALBERTO ALFONSO	FEDERACIÓN REGIONAL DE COOPERATIVAS DE AHORRO Y PRÉSTAMO CENTRO-SUR, S.C.L.	VICEPRESIDENTE DEL CONSEJO DE ADMINISTRACIÓN	MÉXICO
82	MORENO LUIS EDUARDO	FOGACOOP	JEFE TÉCNICO	COLOMBIA
83	MORENO NEIRA JESÚS MARÍA	FEDERACIÓN DE COOPERATIVAS DEL NOROESTE	GERENTE	MÉXICO
84	NAVA GALINDO GRISELDA	UNIÓN DE COOPERATIVAS PIONERAS DE OCCIDENTE, S.C. DE R.L.	VICEPRESIDENTE DEL CONSEJO	MÉXICO
85	NAVARRETE BAÑUELOS VERÓNICA	DID-BANSEFI	CONSULTOR EXTERNO	MÉXICO
86	NERIO SAÚL ANTONIO	FEDERACIÓN DE ASOSCIACIONES COOPERATIVAS DE AHORRO Y CRÉDITO DE EL SALVADOR, R.L.	JEFE DE AUDITORÍA Y SERVICIOS CONTABLES	EL SALVADOR
87	NUÑEZ JUANA ALEYDA	COMISIÓN NACIONAL DE BANCA Y SEGUROS	EXAMINADOR 4	HONDURAS
88	OCHOA BAUTISTA JOSÉ LUIS	COMISIÓN NACIONAL BANCARIA Y DE VALORES	VICEPRESIDENTE	MÉXICO
89	OLEA LEYVA ARCELIA	COMISIÓN NACIONAL BANCARIA Y DE VALORES	SUBGERENTE	MÉXICO
90	OLIVA RAÚL	MINISTERIO DE ECONOMÍA	ASESOR	CHILE
91	OROZCO WATERS ALFONSO	COMISIÓN NACIONAL BANCARIA Y DE VALORES	DIRECTOR GENERAL	MÉXICO
92	ORTA MARTÍNEZ MANUEL	FEDERACIÓN REGIONAL DE COOPERATIVAS DE AHORRO Y PRÉSTAMO CENTRO-SUR, S.C.L.	JEFE DEL DEPARTAMENTO DE OPERACIONES	MÉXICO
93	ORTEGA CARVAJAL JOSÉ ANTONIO	ASOCIACIÓN MEXICANA DE UNIONES DE CRÉDITO DEL SECTOR SOCIAL, A.C. AMUCSS	ENCARGADO DE ANÁLISIS FINANCIERO	MÉXICO
94	ORTELLADO SIENRA LOURDES	LA COOPERATIVA UNIVERSITARIA	MIEMBRO DEL CONSEJO DE ADMINISTRACIÓN	PARAGUAY
95	ORTÍZ GUÁNES ANTONIO	INSTITUTO NACIONAL DE COOPERATIVISMO (INCOOP)	DIRECTOR	PARAGUAY
96	OVIEDO GÁMEZ JOEL	FEDERACIÓN DE COOPERATIVAS DEL NOROESTE	PRESIDENTE DEL CONSEJO DE ADMINISTRACIÓN	MÉXICO
97	PABST MARLYS	BANCO CENTRAL DE CHILE	ANALISTA	CHILE
98	PAGNUSSAT ALCENOR	CONFEDERACIÓN INTERESTATAL DE LAS COOPERATIVAS SICREDI	PRESIDENTE	BRASIL
99	PENIDO HELI	CONFEDERACIÓN NACIONAL DE LAS COOPERATIVAS SICOOB, LTDA.	PRESIDENTE	BRASIL
100	PÉREZ ABELLEYRA GUSTAVO	COMISIÓN NACIONAL BANCARIA Y DE VALORES	SUPERVISOR	MÉXICO

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No.	NOMBRE	INSTITUCIÓN	PUESTO	PAÍS
101	POLINO GÓMEZ EDUARDO	COMISIÓN NACIONAL BANCARIA Y DE VALORES	SUPERVISOR EN JEFE	MÉXICO
102	PRENDES HERRERA JOAQUÍN	COMISIÓN NACIONAL BANCARIA Y DE VALORES	DIRECTOR GENERAL	MÉXICO
103	RABINES MANUEL	FEDERACIÓN NACIONAL DE COOPERATIVAS DE AHORRO Y CRÉDITO DEL PERÚ	DIRECTOR EJECUTIVO	PERÚ
104	RAMÍREZ SOTO ALBERTO	COMACREP	VICEPRESIDENTE	MÉXICO
105	RANGEL VILLAGÓMEZ FELIPE	DID-BANSEFI	CONSULTOR EXTERNO	MÉXICO
106	RIVAROLA MERNER MIGUEL ANGEL	CHEMONICS INTERNATIONAL, INC.	JEFE DEL PARTIDO	MÉXICO
107	RIVERA GARCÍA SONIA	DIGECOOP, MINISTERIO DEL TRABAJO	DIRECTORA DEL REGISTRO NACIONAL	NICARAGUA
108	RIVERA JOSÉ EVERARDO	SUPERINTENDENCIA DEL SISTEMA FINANCIERO DE EL SALVADOR	MIEMBRO DEL CONSEJO DIRECTIVO DE LA INSTITUCIÓN	EL SALVADOR
109	ROCHA VACÍO JOSÉ	PRICEWATERHOUSECOOPERS	SOCIO DE AUDITORÍA	MÉXICO
110	RODRÍGUEZ ANA GLORIA	SUPERINTENDENCIA DEL SISTEMA FINANCIERO DE EL SALVADOR	AUDITOR DE LA UNIDAD DE INTERMEDIARIOS FINANCIEROS NO BANCARIOS	EL SALVADOR
111	RODRÍGUEZ FERNÁNDEZ BENITO	COMACREP	INTEGRANTES DE LA COMISIÓN DE SUPERVISIÓN AUXILIAR	MÉXICO
112	RODRÍGUEZ MARÍA EPIFANIA	BANCO CENTRAL DEL PARAGUAY	JEFE DE NORMAS	PARAGUAY
113	RODRÍGUEZ ORTEGA MARÍA GUADALUPE	UNIDAD DE CONTROL INTEGRAL, S.C. UNICIM	COORDINADOR DE SUPERVISIÓN	MÉXICO
114	ROJO GONZÁLEZ ABIGAIL	COMISIÓN NACIONAL BANCARIA Y DE VALORES	INSPECTOR "A"	MÉXICO
115	ROMÁN TACUBA LUIS ESTEBAN	ASOCIACIÓN OAXAQUEÑA DE COOPERATIVAS DE AHORRO Y CRÉDITO/FEDERACIÓN ATLÁNTICO PACÍFICO	DIRECTOR DE SUPERVISIÓN DEL COMITÉ	MÉXICO
116	ROSALES TENIENTE JOSÉ	FEDERACIÓN DE COOPERATIVAS DEL NOROESTE	INSPECTOR	MÉXICO
117	RUEDA ACEVEDO FLORENTINO	SUPERINTENDENCIA DE LA ECONOMÍA SOLIDARIA	COORDINADOR DEL CONVENIO BID PARA EL SECTOR DE AHORRO Y CRÉDITO	COLOMBIA
118	RUÍZ GONZÁLEZ SERGIO RICARDO	AMSAP	AUDITOR INTERNO	MÉXICO
119	RUÍZ ORTEGA SOFÍA ALEJANDRA	COMISIÓN NACIONAL BANCARIA Y DE VALORES	SUPERVISOR	MÉXICO
120	SAGASTUME CARLOS ALBERTO	CALIFICADORA DE INSTITUCIONES WOCCU	TÉCNICO EN ANÁLISIS DE RIESGOS	GUATEMALA

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No.	NOMBRE	INSTITUCIÓN	PUESTO	PAÍS
121	SALAZAR GONZÁLEZ ESTEBAN	COMISIÓN NACIONAL BANCARIA Y DE VALORES	SUPERVISOR	MÉXICO
122	SAN JUAN RAMÍREZ RUFINO	ASOCIACIÓN OAXAQUEÑA DE COOPERATIVAS DE AHORRO Y CRÉDITO/FEDERACIÓN ATLÁNTICO PACÍFICO	PRESIDENTE DE LA FEDERACIÓN ATLÁNTICO PACÍFICO	MÉXICO
123	SÁNCHEZ CRUZ GUSTAVO	ASOCIACIÓN MEXICANA DE UNIONES DE CRÉDITO DEL SECTOR SOCIAL, A.C. AMUCSS	DIRECTOR OPERATIVO	MÉXICO
124	SANTOS LÓPEZ GILDA IDALIA	COMISIÓN NACIONAL BANCARIA Y DE VALORES	INSPECTOR "A"	MÉXICO
125	SEGOVIA BOLTES MODESTO	CENCOPAN, LTDA.	PRESIDENTE	PARAGUAY
126	SIERRA ALVAREZ FÉLIX	CAJA POPULAR MEXICANA/AMSAP	DIRECTOR DE CONTRALORÍA	MÉXICO
127	SILVA NAVA AARÓN	BANSEFI	DIRECTOR GENERAL ADJUNTO DE PLANEACIÓN ESTRATÉGICA Y EVALUACIÓN	MÉXICO
128	SOSA YAÑEZ FACUNDO	CONSEJO COORDINADOR NACIONAL DE CAJAS SOLIDARIAS	COMITÉ DE SUPERVISIÓN	MÉXICO
129	SUIRA ABDIEL E.	CORPORACIÓN FONDO DE GARANTÍA DE COOPERATIVAS DE AHORRO Y CRÉDITO DE PANAMÁ, R.L. (COFEP)	PRESIDENTE	PANAMÁ
130	TABOADA CORTINA SERGIO	COMISIÓN NACIONAL BANCARIA Y DE VALORES	INSPECTOR	MÉXICO
131	TORRES MALLEA MARCELO	VICEMINISTERIO DE ASUNTOS FINANCIEROS	DIRECTOR GENERAL DE SEGUIMIENTO FINANCIERO	BOLIVIA
132	VALLE PÉREZ JORGE	UNISAP DE OCCIDENTE, A.C.	DIRECTOR DEL COMITÉ DE SUPERVISIÓN	MÉXICO
133	VALVANEDA REBELES JOSE	UNISAP DE OCCIDENTE, A.C.	ASISTENTE DE ASESORÍAS	MÉXICO
134	VIDARGAS ROJAS BENJAMÍN	COMISIÓN NACIONAL BANCARIA Y DE VALORES	VICEPRESIDENTE	MÉXICO
135	VILLARREAL ELNECAVE JOSÉ	UNIDAD DE CONTROL INTEGRAL, S.C. UNICIM	ENCARGADO DE ANÁLISIS FINANCIERO	MÉXICO
136	VILLARREAL JACINTO	CORPORACIÓN FONDO DE GARANTÍA DE COOPERATIVAS DE AHORRO Y CRÉDITO DE PANAMÁ, R.L. (COFEP)	GERENTE GENERAL	PANAMÁ
137	YUNDA EDUARDO	COLAC	GERENTE GENERAL	PANAMÁ
138	ZAPATA PECH MARÍA EUGENIA	UNIDAD OPERATIVA COMITÉ DE SUSPERVISIÓN MÉRIDA/SISTEMA COOPERA	RESPONSABLE DE LA UNIDAD	MÉXICO
139	ZARCO GONZALO ALBERTO	SUPERINTENDENCIA DE BANCOS DE GUATEMALA	SUPERINTENDENCIA DE BANCOS DE GUATEMALA	GUATEMALA
140	ZAVALA JOSÉ MIGUEL	SUPERINTENDENCIA DE BANCOS E INSTITUCIONES FINANCIERAS	JEFE, DEPARTAMENTO DE ESTUDIOS	CHILE

PARTICIPANTS

No.	NOMBRE	INSTITUCIÓN	PUESTO	PAÍS
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142	ZUÑIGA IZQUIERDO ALMA ELENA	COMISIÓN NACIONAL BANCARIA Y DE VALORES	INSPECTOR "A"	MÉXICO

SPEAKERS & ORGANIZERS
SEMINARIO DE MEJORES PRÁCTICAS PARA LA SUPERVISIÓN DE COOPERATIVAS DE AHORRO Y CRÉDITO
29 a 31 de mayo de 2002

Nombre	Apellido	Cargo	Organización	País
Janet	Paz-Castillo	Subdirectora	Agencia Estadounidense para Desarrollo Internacional (USAID)	México
Arthur	Arnold	Presidente y Director Ejecutivo	Consejo Mundial de Cooperativas de Ahorro y Crédito (WOCCU)	Estados Unidos
David	Richardson	Gerente Ejecutivo de Desarrollo Técnico	Consejo Mundial de Cooperativas de Ahorro y Crédito (WOCCU)	Estados Unidos
Matthias	Arzbach	Director, Oficina Regional para América Latina y el Caribe	Confederación Alemana de Cooperativas (DGRV)	Costa Rica
Glenn	Westley	Asesor Senior	Banco Interamericano de Desarrollo	Estados Unidos
José	Velasco	Examinador	Administración Nacional de Cooperativas de Ahorro y Crédito (NCUA)	Estados Unidos
Adriana	Maturana	Asesora	Développement International Desjardins	México
Nelson Alexis	Aldana	Director Ejecutivo	Calificadora de Instituciones WOCCU	Guatemala
Rudy	Araujo	Secretario Ejecutivo	Asociación de Supervisores Bancarios de las Américas (ASBA)	México
Helmut	Pabst	Director de Proyecto	Confederación Alemana de Cooperativas (DGRV)	Chile
Hector	Noriega	Examinador	Administración Nacional de Cooperativas de Ahorro y Crédito (NCUA)	Estados Unidos
Patricio	Riquelme	Jefe del Departamento de Auditoría	Federación Chilena de Cooperativas de Ahorro y Crédito	Chile
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Altamar	García Méndez	Gerente Técnico do Departamento de Supervisión Directa	Banco Central do Brasil	Rio Grade do Sul, Brasil
Henry	Murillo	Director General de Supervisión de Entidades Financieras no Bancarias	Superintendencia General de Entidades Financieras	Costa Rica
Juan Carlos	Pizarro	Jefe de División, Intendencia de Supervisión de Entidades no Bancarias	Superintendencia de Bancos y Entidades Financieras	Bolivia
Jessica	Bravo	Supervisora	Superintendencia de Bancos e Instituciones Financieras	Chile
Galo	León	Director de Microfinanzas	Superintendencia de Bancos y Seguros	Ecuador

SPEAKERS & ORGANIZERS

Nombre	Apellido	Cargo	Organización	País
Luis Humberto	Ramírez	Consultor	Confederación Alemana de Cooperativas (DGRV)	Colombia
Mark	Cifuentes	Director Regional de América Latina, el Caribe y Africa	Consejo Mundial de Cooperativas de Ahorro y Crédito (WOCCU)	Estados Unidos
Alvaro	Durán	Asistente de Proyecto	Confederación Alemana de Cooperativas (DGRV)	Costa Rica
Janette	Klaehn	Gerente del Programa de Mejores Prácticas de Ahorros	Consejo Mundial de Cooperativas de Ahorro y Crédito (WOCCU)	Estados Unidos
Anna Cora	Evans	Analista, WOCCU Washington	Consejo Mundial de Cooperativas de Ahorro y Crédito (WOCCU)	Estados Unidos
Monnie	Biety	Consultora		Estados Unidos
Mario	Galarraga	Director	WOCCU México	México
Jeremy	Smith	Experto de Microfinanzas	Agencia Estadounidense para Desarrollo Internacional (USAID)	Estados Unidos

From Mexico

Jonathan	Davis	Presidente	Comision Nacional Bancaria y de Valores (CNBV)	México
Pablo	Escalante	Vicepresidente de Supervision de Instituciones Financieras "3"	Comision Nacional Bancaria y de Valores (CNBV)	México
Guillermo	Zamarripa	Vicepresidente de Supervision de Instituciones Financieras "1"	Comision Nacional Bancaria y de Valores (CNBV)	México
Héctor	Tinoco	Vicepresidente de Normatividad	Comision Nacional Bancaria y de Valores (CNBV)	México

Attachment 11

Presentations from Supervision Best Practice Conference, Mexico City, Mexico

ENCLOSED

Attachment 12

Participant list from Savings Best Practices Conference, Washington, DC

NAME	LAST NAME	TITLE	ORGANIZATION	COUNTRY
Susan	Achilo	Credit Officer	Uganda Small Scale Industries Association	Uganda
Glenda Patricia	Acosta de Meonez	Lic. Contaduria Publica	COOMPOL	Honduras
Dale	Adams	Professor Emeritus	The Ohio State University	USA
Pauline	Albright	NGO	Maryknoll Office for Global Concerns	USA
Elvis Benito	Alva Galvez	Consultant	Carana Corporation	Honduras
Carlmagno	Amaya	Gerente General	FACACH	Honduras
José	Aparicio S.	Gerente General	Cooperativa Inca Huasi	Bolivia
Paul	Armbruster	Director of International Relations	DGRV	Germany
Arthur	Arnold	President and CEO	WOCCU	USA
Matthias	Arzbach	Director for Latin America and the Caribbean	DGRV	Costa Rica
Caroline E.	Averch	Associate Development Specialist	Development Alternatives, Inc.	USA
Moisés	Ayala Rojas	Licenciado	Caja Popular Mexicana, SAP	Mexico
Mahlon	Barash	Microfinance (of Housing) Specialist	Independent Consultant	USA
Francisco	Barcelo		CENCOPAN	Paraguay
Leslie	Barcus	Microfinance Specialist	CGAP	USA
Pham Tanh	Binh	Director, Bank and Non-Bank Credit Institutions Dept.	State Bank of Vietnam	Vietnam
Brian	Branch	Vice President	WOCCU	USA
William	Brands	Acting Team Leader, Broad-based Economic Growth Group, LAC Bureau	USAID	USA
J. Dickson	Brown			USA
Tillman	Bruett	Partner	Alternative Credit Technologies	USA
Oyungerel	Byambajav	CEO	Netmon LLC	Mongolia
Tom	Carter	Cooperatives Coordinator	USAID/BHR/PVC	USA
Robert	Christen	Senior Advisor	CGAP	USA

Mark	Cifuentes	Regional Manager for Latin America, the Caribbean and Africa	WOCCU	USA
Monique	Cohen	President	Microfinance Opportunities	USA
Brett E.	Coleman	Project Economist	Asian Development Bank	Philippines
Héctor David	Córdova	Gerente Corporativo	FEDECACES	El Salvador
Isabel	Cruz	Director	Asociación Mexicana de Uniones de Crédito del Sector Social, A.C.	México
Ana Carolina	Cruz Aguilar		CNBV	México
Carlos	Cuevas	Principal Financial Economist	World Bank	USA
Angel	Dávila G.	Gerente General	Cooperativa San José de Punata	Bolivia
Carla	Decker	President/CEO	District Government Employees FCU	USA
Janice	Del Aguila	Graduate Student	Georgetown University	USA
Prakash	Dhanrajh	Vice President	MICROFIN St Lucia Ltd.	Trinidad
Henri	Dommel	Rural Finance Adviser	International Fund for Agricultural Development	Italy
Sergio	Duchen	Director Programa Movilizacion del Ahorro Popular	Fondo de Desarrollo del Sistema Financiero y de Apoyo al Sector Productivo	Bolivia
Bat-Ochir	Dugersuren	CFO	XacBank	Mongolia
Arti	Duggal	Project Manager	Bankworld Inc.	USA
Donald	Eberly	Senior Counselor for Civil Society	USAID	USA
Anna Cora	Evans	Development Finance Analyst	WOCCU	USA
David	Ferrand	Financial Sector Specialist	Department for International Development	Kenya
Heike	Fiedler	Principal Advisor	DSF-GTZ	Bolivia
Gary	Fine	Senior Private Sector Development Specialist	The World Bank	USA
Catherine	Ford	Manager	WOCCU	USA
Adolfo	Franco	Assistant Administrator for Latin America and the Caribbean	USAID	USA

Alfonso	García Moreno	Licenciado	Caja Popular Mexicana, SAP	Mexico
Fabián	Garcíarivas Reyes		CNBV	Mexico
Charlie	Garrigues	Senior Payment Infrastructure Specialist	World Bank	USA
Judith	Gilmore	PVC Office Director	USAID	USA
Mario Alberto	Gonzalez Espinoza	General Director	Union de Crédito Progreso, SA	Mexico
David	Grace	Financial and Regulatory Affairs Manager	WOCCU	USA
Raul	Guevara	Operations Officer	OAS Staff FCU	USA
Olga	Guzman de Rodrigu	Secretaria Comercial	COOMPOL	Honduras
Joan	Hall	Independent Consultant		USA
Magdalene G.	Harris	Micro-credit Field Monitor	UNDP/UNOPS Micro-credit	Liberia
Kelly	Hattel	Director	MicroFinance Network	USA
Mark	Havers	Regional Manager	MICROFIN St Lucia Ltd.	St Lucia
Janet	Heisey	Senior Program Associate for Asia	Trickle Up Program	USA
Brigit	Helms	Microfinance Specialist	CGAP	France
Madeline	Hirschland	Consultant		USA
Claus	Hoehler	Director of Latin America and the Caribbean	DGRV	Germany
Jenny	Hoffmann	CEO	Teba Bank	South Africa
Vu Manh	Hong	Expert of Bank and Non-Bank Credit Institutions Department	State Bank of Vietnam	Vietnam
Kamewe Tsafack	Hugues	Adviser, Financial Sector Development	World Savings Banks Institute	Belgium
Kayitare	Innocent	President	Union of Popular Banks of Rwanda	Rwanda
Saiful	Islam	Senior Associate, Micro Lending and Savings	Women's World Banking	USA
Lucy	Ito	Vice President	WOCCU	USA
Maria	Jaramillo	Director, Research and Development	ACCION	USA
Salim	Jiwani	Chief Operations Officer	The First Microfinance Bank Ltd.	Pakistan

Vendy	Kabele	Marketing Manager	Bankworld Inc.	USA
Alex	Kakuru	General Manager	Faulu Uganda Limited	Uganda
Dean	Karlan	Assistant Professor	Princeton University	USA
H.E. Dr. Specioza	Kazibwe	Vice President of Uganda		Uganda
Janette	Klaehn	Savings Best Practices Project Manager	WOCCU	USA
Zeynep	Kudatgobilik	Consultant	The World Bank	USA
Tiffany	Kultgen	Savings Best Practices Project Intern	WOCCU	USA
Anthony	LaCreta	Director, Office of Credit Union Dev.	National Credit Union Administration	USA
Rolando	Lafuente Anzoleaga	Gerente General	Cooperativa Quillacollo	Bolivia
Rafael	Laguna	Licenciado	COMACREP, A.C.	México
Le Thi	Lan	Project Coordinator	WOCCU Vietnam	Vietnam
Kathryn	Larcombe		TCHUMA	Mozambique
Caesar	Layton	Program Officer	Counterpart International	USA
Donald	Lee	Chief, Poverty Eradication and Employment Unit, Division for Social Policy and Development	United Nations	USA
Jose	Linares	Consultant		Venezuela
Arno	Loewenthal	Financial Advisor	Deutsche Gesellschaft fur Technische Zusammenarbeit (GTZ)	Guatemala
Jorge	Lorenzana	Strategic Planning Officer	BANSEFI	México
Adriana	Lubbe	Nedcor Bank Wealth Creation & Preservation Business Analyst	Nedcor Bank	South Africa
Sixdon	Macasaet	Department Manager, Cooperative Policy Research & Institutional Development Department	NATCCO	Philippines
Eliza	Mahony	Senior Program Manager	Corporation for Enterprise Development	USA

Douglas	Maldonado	Gerente General	Cooperativa de Ahorro y Credito Financiera Avances	Nicaragua
Carolyn	Mayorga	Meetings Assistant P.T.	WOCCU	USA
Elizabeth	McGuiness	Economic Opportunities Specialist	Save the Children	USA
Christopher	McHugh	Gerente Financiero	Central de Cooperativas de Ahorro y Credito Financieras de Nicaragua	Nicaragua
Rafael	Medina	Engineer	Sistema Coorepa Peninsular Crescencio A Cruz	México
Bertha Silvia	Mena de Morán	Gerente de negocios y administración	FEDECACES	El Salvador
Edith	Mendoza de Villatoro		COOMPOL	Honduras
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Hillary	Miller	Microfinance Specialist	SEFIR Project/Development Alternatives, Inc.	Bolivia
Adrienne D.	Munroe	Economic Development Specialist	National Credit Union Administration	USA
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Juan	Navarrete	Social & Economic Analysis Coordinator	BANSEFI	México
Dorothy	Ndegwa	Student	Marymount University	USA
James	Njuguna Mwangi	Finance Director	Equity Building Society	Kenya
Dan	Norell	Team Leader, Microenterprise Development	World Vision Inc	USA
Donat	Nyilinkindi	Research and Marketing Director	URWEGO	Rwanda
Willy	Nzisabira	Managing Director	URWEGO/World Relief	Rwanda
John	Owens	Chief of Party, Microenterprise Access to Banking Services (MABS), Philippines	Chemonics	Philippines
Cathia	Palmer	Executive Vice President	MIBANCO	Panama

John	Pamba	Political Assistant to Her Excellency the Vice President in Charge of Political Affairs	Republic of Uganda	Uganda
Gerry	Pemberton	President	MICROFIN St Lucia Ltd.	Trinidad
Jerome	Pierre-Makime	Director of Operations	Fonkoze	Haiti
Gary	Plank	Second Vice Chairman, WOCCU	Arizona Credit Union League	USA
Tony	Polatajko	Enterprise Development Advisor	DFID	United Kingdo
Luis	Porto	Economist	Confiar - Red Financiera Cooperativa	Uruguay
E. Everett	Post	Program Advisor	Five Talents International	USA
Elmer	Quesnay Diaz	Presidente del consejo de administracion	Finantel Cooperativa de Ahorro y Credito	Peru
Elisabeth	Quispe de Alemán	Presidente	Cooperativa Quillacollo	Bolivia
Manuel	Rabines	General Manager	FENACREP	Peru
Bikki	Randhawa	Senior Financial Specialist	World Bank	USA
Ben	Reno-Weber	Program Assistant	CGAP	USA
Elizabeth	Rhyne	Senior Vice President, Research, Development and Policy	ACCION International	USA
Dave	Richardson	Senior Manager of Technical Development	WOCCU	USA
Silvio	Rivera Lugo	Gerente General	Cooperativa Financiera La Armonia	Nicaragua
Alicia	Robb	Economist	Federal Reserve Board	USA
Marguerite	Robinson	Institute Fellow Emeritus, HIID	Harvard University	USA
Jim	Roth		ILO	Switzerland
Antonio	Salazar	Engineer	Asociación Mex. de Sociedades de Ahorro y Préstamo, AC	México
Petr	Scholz	Deputy Director of Financial Market Dpt.	Ministry of Finance of the Czech Republic	Czech Republ
Modesto	Segovia Boltes	President	CENCOPAN	Paraguay

Nitza E.	Segui Albino	Chief Executive Officer	International Migrants Development Fund	USA
Daniel	Seller	Consultant		Austria
Steven	Shepelwich	Senior Program Manager	Corporation for Enterprise Development	USA
William	Smith	Director	WOCCU Vietnam	Vietnam
KC	Soares	1st Vice Chairman Board of Directors	OAS FCU	USA
Ayinkamiye	Spéciose	General Manager	Union of Popular Banks of Rwanda	Rwanda
H.E. Mrs. Edith Gra	Ssempala	Ambassador (to the US) Extraordinary & Plenipotentiary	Embassy of Uganda	Uganda
Ahmed	Ssenyomo	Minister Counselor, Deputy Chief of Mission and Head of Chancery	Embassy of Uganda	Uganda
Mark	Staehle	Interim Director	SafeSave	Bangladesh
Lisa	Taber	Consultant	World Bank	USA
Rusoke	Tagaswire	ADC/Technical for Government of Uganda		Uganda
Charles	Tansey	Senior Policy Advisor	Neighborhood Reinvestment Corporation	USA
Miguel	Ulloa	Projects & Evaluation Officer	BANSEFI	México
Ted	Vail	President	Strategic Development International	USA
Liza	Valenzuela	Deputy Director, Office of Microenterprise Development	USAID	USA
Marinke	van Riet	Program Officer for Africa	Trickle Up Program	USA
Alfonso	Vega A.	Microfinance Analyst	CGAP	USA
Barton	Veret	Vice Chairman	Lafayette Federal Credit Union	USA
Robert C.	Vogel	Executive Director	International Management and Communications Corporation (IMCC)	USA

Gretchen	Warner	Executive Director	U.S. Overseas Cooperative Development Council (OCDC)	USA
Christina	Way			USA
Ted	Weihe	Executive Director	U.S. Overseas Cooperative Development Council (OCDC)	USA
Glenn	Westley	Senior Advisor	Inter-American Development Bank	USA
Graham	Wright	Program Director	MicroSave-Africa	Kenya

*Fax numbers are provided in place of missing e-mail addresses.

NAME	LAST NAME	TITLE	ORGANIZATION
Adolfo	Franco	Assistant Administrator for Latin America and the (	USAID
Paul	Armbruster	Director of International Relations	DGRV
Arthur	Arnold	President and CEO	WOCCU
		Vice President of Uganda	
Brian	Branch	Vice President	WOCCU
Anna Cora	Evans	Development Finance Analyst	WOCCU
Graham	Wright	Program Director	MicroSave-Africa
Lucy	Ito	Vice President	WOCCU
Mark	Staehle	Interim Director	SafeSave
Madeline	Hirschland	Consultant	
Marguerite	Robinson	Institute Fellow Emeritus, HIID	Harvard University
Mark	Cifuentes	Regional Manager for Latin America, the Caribbea	WOCCU
Dale	Adams	Professor Emeritus	The Ohio State University
William	Brands	Acting Team Leader, Broad-based Economic Grov	USAID
Brian	Branch	Vice President	WOCCU
Jose	Linares	President	Jose Linares & Associates
David	Grace	Financial and Regulatory Affairs Manager	WOCCU
Liza	Valenzuela	Deputy Director, Office of Microenterprise Develop	USAID
Brigit	Helms	Microfinance Specialist	CGAP
Dave	Richardson	Senior Manager of Technical Development	WOCCU
John	Owens	Chemonics Chief of Party, Microenterprise Access	to Banking Services (MABS), Philippines
Elizabeth	Rhyne	Senior Vice President, Research, Development an	ACCION International
Robert	Christen	Senior Advisor	CGAP
Glenn	Westley	Senior Advisor	Inter-American Development Bank
Matthias	Arzbach	Director for Latin America and the Caribbean	DGRV
Carlos	Cuevas	Principal Financial Economist	World Bank
Janette	Klaehn	Savings Best Practices Project Manager	WOCCU
Carolyn	Mayorga	Meetings Assistant P.T.	WOCCU
Tiffany	Kultgen	Savings Best Practices Project Intern	WOCCU

World Council of Credit Unions, Inc.
Savings Best Practices

Attachment 13

Presentations from Savings Best Practices Conference, Washington, DC

ENCLOSED

Attachment 14

Contract Between WOCCU and Pact Publications for Final Publication

1200 18th Street, N.W., Suite 350
Washington, DC 20036
Tel: 202.466.5666

Fax: 202.466.5669
pact@pacthq.org
www.pactworld.org

Pact

Publishing Agreement between World Council of Credit Unions, Inc. (WOCCU) and Pact Publications

This contract sets forth the agreement between the World Council of Credit Unions (WOCCU) and Pact Publications (Pact) concerning the publication a work tentatively entitled *Striking the Balance in Microfinance: A Practical Guide to Mobilizing Savings* (the "Work") on the terms and conditions that follow.

1. Grant of Rights. Pact agrees to print, publish, market, distribute, and sell the Work throughout the world for as long as this agreement is in effect. WOCCU reserves all other rights including but not limited to the right to prepare translations and derivative works.

2. Manuscript Delivery. WOCCU agrees to provide Pact with an original and electronic copy of the final, edited manuscript in photo-ready condition by September 27, 2002. Pact must be notified in writing of any modification of this submission date. Electronic files will include a formatted PDF file as well as complete Quark or Adobe Illustrator files including cover and all images, fonts, color and other specifications. WOCCU agrees to make any reasonable desktop publishing or text changes required for printing.

3. Publication Date. Pact agrees to publish the book in its final form by no later than October 25, 2002. Any modification of this publication date must be agreed upon in writing by both parties.

4. Manuscript Specifications. Pact will produce the publication according to the following specifications:

a. 6x9 inch dimensions
b. 2-color matte cover, to be designed by WOCCU
c. high quality white paper
d. perfect (glue and cut style) binding
e. in compliance with printing regulations for publications supported by the U.S. Agency for International Development

5. Price, Sale and Royalties. The initial retail sales price will be no more than $22.00. Pact will review the retail price annually and may make modifications as needed to maintain profitability. Pact agrees to notify WOCCU of any changes to the full

retail sales price through an amendment to this agreement. Pact retains the right to offer discounts to the sales price as appropriate and at its sole discretion without notification but in no event more than 50% off the cover price. Sales revenues will be divided as follows:

a. 80% of net revenues for Pact.
b. 20% of net revenues for WOCCU.

"Net revenues" for the purposes of this Agreement, means amounts actually received less returns and shipping.

6. Accounting and Payment. WOCCU will credit USAID as required. Pact will provide accounting to WOCCU setting forth the number of books sold, the purchasers of the books, the sales price of the books, and the net revenues realized from the book sales two times per year, or every six months. The royalty payments and accounting statements shall be provided within forty-five (45) days of the end of the preceding six months.

7. Copyrights. WOCCU will retain copyright of the publication and will register the copyrights in its name in the United States and any other countries it determines are appropriate.

8. Copyright Infringement. If it appears that the copyright in the Work is infringed, and if WOCCU and Pact proceed jointly, the expenses and recoveries, if any, shall be shared equally. If they do not proceed jointly, either shall have the right to bring action, in which event such party shall solely bear the expenses, including the expenses of the other party if they are subsequently brought into any such proceeding after having declined to initiate such proceeding, and be solely entitled to any recoveries including any recoveries for costs and expenses, and if the copyright shall not be registered in the name of such party, the other hereby authorizes the action to be brought in the other's name. WOCCU and Pact agree to cooperate fully in any claim or other action seeking to protect or enforce any right granted to Pact in the Work

9. Out of Print.

a. The Work shall be considered in print if it is on sale by Pact in any edition. If the Work is not in print, WOCCU may request in writing Pact keep the Work in print. Pact shall have two (2) months to comply. If Pact fails to comply or does not wish to keep the Work in print, then at the end of this two (2) month period this Agreement shall terminate and all the rights granted to Pact shall revert to WOCCU.

b. In the event of termination under this Paragraph 9, WOCCU shall have the right to purchase the film or plates, if available, of the Work, at the manufacturing cost, including composition, and may, in WOCCU's sole discretion,

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purchase some or all of any remaining copies or sheets of the Work at the manufacturing cost.

10. Pact's Responsibilities. Pact will obtain an ISBN and a LCCN and print an initial run in 2002 of 850 copies of the book. Pact will sell the Work by its usual and customary means, including but not exclusively through: direct mail, online bookstore, print media, organizational contacts, other advertising and exhibition at appropriate conferences. Pact will also provide for distribution to other retail sellers as appropriate.

11. WOCCU's Copies. Pact will ship to WOCCU twenty (20) complimentary copies of the Work upon publication. WOCCU retains the right to purchase up to 500 additional copies of the Work on behalf of authors, for its own use or for resale, at a discount of 50% of the full retail sales price plus any applicable shipping costs. Any copies purchased in excess of this amount will be at a rate of 30% of the full retail sales price and shall be for authors' or its own use only. WOCCU will not be required to split any revenues with Pact if it resells any of the 500 copies at a profit.

12. Termination. This Agreement may be terminated upon 60 days' written notification by either party and may be amended upon written consent of both parties. In case of termination, Pact retains the right to continue to sell any books already produced and still in its possession at the time of termination. In case of termination, WOCCU reserves the right to purchase any stock that Pact is no longer willing to sell at cost, plus shipping.

13. Author's Name. Pact will recognize the contribution of the editors and authors of the Work by placing their names on the Work. The editors and authors agree that Pact may use their name and likeness in advertising and promoting the Work.

14. Notice. Any notice, request or demand required or permitted to be given by either party will be deemed given when mailed by regular mail, postage prepaid, addressed to the respective parties at the following addresses or at such other addresses as either of them may designate for such purpose:

Pact:

Pact Publications
ATTN: Crystal Woods
1200 18th Street, NW Suite 350
Washington, DC 20036

Editor/Author:

World Council of Credit Unions, Inc.
ATTN: Brian Branch and Janette Klaehn
5701 Mineral Point Road
Madison, WI 53705

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15. Heirs and Assignment. This agreement will be binding upon and inure to the benefit of our successors and assigns and their personal representative, heirs and successors.

16. Waiver. No waiver of any provision of this agreement will be effective unless it is in writing and signed by the parties, and no waiver of any breach will be deemed a waiver of any subsequent breach.

17. Choice of Law. This agreement will be interpreted according to the laws of the State of Wisconsin.

Agreed to by:

Pact Publications, a program of Pact, Inc. 1200 18th St. NW, Suite 350 Washington, DC 20024 P: (202) 466-5666 F: (202)466-5669	World Council of Credit Unions, Inc. 5710 Mineral Point Road Madison, WI 53705 P: (608) 231-8634 F: (608) 238-8020
Sarah Newhall Sarah Newhall President and CEO	Mary J Chapman Mary Chapman Vice President and CFO
August 13, 2002 Date	Sept 2, 2002 Date

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www.pactworld.org

Pact

Publishing Agreement between World Council of Credit Unions, Inc. (WOCCU) and Pact Publications

This contract sets forth the agreement between the World Council of Credit Unions (WOCCU) and Pact Publications (Pact) concerning the publication a work tentatively entitled *El balance en microfinanzas: una guía práctica para la movilización de ahorros* (the "Work") on the terms and conditions that follow.

1. Grant of Rights. Pact agrees to print, publish, market, distribute, and sell the Work throughout the world for as long as this agreement is in effect. WOCCU reserves all other rights including but not limited to the right to prepare translations and derivative works.

2. Manuscript Delivery. WOCCU agrees to provide Pact with an original and electronic copy of the final, edited manuscript in photo-ready condition by January 31, 2003. Pact must be notified in writing of any modification of this submission date. Electronic files will include a formatted PDF file as well as complete Quark or Adobe Illustrator files including cover and all images, fonts, color and other specifications. WOCCU agrees to make any reasonable desktop publishing or text changes required for printing.

3. Publication Date. Pact agrees to publish the book in its final form by no later than February 28, 2002 . Any modification of this publication date must be agreed upon in writing by both parties.

4. Manuscript Specifications. Pact will produce the publication according to the following specifications:

a. 6x9 inch dimensions
b. 2-color matte cover, to be designed by WOCCU
c. high quality white paper
d. perfect (glue and cut style) binding
e. in compliance with printing regulations for publications supported by the U.S. Agency for International Development

5. Price, Sale and Royalties. The initial retail sales price will be no more than $22.00. Pact will review the retail price annually and may make modifications as needed to maintain profitability. Pact agrees to notify WOCCU of any changes to the full

retail sales price through an amendment to this agreement. Pact retains the right to offer discounts to the sales price as appropriate and at its sole discretion without notification but in no event more than 50% off the cover price. Sales revenues will be divided as follows:

a. 80% of net revenues for Pact.
b. 20% of net revenues for WOCCU.

"Net revenues" for the purposes of this Agreement, means amounts actually received less returns and shipping.

6. Accounting and Payment. WOCCU will credit USAID as required. Pact will provide accounting to WOCCU setting forth the number of books sold, the purchasers of the books, the sales price of the books, and the net revenues realized from the book sales two times per year, or every six months. The royalty payments and accounting statements shall be provided within forty-five (45) days of the end of the preceding six months.

7. Copyrights. WOCCU will retain copyright of the publication and will register the copyrights in its name in the United States and any other countries it determines are appropriate.

8. Copyright Infringement. If it appears that the copyright in the Work is infringed, and if WOCCU and Pact proceed jointly, the expenses and recoveries, if any, shall be shared equally. If they do not proceed jointly, either shall have the right to bring action, in which event such party shall solely bear the expenses, including the expenses of the other party if they are subsequently brought into any such proceeding after having declined to initiate such proceeding, and be solely entitled to any recoveries including any recoveries for costs and expenses, and if the copyright shall not be registered in the name of such party, the other hereby authorizes the action to be brought in the other's name. WOCCU and Pact agree to cooperate fully in any claim or other action seeking to protect or enforce any right granted to Pact in the Work

9. Out of Print.

a. The Work shall be considered in print if it is on sale by Pact in any edition. If the Work is not in print, WOCCU may request in writing Pact keep the Work in print. Pact shall have two (2) months to comply. If Pact fails to comply or does not wish to keep the Work in print, then at the end of this two (2) month period this Agreement shall terminate and all the rights granted to Pact shall revert to WOCCU.

b. In the event of termination under this Paragraph 9, WOCCU shall have the right to purchase the film or plates, if available, of the Work, at the manufacturing cost, including composition, and may, in WOCCU's sole discretion,

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purchase some or all of any remaining copies or sheets of the Work at the manufacturing cost.

10. Pact's Responsibilities. Pact will obtain an ISBN and a LCCN and print an initial run in 2003 of 400 copies of the book. Pact will sell the Work by its usual and customary means, including but not exclusively through: direct mail, online bookstore, print media, organizational contacts, other advertising and exhibition at appropriate conferences. Pact will also provide for distribution to other retail sellers as appropriate.

11. WOCCU's Copies. Pact will ship to WOCCU twenty (20) complimentary copies of the Work upon publication. WOCCU retains the right to purchase up to 250 additional copies of the Work on behalf of authors, for its own use or for resale, at a discount of 50% of the full retail sales price plus any applicable shipping costs. Any copies purchased in excess of this amount will be at a rate of 30% of the full retail sales price and shall be for authors' or its own use only. WOCCU will not be required to split any revenues with Pact if it resells any of the 250 copies at a profit.

12. Termination. This Agreement may be terminated upon 60 days' written notification by either party and may be amended upon written consent of both parties. In case of termination, Pact retains the right to continue to sell any books already produced and still in its possession at the time of termination. In case of termination, WOCCU reserves the right to purchase any stock that Pact is no longer willing to sell at cost, plus shipping.

13. Author's Name. Pact will recognize the contribution of the editors and authors of the Work by placing their names on the Work. The editors and authors agree that Pact may use their name and likeness in advertising and promoting the Work.

14. Notice. Any notice, request or demand required or permitted to be given by either party will be deemed given when mailed by regular mail, postage prepaid, addressed to the respective parties at the following addresses or at such other addresses as either of them may designate for such purpose:

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Madison, WI 53705

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15. Heirs and Assignment. This agreement will be binding upon and inure to the benefit of our successors and assigns and their personal representative, heirs and successors.

16. Waiver. No waiver of any provision of this agreement will be effective unless it is in writing and signed by the parties, and no waiver of any breach will be deemed a waiver of any subsequent breach.

17. Choice of Law. This agreement will be interpreted according to the laws of the State of Wisconsin.

Agreed to by:

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Mary J. Chapman

Mary Chapman
Vice President and CFO

Sept 2, 2002
Date

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Attachment 16

Book – ***Striking the Balance in Microfinance: A Practical Guide to Mobilizing Savings***

ENCLOSED

Attachment 15

Guide – ***A Technical Guide to Savings Mobilization: Lessons from the Credit Union Experience***

ENCLOSED

Attachment 17

Book – *El logro del equilibrio en las microfinanzas: guía práctica para movilizar los ahorros*

ENCLOSED

Attachment 18

White Paper Overivew of Supervision Practices in Latin America

DRAFT – June 27, 2002

BEST PRACTICES IN CREDIT UNION REGULATION AND SUPERVISION

Written by Monnie M. Biety

Credit unions have been important contributors to social and economic development worldwide since the mid-1800s. Credit unions are now significant players in financial markets in many countries and are here to stay. Therefore they should be regulated and supervised as other financial institutions that take deposits from the public.

Credit unions are cooperative non-profit financial institutions organized to provide their members with a safe place to save and a source of loan funds at reasonable interest rates. Eligibility for membership may be open or defined within the credit union's charter. An individual becomes a member upon approval of an application for membership, subscription to and payment of at least one share and payment of an entrance fee if required by the board of directors. Members exercise democratic control by attending and participating in general and special meetings and by electing officials to oversee operations and to represent their best interests. Each member is entitled to not more than one vote irrespective of the number of shares owned.

Credit unions are an important part of the financial institution environment within a country for several reasons. First they are a prominent source of semi-formal and formal credit to small and medium microenterprises, businesses that larger financial institutions are not interested in lending to, because their scale is outside the scope of a medium and/or large bank. "In Latin America, commercial banks, *financieras* and non-governmental organizations (NGOs) provide a total of about $800 million in loans to micro-enterprises, compared with $2.6 billion for credit unions. This makes credit unions the major source of credit from financial institutions to microenterprises in the region."[1] Second, credit unions are focused on providing a full array of services that members desire and are not driven by the profit motives of their investors. Third, credit unions have a great potential for expansion and growth. As compared to the market penetration of banks, their percentage of the financial marketplace is small (see the table below). Lastly, credit unions reach individuals of limited means, although they are not exclusively oriented to serving the poor. This is a very underserved but economically important segment of the market that credit unions have the ability to serve.

The impact of credit unions and their importance is clearly illustrated in the World Council of Credit Union's 2001 Statistical Report:

Region	Credit Unions	Clients	Penetration*	Loans (US$) Savings (US$)	Assets (US$)
Africa	3,359	1,995,753	2.24%	445,477,529 494,443,632	520,079,533

[1] Safe Money, Glenn D. Westley and Brain Branch, Editors. Washington D.C.: The John Hopkins University Press, 2000.

Asia	13,918	9,103,772	2.31%	14,086,310,283 24,421,894,770	26,157,374,601
Caribbean	359	1,375,757	49.63%	1,130,103,648 1,308,423,339	1,637,624,360
Europe	5,898	5,215,431	3.05%	4,586,507,946 6,780,969,627	7,761,857,395
Latin America	2,022	4,823,994	2.86%	2,316,233,284 2,706,833,872	3,657,710,141
North America	11,049	86,478,181	55.08%	362,553,357,822 485,808,278,669	555,159,291,129
South Pacific	296	3,281,999	28.04%	8,470,351,399 8,929,283,927	10,624,359,644
TOTAL	36,901	112,274,887	11.30%	393,588,341,911 530,450,127,836	605,518,296,803

- The penetration rate is calculated by dividing the total number of reported credit union members by the economically active population.

Why Credit Unions Should Be Regulated?

Any institution that accepts savings deposits from its members or the public should be regulated as to protect the member's money and to establish and maintain a level of trust and confidence in the formal financial system. Credit unions worldwide mobilize savings deposits from their members.

Who Should Regulate Credit Unions?

There is considerable debate about regulating credit unions and to what extent they should be regulated. Existing superintendencies should supervise credit union but most bank supervisors have little interest in regulating credit unions because:

- they are small in asset size and market penetration (credit union failure does not affect the overall economic situation in a country like a bank failure),
- they are geographically dispersed,
- they are mutualist organizations, operated and managed by their member/owners which provides the necessary operational oversight,
- management and officials have limited financial training and knowledge (therefore examiners would have to spend more time with them), and
- superintendencies do not have the budgets or the institutional capacity necessary to provide supervision to all these entities.

This reluctance to supervise credit unions probably could be overcome if the superintendencies charged cost-covering fees for their services. It is in credit unions' best interest to pay the full cost for quality supervision given the benefits received from such oversight.

"If the government is to supervise credit unions directly, the responsibility should be given to the existing banking superintendency-assuming that is has displayed reasonable competency in supervising banking institutions-rather than creating a separate credit union supervisory agency. Creating a new agency would be costly. Keeping banking and credit union supervision together in one institution would also facilitate a consistent regulatory approach to and treatment of different types of supervised financial institutions. It may at the same time be efficient to create a specialized credit union department within the overall superintendency because they have a unique ownership and governance structure and other special characteristics."[2]

Credit unions have many similarities to banks and other financial institutions. In general they offer the same financial products and services (although on a smaller and simpler scale). With regards to risks presented by the services offered, they are similar to other financial institutions.

Banking superintendents use different benchmarks to determine the credit unions that will fall under their authority including asset size, number of members, minimum capital amount, common bonds amongst members, ownership and control by members which is perceived to offer some form of supervision. This perception of member ownership providing supervision is entirely false, because members generally do not have the expertise needed to effectively supervise an institution. This mutual or democratic form sets credit unions apart from other financial institutions. Member oversight is believed to be less than in stockholder owned enterprises because members have only one vote no matter how many shares they have. With only 1 vote, they can not influence operations like stockholders in banks can. This uniqueness must be considered when discussing the institutions and their supervision.

Credit unions that do not meet the requirements of the superintendency and are outside of their scope are at much greater risk of failure. This policy of selection places at risk the savings of many individuals who are of very limited means and make up the most vulnerable segment of society. In many countries the credit unions outside of the scope of the superintendency are monitored by a cooperative development agency. This supervision has proven to be of little or no value. "There is widespread agreement that because of the highly technical nature of prudential supervision, it should be carried out by the banking superintendency not by the cooperative development agency. The latter is charged with promoting and rather superficially overseeing all of the different types of cooperatives in a country. Cooperative development agencies are not equipped to carry out prudential supervision of credit unions."[3]

What is Effective Regulation?

Credit union members are simultaneously the owners and clients; these are separate and distinct entities in a bank. Their desires as clients drive the operating policies and procedures of the institution in their role as owners. This can have a negative long-term effect depending on the member's reasons for joining the credit union. Many members join to access credit. Often this is very obvious in the low loan and savings rates offered. Supervisors have to be aware of these differences and design regulations for these institutions as to minimize the impact of these and other issues.

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[2] IBID, page 18.
[3] IBID, page 18.

All credit unions should be regulated within a framework that includes:

- a law specific to credit union operations,
- standardized institutional bylaws, and
- rules and regulations established by the regulatory body.

In many developing countries credit unions are not regulated under specific credit union regulation. Rather, they are subject to the same general cooperative societies acts that regulate the business operations or non-financial cooperatives and, in a few countries, some sections of financial institutions or banking acts. An ultimate objective of the credit union movement in any jurisdiction should be the enactment of a specific enabling law for credit unions. While credit unions are cooperative organizations, their specialization in financial services makes them different in many significant respects from other cooperative societies. Thus the general cooperative societies acts which govern the business operations of agricultural, consumer, commercial and industrial cooperatives are usually inadequate for credit unions, whose business operations most closely resemble banking institutions. Microfinance institution legislation generally does not recognize the savings orientation of credit unions. Legislation intended for commercial banks is generally inappropriate for credit unions, whose purpose is to provide cooperative financial services to members who are its depositors, borrowers and owners.

The approved credit union law should be general in nature (so as to avoid frequent changes) and address credit union organization, powers, membership, management and administration, share and deposit structure, credits, investment of funds, reserves and allowances, regulation and supervision, credit union associations and voluntary changes in organizations such as charter conversions, mergers, consolidations and liquidations.

Standardized bylaws should be established by the regulatory body that each credit union must adopt prior to commencing operations. Standardized bylaws may be amended only by a credit union submitting a request for change and receiving approval from the regulator. Bylaws are defined as rules adopted by the members and board of directors that:

- define the field of membership,
- establish the par value of shares,
- define the services the credit union can offer,
- define the powers, duties and responsibilities of the officials,
- set the internal procedures it will follow, and
- give the general method by which the credit union functions are to be carried out.

More specifically bylaws address:

- credit union, name, location, purpose, common bond (if applicable), membership requirements,
- capital, liquidity, loan losses and savings requirements,
- the method in which member disputes and expulsions will be handled,
- the procedures for membership meetings and elections of officials,
- the composition, powers, duties, requirements and restrictions of the board of directors, supervisory committee and credit committee (if applicable),

- duties and responsibilities of operational management,
- resolutions of conflicts of interest,
- payment of dividends,
- loans granted to members,
- mergers and liquidations, and
- amendments to bylaws.

Rules and regulations are established, amended or revoked by the agency or institution charged with the supervision of credit unions. These prudential regulations are extremely important and establish minimum operational requirements. Because credit union structure differs from that of a bank there should be rules and regulations that are specific to credit union operations and consider the intricacies of their internal incentives and their mutual-based ownership structure. Prudential regulations should be developed that address, at a minimum, the following areas.

Capital Adequacy – Capital adequacy requirements are the single most important regulatory requirement for the effective management of risk taking by financial intermediaries. This regulation normally specifies that a financial institution should maintain at least a minimum ratio of capital to risk-weighted assets. The ratio is typically between 8-12%. Capital normally is composed of reserves, undivided earnings, accumulated gains and losses and in some countries, shares.

Capital requirements should be higher for a credit union than a bank because the governance structure is more problematic. Credit unions do not have:

- investors that respond to calls to increase capital as in banks,
- geographically dispersion as banks do in the form of regional and national banks (this dispersion allows them to survive local economic shocks), and
- government or private deposit insurance as some countries may have for bank deposits (credit union deposits are totally uninsured). The only insurance credit union depositors have is the accumulated capital.

In order to join a credit union, individuals are required to make a minimum share contribution. In most countries, these shares are considered capital, however they are withdrawable upon membership termination and can be used to secure a loan. Credit unions grant loans based on a multiple of the share balance, 2:1, 5:1 or 10:1. In fact these shares represent a compensating balance for the loan, rather than an equity investment. "Not only have the net borrowers effectively withdrawn their shares in the form of a loan, but also they have borrowed the resources of the net savers and other creditors of the institution. As a result, in a financial crisis, this risk capital is not available; it has already been loaned out to net borrowers, who are unlikely to repay these funds at a future date. Therefore, this risk capital does not provide effective protection to those members who remain net savers of the institution or to other creditors."[4] Because of this treatment of shares they should not be considered capital or in the determination of institution solvency. Shares should only be considered capital if they can not be

[4] IBID, page 148.

withdrawn under any circumstances by members and the funds are available to absorb losses.

Superintendencies have defined minimum capital using several different methods. In the U.S., shares are not considered part of capital. The membership share is part of the regular share account and is nothing more than a savings deposit. Minimum capital is not discussed in the Law or the rules and regulations. Minimum capital requirements are not used to limit the licensing of credit unions. The assessment of capital is handled during the annual examination (within the CAMEL rating) and periodically throughout the year in reviews of financial performance performed by examiners. Credit unions are required to have a net worth (reserves, undivided earnings and net income) to total assets ratio of at least 6%. If it falls below this percent, regulatory action is taken.

Capital adequacy and provisioning for loan losses must be addressed jointly. A credit union can have a respectable capital ratio, but be insolvent if the provision for loan loss account is not adequately funded for potential loan losses. Full and fair disclosure of the credit union balance sheet is addressed in U.S. regulation. The regulation states that the provision for loan loss account must be adequately funded at all times to fully and fairly disclose the true value of credit union assets.

Bolivia has established four categories of minimum capital adequacy for supervised credit unions. Minimum capital requirements were established so that the amounts are constant in real terms. The requirements were indexed to keep them permanently up-to-date. The four categories are:

- Category 1 – 150,000 special drawing rights / Ratio of net worth to risk-weighted assets of at least 20%,
- Category 2 – 250,000 special drawing rights / Ratio of net worth to risk-weighted assets of at least 15 %,
- Category 3 – 630,000 special drawing rights / Ratio of net worth to risk-weighted assets of at least 10%, and
- Category 4 – 5,500,000 special drawing rights / Same as category 3.

Categories 1 and 2 are authorized to engage in basic financial intermediation, primarily mobilizing deposits and making loans, category 3 may also issue and place debt instruments, obtain loans from financial entities abroad and the Central Bank of Bolivia and category 4 is authorized to engage in most operations that banks do.

If a credit union does not have the minimum capital of 150,000 special drawing rights then it is considered a "closed" credit union and is unable to mobilize savings deposit. Only share deposits may be accepted. This policy could force the closure of credit unions and prevent the chartering of new credit unions. Superintendencies need to be careful not to impede local financial intermediation through regulation. Many believe it is a mistake to prohibit deposit taking just because they are too small or remote to be supervised effectively. "Individuals are often well aware that such organizations are risky, but continue to use them because the other available savings options are even riskier-cash in the house can be stolen, livestock can die of disease or be unsaleable when cash is needed. In such cases, the unsupervised community-based depository may well be the least risky option available to the saver."[5]

Shares in Bolivia are considered part of capital; however, they can only be withdrawn with an advance notice of 90 days:

- if the credit union is in compliance with all legal and technical limits,
- if the withdrawal will not decrease the share total to less than 90% of the share balance as of the beginning of the fiscal year, and
- if the credit union does not have a current or accumulated loss.

Regulation also clearly addresses the provisioning for loan losses. Credits are classified into four categories: microcredits, consumer, real estate and commercial. The first 3 categories are classified according to the age of the delinquency and the commercial loans are classified based on the borrower's ability to repay the loan. The loans are then assigned a percentage that indicates the potential loss. The categories and percentages are as follows:

Category	Real Estate Classification	Microcredit and Consumer Classification	Provision Requirement
1. Normal	0-30 days delinquent	0-5 days delinquent	1%
2. Potential Problems	31-90 days delinquent	6-30days delinquent	5%
3. Deficient	91-180 days delinquent	31-60 days delinquent and/or it has been refinanced 1 time	20%
4. Doubtful	181-360 days delinquent	61-90 days delinquent and/or it has been refinanced 2 times	50%
5. Loss	>360 days delinquent	>60 days and/or it has been refinanced 3 or more times	100%

World Council of Credit Unions (WOCCU) addresses capital adequacy and full and fair disclosure in the PERLAS (PEARLS in English) monitoring system (See Annex 2) under Proteccion (Protection) and Estructura Financiera (Financial Structure). The ratios that are used to measure the level of protection within an institution refer to the adequacy of the loan loss provisions and the processes whereby delinquent loans are written off the financial statements. There are two ratios used to determine the adequacy of the loan loss provision. The first measures the amount of provision for loans that are delinquent more than 12 months. The goal ratio is 100%. The second measures the amount of the loan loss provision for loans delinquent between 1 and 12 months. The goal ratio is 35%. Institutional capital ratios are part of the financial structure ratios. The goal for the institutional capital to total assets ratio is at least 10%. Institutional capital does not include member shares, loan loss provisions, or educational, social, or revalued fixed asset reserves that are typically counted as capital under the Basle Accords. The only capital accounts included are statutory reserves and undivided earnings.

[5] The Rush to Regulate: Legal Frameworks for Microfinance, Robert Peck Christen and Richard Rosenberg. Washington, D.C., January 10,2000.

Entry Requirements – Currently regulations addressing entry requirements are minimal in most countries. It is not uncommon to have 20 or fewer individuals starting a credit union with only a small amount of capital. This has a led to a large number of institutions that can not offer their members the services they want and are unable to compete financially because they do not have the economies of scale. Licensing institutions that can not demonstrate sustainability is a mistake and a burden on the agency in charge of regulation and supervision.

In the U.S., prior to chartering a credit union, the regulator must be satisfied that the institution will be viable and that it will provide needed services to its members. A minimum field of membership size for chartering a credit union has not been established. Groups of any size may apply for a charter if they demonstrate economic viability through a business plan. However, often the size of the group is indicative of the potential for success. For this reason, a charter application with fewer than 3,000 potential members may be economically unadvisable.

Liquidity Risks – In many countries credit unions do not have access to a liquidity facility or the lender of last resort facility at the central bank. Because of this credit unions are subject to severe liquidity risks. To confront liquidity risks many credit unions have developed centralized liquidity pools. These pools are adequate to meet demands posed by seasonal liquidity needs in individual credit unions. They are not adequate to meet liquidity risk on a larger scale. Regulations should establish minimum liquidity ratios for individual credit unions. Within the PEARLS monitoring system (see Annex 2) liquid investments and liquidity reserves are measured against savings and time deposits to ensure adequate institutional liquidity for satisfying all deposit withdrawal requests. The liquidity ratio (liquid assets – accounts payable less than 30 days / savings deposits) goal is a minimum of 15%.

Fixed Assets – The total value of fixed assets should be restricted so that credit union funds are invested in productive rather than non-productive assets. In Bolivia investment in fixed assets is limited to no more than net capital. In the U.S, fixed assets are limited to no more than 5% of savings and retained earnings, unless a waiver is obtained from the regulator. The PEARLS ratio goal for Non-earning Assets / Total Assets (this includes not only fixed assets, but cash, checking accounts and other assets that do not directly generate income) is less than or equal to 5%. For small or newly chartered credit unions, there will have to be some exceptions to this rule because total assets are limited; and the purchase of information systems, office space or other assets might be a necessity. These exceptions should be granted on a case by case basis by the regulator.

Insider Lending – Regulations should prohibit loans to all officials while they are in office and their family members. Bolivian regulation has done just that; it also goes one step further and states that executives may not have loans at the credit union they manage.

Portfolio Diversification – Prudential regulations should address the diversification of risk within the loan portfolio by limiting the concentration of loans granted to individuals and groups of related individuals. In the U.S., no loan may be granted to an individual if the aggregate amount of their debt exceeds 10% of total savings and retained earnings. In Bolivia, loans to a borrower or a related group may not exceed 3% of net capital and only 1% of net capital if the loan is collateralized only by a personal guarantee.

External Debt – The amount of external debt should be strictly limited. External debt reduces the presence of net savers in an institution; this negatively impacts the governance of a credit union. The use of external debt throughout Latin America in the 1980s to fund targeted credit programs negatively impacted the credit union missions and objectives and harmed their financial position.

The PEARLS goal ratio for External Credit / Total Assets is 0%. Bolivia has developed maximums based on the source of the credit. Credit with other financial entities is limited to no more than net capital and credit with a government entity is limited to 33% of assets. Others believe that external credit should be limited to 10-15% of assets as long as there is a specific plan for the use of the credit that fits within the credit union's business plan.

Investment Activities – Credit unions are chartered to meet member savings and credit needs; because of this the type of permissible investments outside of member loans should be highly regulated. In the U.S., regulation states: the types of investments that a credit union may and may not invest in, the board of director investment responsibilities, the general practices and procedures that must be followed in conducting transactions, how the risk is to be monitored for investments made and how investments are to be valued periodically.

Standardized Accounting –Credit unions should be required to use standardized accepted accounting procedures. Full and fair disclosure of the balance sheet should also be required so that assets are not over or understated. Without standardized accounting it is impossible for a regulator to determine the financial safety and soundness of an institution or compare the financial performance amongst credit unions.

External Audits – Annual audit performed by an independent third party should be mandatory for all credit unions. There are several options for the selection of an individual or organization to perform the annual financial audit. Credit unions, through their supervisory committees may:

- choose any auditor, preferably one who is affiliated with the national professional auditing association,
- choose only those auditors that are authorized by the superintendency and/or by the cooperative development institute (this is the case in Bolivia), or
- accept the auditing services of the organization to which supervision has been delegated (this could be less than independent and may present a conflict of interest).

In the U.S. the supervisory committee may perform the annual audit. This is permissible for small credit unions with cost constraints. However, this is not a preferred method because committee members rarely have the expertise or related experience needed to perform an acceptable audit.

Regulation should also allow the superintendency to request that an audit be performed again if it is found to be substandard.

Governance Issues – As previously stated the structure of credit union governance has inherent weaknesses. In Bolivia there are now regulations that define the principal functions of the board of directors and the supervisory committee as well as for the general manager and the internal auditor. Board of director terms are limited to 3 years. They may be reelected for one additional 3 year term after which they may not be elected to the board for one term or 3 years. Directors are not allowed to have any delinquent loans in the financial system and they may not be members of other credit unions. The regulations also define the functions and authority of the supervisory committee, as the internal controller of the credit union, with oversight over all credit union operations including those of the board of directors and management as well as the liability of the supervisory committee members. Bolivia regulations mandate that credit unions have an internal auditor and that the auditors should be free to carry out their work fully and without restrictions.

Other countries such as Mexico and the U.S. have addressed the duties and responsibilities of the board and committee members in the Law. Mexican Law also addresses the obligations of the general manager.

Meeting Requirements of the New Regulatory Framework

Non-regulated institutions can not be expected to comply immediately with all aspects of the Law, bylaws and rules and regulations. There must be a realistic period of transition for the institutions that will be regulated to allow for changes in operations, financial structure, procedures, policies, accounting, etc.

In Mexico, credit unions have been given a period of 2 years from the enactment of the Law to solicit the CNBV for the authorization to operate as a financial intermediary. If credit unions cannot meet the 2 year deadline then they will be unable to mobilize savings deposits from members.

Bolivia also established a transition period so that credit unions can meet the standards required to obtain an operating license. This period was established to ensure that the Supreme Decree 24439 was not an insurmountable obstacle to the continuing operations of credit unions involved in financial intermediation. "The process of bringing credit unions into line with the regulatory framework so they can engage in financial intermediation has four stages. The first stage gives instructions to the credit unions to decide whether to operate as open or closed credit unions. The second stage involves the receipt and evaluation of requests and the formation of priority groups. The third stage entails monitoring and inspection. The fourth stage is the granting of an operating license."[6]

Types of Supervision

Supervision is the on-going monitoring of the financial and operational condition of credit unions both on-site at the institution and off-site. It is important to remember that the most carefully crafted regulations will be useless if they can not be enforced with effective supervision and even the best supervision can never replace good daily management and sound internal controls.

There are four different types of supervision currently being used successfully in the United States and Latin America: direct, hybrid, auxiliary and a private rating agency.

Direct Supervision

Direct supervision is when the superintendency performs both the off and on-site supervision of all credit unions with their own staff and they have all sanctioning powers. U.S. credit unions are under direct supervision; they are supervised by an agency, the National Credit Union Administration (NCUA) that is solely dedicated to credit union chartering and supervision. NCUA also administers the National Credit Union Share Insurance Fund (NCUSIF) that insures credit union member deposits up to $100,000. Promotion of credit unions is left to the national and statewide trade associations.

NCUA examiners are highly skilled and possess specialized knowledge and training that allows them to understand operational issues and problems that are routinely encountered by these institutions. On an annual basis, examiners are assigned a group or district of credit unions. They are responsible for both off and on-site monitoring of these institutions throughout the fiscal year. Any problems are addressed immediately with credit union management and the supervisory examiner. From time to time specialized examiners are used to solve problems and/or the problems are addressed on the regional level (in one of the 5 regional offices) if they can not be solved at the local level.

Direct supervision is probably the most effective model because all credit unions are supervised, there are no conflicts of interest between the regulator and the credit unions and supervision is performed by individuals who have been trained in credit union operations. The main drawback of direct supervision is the cost.

DIRECT SUPERVISION
Credit Union Regulation and Supervision in the United States

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[6] Safe Money, Glenn D. Westley and Brain Branch, Editors. Washington D.C.: The John Hopkins University Press, 2000.

Federally chartered credit unions in the United States are supervised by the National Credit Union Administration (NCUA), a government agency. State chartered credit unions are supervised at the state level. NCUA can take part in the on and off-site supervision of state chartered credit unions at their discretion, due to the fact that the agency is responsible for the safety and soundness of the deposit insurance fund that insures member deposits in both federal and state chartered credit unions.

Changes in the regulatory environment have been dramatic and numerous since the Federal Credit Union Act was signed in 1934, which authorized the establishment of federally chartered credit unions in all states. In the congressional debate concerning the Federal Credit Union Act neither the Comptroller of the Currency nor the Federal Reserve Board wanted to oversee federal credit unions. Eventually the Farm Credit Administration agreed to take the responsibility. Regulatory responsibility shifted over the years to include bureaus within the Federal Deposit Insurance Corporation, the Federal Security Agency and the Department of Health, Education and Welfare.

In 1970, NCUA was created to charter and supervise federal credit unions and the National Credit Union Share Insurance Fund (NCUSIF) was organized to insure credit union deposits and was capitalized solely by credit unions. In 1979, Congress created the Central Liquidity Facility, the credit union lender of last resort. In the early 1980s, the effect of high interest rates and unemployment had a devastating effect on the NCUSIF. With the NCUSIF near bankruptcy congress approved a plan to recapitalize the NCUSIF by depositing 1 percent of credit union shares into the Fund. Backed by the "full faith and credit of the United States Government" the NCUSIF now has 3 fail safe features: credit unions must maintain a 1 percent deposit in the NCUSIF, premiums may be levied if necessary, and when the equity ratio exceeds 1.3 percent ($1.30 on deposit for every $100 insured) a dividend is to be distributed to credit unions.

As of 2002 there are 6,566 federally chartered and 4,062 state chartered credit unions. All of these institutions are directly supervised by a state or federal agency or both. Each institution undergoes an annual examination performed by the respective supervisory body. Upon completion of the examination the credit union receives a CAMEL rating (See Annex 1) and a written report outlining the problems and resolutions, the individual responsible for resolving the problem and the time frame in which the problem is to be resolved. The CAMEL rating is used by the supervisory body to assess the risk the credit union poses to the NCUSIF and to prioritize institutions needing additional examiner attention. If the credit union has problems demanding additional assistance, an examiner can visit several times throughout the year to follow up on the resolution of all problems. In order to provide effective, results-oriented supervision NCUA also uses specialized examiners in addition to regular examination staff to work with credit unions:

- that have problems that could negatively effect the NCUSIF,
- that serve low-income areas,
- that have difficult or higher risk investments, and
- in the area of information technology.

In addition to on-site supervision, credit unions are required to submit semi-annual or quarterly (dictated by asset size) financial information to the supervising agency. This financial information is collected and analyzed by the examiners to identify problems that could pose a risk to the credit union and the overall system. Examiners are encouraged to communicate regularly with their assigned credit unions, so that potential problems do not go undetected.

Should credit union management either be unwilling or unable to correct problems, NCUA as the supervisory body has authority to:

- remove management or officials,
- merge, conserve or liquidate a credit union,
- issue prohibitions against employees or officials for further involvement with any credit unions,
- discontinue the insurance of member shares, and
- revoke the credit union charter.

In order to effectively supervise the federally chartered credit unions and those state credit unions that pose at risk to the NCUSIF, NCUA has approximately 1000 employees, of which 800 are examiners. The cost of supervision is paid by the credit unions and the NCUSIF. In 2002, as in the past federally chartered credit unions were assessed an annual operating fee based on their asset size. The fee base was as follows:

Total Assets		
Over	But not more than	Assessment Rate
$0	$500,000	$0
$500,000	$750,000	$100
$750,000	$560,530,205	.00023340 * total assets
$560,530,205	$1,696,155,982	$130,828.39 + .00006802 * total assets > $560,530,205

For example - A credit union with $5 million in assets pays $1,167 per year for supervision and a $50 million credit union pays $11,670.

In order to determine the amount that the NCUSIF pays, a study is performed to ascertain the percentage of examiner time that is spent on insurance related issues. In 2002, it was 62 percent; therefore the NCUSIF funded 62% of NCUA's budget.

Hybrid Supervision

Hybrid supervision is a derivation of direct supervision. Hybrid supervision occurs when the superintendency regulates just those institutions that meet certain requirements such as capital adequacy minimums as is the case in Bolivia. Under this scenario the off and on-site supervision of the institutions that meet the established criteria is performed by the employees of the Superintendency. The supervision of those institutions that do not meet the requirements is performed by a cooperative development agency. There is widespread agreement that cooperative agencies are unable to supply adequate supervision because of limited budgets and the lack of employees that possess the technical skills needed to regulate and supervise a financial institution.

Hybrid supervision is used to reduce the cost of supervision and to limit the use of superintendency employees to the largest institutions. The main drawback to this supervision model is that not all credit unions receive adequate supervision. All credit unions should be supervised because "selective supervision is likely to place many institutions–particularly small, rural institutions-at risk because of a competitive disadvantage. All else being equal, depositors will seek out supervised institutions over unsupervised ones."[7] Additionally, all depositors should be entitled to the same level of safety with regards to their deposits in financial institutions and should an institution be operated ineffectively or fraudulently all depositors should be assured that the supervisory authority will step in to protect deposits and confidence in the credit union system.

HYBRID SUPERVISION
Credit Union Regulation and Supervision in Bolivia

On December 13, 1996, the Supreme Decree 24439 was approved which dictates the formation and operation of credit unions. This decree makes a distinction between two types of credit unions: open and closed. Open credit unions are those institutions that make loans to their members and mobilize savings both from the members and public. The Superintendency of Banks and Financial Entities (SBEF) is responsible for monitoring, supervising and sanctioning the open credit unions. Within the SBEF, the Department of Supervision of Non-Bank Entities is directly responsible for the off-site and on-site supervision of the open credit unions. Closed credit unions are those institutions that do not take deposits, they offer only share accounts and they lend exclusively to their members. Closed credit unions are governed by the National Institute of Cooperatives (INALCO), an agency that regulates the activities of non-financial cooperatives.

In order for a credit union to be designated as an open credit union, the SBEF issues the required operating license. The credit union must meet licensing requirements in the areas of: operational self-sufficiency, solvency and capital adequacy. As stated previously, four minimum capital requirements were established for open credit unions:

- Category 1 – 150,000 special drawing rights / Ratio of net worth to risk-weighted assets of at least 20%,
- Category 2 – 250,000 special drawing rights / Ratio of net worth to risk-weighted assets of at least 15%,
- Category 3 – 630,000 special drawing rights / Ratio of net worth to risk-weighted assets of at least 10%, and
- Category 4 – 5,500,000 special drawing rights / Same as category 3.

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[7] Safe Money, Glenn D. Westley and Brain Branch, Editors. Washington D.C.: The John Hopkins University Press, 2000.

Categories 1 and 2 are authorized to engage in basic financial intermediation, primarily mobilizing deposits and making loans, category 3 may also issue and place debt instruments, obtain loans from financial entities abroad and the Central Bank of Bolivia and category 4 is authorized to engage in most operations that banks do. In addition to these requirements, personal documentation must be submitted for the members of the board of directors, the supervisory committee and the management of the credit union in order to ascertain each individual's professional background and suitability for their position.

As of mid 2002, there were 76 closed credit unions, 23 open credit unions and 8 in the process of applying for the license to operate as an open credit union. The supervision of the open credit unions is focused on determining and meditating inherent risk. Supervision is separated into off-site and on-site supervision. Off-site supervision is performed by a group of 10 examiners (they also perform this task for other non-bank entities). Each examiner is responsible for 5 institutions. Off-site supervision is centered around the following:

- A review of the "Central de Informacion de Riesgo" (CIRC) is conducted for credit union's that demonstrate above average risk in operational areas such as the types of credit offered. CIRC information is updated monthly.
- A review of the "Sistema de Informacion Financiera" (SIF) is performed that monitors the legal reserving and capital adequacy requirements. This information is updated daily.
- A review of the PEARLS ratios (See Annex 2) and the overall financial situation of the credits unions is performed monthly. Quarterly reports are prepared that discuss the financial situation, compare the credit unions with their peers, address compliance or non-compliance with existing laws and norms, and include comments and observations from follow-up visits performed. Written correspondence with credit unions is generated from this quarterly process addressing negative trends and emerging or existing problems.

Based on the off-site review, the supervisor who is responsible for the on-site examination can prioritize and plan on-site visits of their assigned credit unions. On-site examinations are performed every 2 years. Follow-up visits are made for one or two days to credit unions that were not examined during the year.

During the on-site examination, off-site examiners participate at the beginning and end of the examination. Their input is important in the beginning because they are familiar with the credit union and at the termination of the exam because they will be responsible for the follow-up on observations made and compliance with the Plan of Action. The on-site visit concentrates on the review of credit union governance, administration, policies, the loan portfolio, accounting, internal controls and daily operations. A team of examiners will perform the examination. The number of examiners and the length of the examination will depend on the asset size and financial sophistication of the credit union. Upon completion of the examination, the supervisor in charge prepares a report detailing the principal findings, problems, and recommendations for correcting the problems. These recommendations are documented in a "Plan of Action" along with the individual responsible for making the correction and the time frame. All of the findings and recommendations are discussed with the employees and officials and are included in the written report sent to the credit union upon examination completion. Based on the severity of the problems, follow-up or additional on-site visits may be scheduled to review the progress or lack thereof in complying with the "Plan of Action" developed during the initial contact.

Semi-annually, the supervised credit unions pay an amount equal to 1*1000 divided by average assets. This amount was set forth in the Law.

Auxiliary Supervision

The auxiliary supervision model maintains all sanctioning authority at the superintendency level while the off and on-site supervision is performed by a third party. Typically this is a second tier institution, such as a national credit union federation. Upon completion of all off and on-site reports, the information is forwarded to the superintendency. The superintendency reviews all reports and financial information to ensure the safety and soundness of the institutions. A representative of the superintendency will discuss operational problems and solutions both with the 3rd party providing the supervision and in some instances with credit union representatives.

A clear advantage to the auxiliary model is that all credit unions are supervised and it does not require the superintendency to hire and train additional employees. However this model suffers from a severe conflict of interest. The national credit union federation is being asked to play two conflicting roles, that of promoter and of regulator. Because the federations are owned by credit unions and credit union managers are on the boards and committees, the federation may be hesitant to address serious problems and, if necessary, close participating credit unions. The federation or 3rd party may also be hesitant to alert the superintendency to problems because these institutions own and direct the affairs of the federation.

It has been argued that the creation of a stabilization fund can greatly reduce the federation's conflict of interest problem. "The purpose of the fund is to protect the depositors of the affiliated institutions. Typically, the credit union federation establishes the fund and manages its resources. By regularly contributing capital to the stabilization fund, all credit unions take on the responsibility for any one credit union's losses. This mechanism provides a major incentive for all credit unions to keep supervision strong and independent."[8]

AUXILIARY SUPERVISION
Credit Union Regulation and Supervision in Mexico

As of June 4, 2001 the "Ley de Ahorro y Credito Popular" became effective. This Law allows the government agency, "Comision Nacional Bancaria y De Valores" (CNBV), that is charged with regulation of financial institutions to delegate regular monitoring

[8] IBID, page 196.

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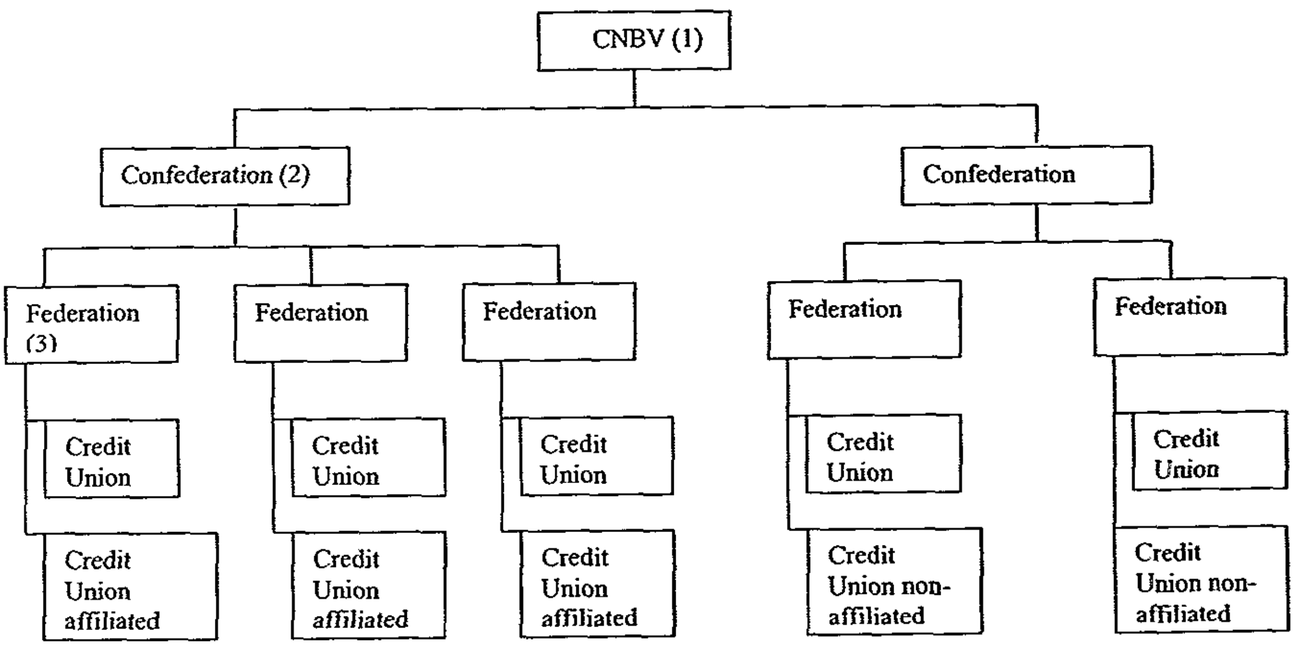
and on-site inspection to a third party while maintaining the legal authority, responsibility and right to sanction the entities supervised by the 3rd party.

CNBV has two years from the enactment of the law to draft prudential regulations, authorize the federations to perform the auxiliary supervision, improve credit union operations so that they are in compliance with the Law and improve the professionalism of credit union management and officials through training. The Law has four main objectives:

- to regulate, promote and facilitate credit union operations,
- to improve the financial soundness of these institutions,
- to organize federations and confederations and focus their daily operations on the protection of the overall system and the financial interests of depositors at the individual credit unions, and
- to establish the terms by which the financial authorities will regulate and supervise the credit unions.

The regulatory structure is four tiered and is organized as illustrated below:



(1) CNBV is responsible for the supervision of commercial banks, development banks, brokerage houses and nonbank financial intermediaries, which includes credit unions. CNBV will provide the minimum prudential regulation that will govern the credit unions and the minimum corrective measures with which the credit unions must comply. The credit unions, federations and confederations will provide CNBV with all information they request to fulfill their supervision role. CNBV can remove officials, management and employees of the federations and confederations with due cause and can assess penalties.

(2) Confederations are voluntary groups formed by at least 5 federations. Confederations will be responsible for the performance and administration of the "Fondo de Proteccion" and supervision of the federations with regards to the distinct services provided through auxiliary supervision. Confederations will also communicate with the federal government in order to design and execute programs that will facilitate credit union activity.

The ultimate body of authority of a confederation is the general assembly. Members of the general assembly will be representatives from the affiliated federations. The board of directors will be elected by the general assembly. Internal control oversight will be the responsibility of the supervisory committee. CNBV retains the right to veto the election or appointment of the board and committee members and the general manager.

(3) Federations are voluntary groups formed by at least 10 credit unions that are authorized by CNBV to perform auxiliary supervision. CNBV will directly supervise the federations. The federation's supervisory responsibilities will be to: review, verify and evaluate the assets, liabilities and equity, along with the daily operations, internal controls and overall financial position of the credit unions. The federations will rely on a "Comite de Supervision" that will be actually in charge of the auxiliary supervision of the affiliated and unaffiliated credit unions. The committee members are designated by the board of directors of the federation. The members of this committee may only be removed from their position upon approval of CNBV.

The ultimate authority of the federations is the general assembly. The assembly members will be elected by the affiliated credit unions. The board of directors will be elected by the general assembly. The supervisory committee is in charge of the overall internal control of the federation. The members are elected by the board of directors and approved by the general assembly. CNBV retains the right to veto the election or appointment of the board and committee members and the general manager.

The "Comite de Supervision" may take corrective measures against a credit union and may remove officials and/or management upon informing the "Comite Tecnico" of the "Fondo de Proteccion". "El Comite Tecnico" is responsible for merger, dissolution, liquidation or sale of a credit union. The "Comite Tecnico" will decide which of the measures to take based on the impact to the "Fondo de Proteccion".

(4) Affiliated Credit Unions are those credit unions that have a formal contract of affiliation with a federation stipulating the terms and conditions of the auxiliary supervision. Affiliated credit unions are represented in the federation's general assembly.

(5) Non-affiliated Credit Unions are those credit unions that do not have a formal contract of affiliation with a federation and are not represented in the general

assembly. The CNBV will assign these credit unions to a federation that will provide supervision. There will be a contract between the federation and the non-affiliated institution. The non-affiliated entity will have all the obligations of an affiliated entity with regards to auxiliary supervision, including the cost of the supervision.

Non-affiliated entities may request to participate in the "Fondo de Proteccion" of a confederation or, with the approval of CNBV may establish their own "Fondo de Proteccion", but it may not offer lesser benefits to the depositors than what is addressed in the Law.

Auxiliary supervision will be separated into off-site and on-site supervision. Off-site supervision will consist of financial analysis and follow-up; while on-site supervision will consist of planning and the actual on-site visit. On-site examinations are broken down into three types, integral, specific or special. Integral exams are full-scope examinations and will be performed biennially. Specific examinations will be performed bi-annually and the scopes are limited to particular points or areas that require additional review. Special inspections are outside of the normal supervision scope and are conducted as needed to review and analyze an emerging problem or situation.

The principal objectives and responsibilities of off-site supervision will be to: verify compliance with established rules and regulations, examine individual credit union performance, evaluate the financial conditions and risks, follow-up on observations and detect emerging problems. In order to determine the financial condition of a credit union and detect adverse trends, analysts will use 11 principal and 24 complementary ratios. They will also look at growth rates and compare similar credit union's financial results and ratios. Monthly analysts will generate reports addressing: general credit union information, the financial statements, financial structure and trends, and conclusions and recommendations. Quarterly reporting is more comprehensive and will include: a diagnostic of the financial situation, determination of credit union compliance with established rules and regulations, financial comparison amongst similar entities, monitoring of any previous observations made or corrective actions taken, and follow-up on any sanctions made and/or penalties assessed.

The principal objectives of on-site supervision will be to: verify compliance with prudential norms, ascertain the adequacy of the internal control environment, examine the internal processes within each credit union and perform an in-depth analysis of relevant information discovered through off-site supervision. Upon the conclusion of the on-site visit and within 20 business days a written report will be issued discussing the objectives of the on-site visit, the areas reviewed and the conclusions made. Also within this time period, an oral presentation of the information will be given to the board of directors and manager of the credit union, and to a representative of CNBV. In addition, on a quarterly basis the "Comite de Supervision" will report the results of inspections made and pending to the board of directors of the respective federation.

The CNBV is funded entirely by the government and the credit unions will provide the funding for the federations. Each credit union will be assessed an annual fee of .0008 of their total liabilities. The federations will fund the confederations.

Private Rating Agency

A private rating agency is another supervision alternative; however it is an alternative only when the government fails to provide adequate supervision and financial institutions are left with no other alternative. This failure is due in part or completely to the lack of: interest on the part of the government, an adequately trained and staffed regulatory agency, an adequate government budget for regulation and supervision and/or adequate laws that address credit union operations.

The private rating agency performs all off and on-site supervision. It has no power to sanction institutions. Since the rating agency is formed by the credit unions, the officials and management should be independent. In other words, to avoid a conflict of interest they should not be a part of daily management and decision making. The rating agency can increase institution creditability and consumer confidence through advertising and public education as to the advantages of a rated institution. The most obvious disadvantages of a private rating agency are that:

- participation in the rating agency is voluntary, should an institution have problems and not want the issues addressed it may simply withdraw from the agency,
- the agency has no power to sanction any of the participating credit unions, and
- it can be difficult to educate the public to the advantages of a rated or certified credit union over a credit union with no certification due to low levels of public financial education and high levels of illiteracy.

PRIVATE SUPERVISION
Credit Union Regulation and Supervision in Guatemala

In 1978 the General Law of Cooperatives was passed. This Law created a National Institute of Cooperatives and the General Inspection of Cooperatives that was given the task of monitoring credit unions. The Law governs all types of credit unions, not just financial cooperatives and is very generic; the Law contains no established norms for each type of cooperative. Because of the state's failure to adequately regulate and supervise credit unions and the high cost of attracting member deposits (due to low public confidence), 22 credit unions have chosen to contract with a private rating agency, that was established by international organizations, to evaluate, rate and certify the financial health and administration of the participating institutions. These 22 credit unions represent 91% of the assets within the credit union system. The objectives of the agency are to improve public confidence and to provide independent external control over the financial soundness of the participating entities.

In order to form this agency it had to be:

- an authorized, legal institution,
- staffed by technical and professionally capable individuals,

- financially self-sustainable, and
- politically independent.

The government agency in charge of monitoring credit unions has not delegated any authority to the rating agency. The credit unions do not control the rating agency. It is a private agency originated out of necessity. The board of directors of the agency is made up of 7 individuals with experience in the areas of international credit union regulation, bank supervision, external auditing and law.

There is a three party contract of rating and certification between the credit union, the rating agency and FENCOAC (the credit union federation). Credit unions had to meet certain conditions in order to participate in the rating and certification process of the agency. The credit unions had to be financially viable and following established prudential norms. They had to use standardized accounting nomenclature and financial forms along with the PEARLS monitoring system (See Annex 2). Lastly, in addition to the visits performed by the rating agency, credit unions also had to submit to an annual external audit performed by an independent source.

In assigning a rating and certification the agency performs:

- a review of the compliance with prudential norms,
- an off-site risk diagnostic, and
- an on-site verification along with a PEARLS analysis (See Annex 2).

Currently there are 5 employees or analysts performing the financial review and risk diagnosis. Per the contract between the credit unions and the rating agency, the credit unions are obligated to send their financial statements to the agency monthly. Using PEARLS (See Annex 2) the analysts perform a thorough off-site financial trend analysis. This analysis helps to orient the agency towards the areas and institutions of greatest risk. Annually, two on-site visits are made to follow-up on the high-risk areas identified during the off-site PEARLS analysis, to verify the quality of the institution's assets and to perform a complete risk diagnosis of all operational areas.

From these off and on-site reviews a draft report is generated that is discussed with credit union management and officials. Upon acceptance of the draft report, a final report is written and certification granted. The report is presented to the credit union officials, management and representatives of FENCOAC. Based on the results of the report, a Plan of Action is drafted by FENCOAC and credit union officials and management to resolve the identified problems. FENCOAC provides on-going technical assistance to assist the credit unions in problem resolution. The rating agency will verify credit union compliance with the established Plan of Action.

The principal sanction for non-compliance is the revocation of the certification plaque previously awarded to the credit union. This revocation is damaging to the credit union due to a large advertising campaign that focused on building public recognition of the plaque representing the certification.

Since the inception of the rating agency the participating credit unions have paid 100% of the local operating expenses of the agency. Expenses associated with international technical assistance, publicity to launch the rating agency and on-going marketing emphasizing the meaning and importance of the certification process are currently being paid by the World Bank. The World Bank will continue to pay these expenses until 2004.

What is Quality Supervision?

The purpose of supervision is to ensure the long-term viability of credit unions by addressing and resolving problems in a timely manner. Supervision is the on-going monitoring of a credit union's compliance with established regulations along with their financial position. In order for supervision to be effective, it must be constant and consistent in nature. This is the key to prompt problem resolution and a viable credit union movement.

No matter what supervision model is chosen, supervision should include both off-site and on-site components. Off and on-site supervision may be performed by the same examiner or it may be performed by 2 distinct examiners. There are numerous views with regards to which style is more effective. If there is only one examiner performing both functions, they may overlook something in performing the off-site analysis. The "two sets of eyes" approach is missing. However if off and on-site supervision are performed by two individuals, channels of communication must be open and the dissemination of information timely so that emerging problems and/or negative trends are addressed immediately.

Both off and on-site reviews should be standardized so that each credit union is reviewed and analyzed taking into consideration the same information. Written procedures, policies and workpapers are needed to standardize the process.

Quality off-site supervision is composed of the following:

- examiners specifically trained in credit union operations and regulations,
- assignment of a group of credit union's to an examiner that are distributed amongst examiners taking into consideration their size and complexity,
- examiner responsibility for the complete off-site analysis of their assigned credit unions,
- collection of reliable information and data in a standardized format,
- sufficient resources that allow for the timely collection and timely analysis of data,
- monthly or quarterly (depending on size, complexity and existing credit union problems) written analysis of financial statements, trends, ratios and any other key indicators that focus on identifying risk, and
- review of periodic information submitted by credit unions such as a call report that requests additional financial and operational information not reviewed on a more frequent basis.

In reviewing information submitted by a credit union, the examiner should take note if:

- The reports were received on time. Reports received consistently after an established deadline could be an indication of more serious operational problems at the credit union.
- The same individual completes the report or it is someone different each time. Does there appear to be excessive turnover in the accounting and financial departments?
- The report was completed correctly.
- There were any material changes in the information submitted as compared to the information submitted in prior reports. This is best done by performing a trend analysis of information received from one period to the next.
- There are any negative trends or emerging problems. When negative trends or emerging problems are apparent, an examiner must communicate immediately with their superior and credit union management to establish a plan to resolve the problem as quickly as possible.

In addition to reviewing information received, off-site supervision includes communication between the superintendency and the regulated institutions. Good communication only improves the effectiveness of supervision. Regular discussions between the examiners and their supervisor concerning negative trends and identified problems should take place to improve problem solving and diminish the possibility of unpleasant surprises. Examiners should also be free to contact credit unions as often as necessary by phone, fax, mail, or whatever form best suits the environment.

Off-site supervision should help to identify and prioritize those credit unions with problems or that pose more risk to the integrity of the credit union system. On-site contacts can be scheduled taking into consideration information revealed by off-site analysis.

On-site supervision is defined as periodic visits to credit unions to evaluate their financial soundness, appraise the quality of management, identify problems and develop plans to resolve them, and determine the degree of risk that the credit union poses to the integrity of the overall system. On-site visits can be broken down into 2 types, the full examination and the follow-up or special visits.

Each supervised credit union, depending on the systemic risk it poses and the resources available, should receive a full examination no less than every 2 years. If adequate resources exist then the full examination should be performed annually. Follow-up or special visits should be used to monitor the resolution of problems and discuss negative trends identified during the most recent annual exam or off-site analysis. Follow up visits will vary in time depending on the problems, asset size and complexity of the institution. They usually range from one to five days.

Annual exams and/or follow-up visits can be performed with advance notice or on a surprise basis. However, because of the planning involved both by the superintendency and the credit union surprise contacts should only be used when there is a suspicion of fraud, illegal actions or unsound practices. Two to three weeks prior to the commencement of the examination, the examiner should contact management in writing with the effective date of the exam, the number of examiners that will be present and to request the general information needed to perform the exam. One week prior to the full exam, the examiner should contact the general manager by phone (if possible) to answer any questions, make sure that all key employees will be present and that there is adequate room for the examination team.

At the beginning of each examination year the supervisory examiner should divide the credit unions among the examiners taking into consideration the size, complexity and the geographic location. The examiners should be responsible for the supervision of these institutions throughout the year. Credit unions should be rotated amongst the examiners so that no examiner has the same credit union more than three consecutive years. If the exam requires more than 1 examiner then the supervisory examiner should assist the examiners with the scheduling. When examiners are prioritizing and scheduling exams, they should consider the following:

- financial condition and trends,
- quality of officials, management and employee turnover,
- potential risk posed to the integrity of the overall credit union system, and
- date of the last examination.

In performing the on-site examination, the examiner should have as a primary objective the identification and documentation of problems, the design of actions to resolve identified problems and the agreement of officials and daily management as to the most effective way to solve the problems in a timely manner. Thus, at a minimum, the examiner should:

- determine that officials and management have established and implemented adequate policies and procedures of all major operational areas,
- ascertain that the books and records are properly maintained (current and in balance) and accurately reflect the operations of the credit union,
- ensure that officials and management are complying with applicable regulations and agreements (from previous exams or contacts) and that the credit union is operating in a safe and sound manner,
- determine that the officials and management are trained and able to meet all of their duties and responsibilities,
- establish open communication with management so they are aware of examination progress and findings,
- develop reasonable plans for corrective action with credit union management and present these plans to the officials, and
- follow up with management as needed to ensure problems are corrected timely.

More specifically during the full examination, examiners should:

- perform a review of the general ledger – verifying the financial statement balances are equal to the general ledger balances and that each general ledger account is supported by a subsidiary ledger with the same balance,
- determine that the value of the assets are fully and fairly stated and that income and expense accounts are correct and that all necessary documentation is present,

- review the adequacy of credit union profitability including material expenses to ensure that they are authorized and properly documented,
- review the adequacy of the capital accounts and the appropriateness of entries in the capital accounts,
- review a random sample of loans to ensure that they are within credit union policy, are adequately documented and borrowers have the ability to repay the loan,
- determine that delinquency is properly stated and recorded,
- review the collection program and use of loan extensions and charge offs,
- ensure that loans are charged off in a timely fashion and with the proper approval,
- review all written policies and procedures for key operating areas,
- review board and committee minutes,
- review the internal and external audits, noting the adequacy of both,
- determine the presence and effectiveness of internal control with respect to protecting credit union assets and the value of member deposits,
- review the annual operating budget and the business plan, if available
- determine that all reports requested by the superintendency are submitted correct and on time,
- assess the liquidity needs with respect to loan demand, share withdrawal and operating expenses, and
- review and assess interest rate risk with regards to the structure of savings, deposits and shares.

All of these areas of review should be adequately documented. The workpapers used for the review should be maintained in the credit union file. From these reviews an examination overview should be generated discussing all the areas reviewed and the problems detected. A plan of action should be developed that specifically details: the steps needed to solve the problems identified, the time frames and the person(s) responsible for the correction of the problem. This plan should be developed with the assistance of management and presented to the board for adoption upon the termination of the exam. Adoption of the plan by the board states that they will ensure that the individual charged with solving the problem does so in the allotted time frame. Lastly a rating (CAMEL, PEARLS, etc. See Annexes 1 and 2) should be assigned that will be used to assess the risk the credit union poses to the overall system and the insurance fund, if applicable. The rating can be disclosed to management or it can be an internal tool used by the regulator. Upon termination of the exam, a formal written report including the examination overview, plan of action, examiner findings (immaterial problems, errors and/or non-compliance with policies, procedures, regulations, etc), overall rating (if is not considered confidential) and pertinent workpapers should be delivered to the credit union no later than 2 weeks after the close of the full examination.

Examiners along with their supervisors should determine when follow-up visits are needed. Considerations in scheduling a follow up visit include: the seriousness of the problems, the quality of management, the risk posed by the credit union to the overall system, other examination needs and examiner judgement.

Follow up visits are used to:

- ensure that management is following the plan of action adopted during the full examination and it is still valid,
- develop solutions to new and/or emerging problems,
- detect emerging financial trends that could threaten credit union solvency,
- assess the continued economic viability of the institution, and
- recommend further supervision plans and contact dates.

Follow up contacts should be documented and a report generated discussing what was reviewed and any new problems and/or negative trends detected. If needed a revised plan of action can be drafted and adopted by the officials. To enhance continuity, the examiner that performed the full examination also will conduct the follow-up visit.

If the off and/or on-site supervision do not achieve the desired results, the regulator must have the power to take more definitive or severe actions such as:

- the removal of officials and/or employees,
- prohibitions against certain actions,
- monetary penalties,
- cease and desist orders,
- conservatorship,
- liquidations or mergers, and
- revocation of the license, charter and/or insurance of member deposits

Differences between an Audit and an Examination

Sound regulation should stipulate that a credit union should be subject to a full scope examination and an annual external audit. Many people think that there are few differences between the two, however, the differences are significant. The primary objective of an external audit is determine if the books and records fully and fairly represent the financial condition of the entity. The purpose of an examination is oriented towards the assessment of risk and determination of potential loss to the insurance fund or loss of member deposits. The material differences are:

Criteria	External Audit	Full Scope Examination
Regulator	Professional Accounting Association (such as the AICPA in the U.S.)	Government agency, Superintendency, 3rd party – federation, private rating agency
Authority	Generally accepted accounting and auditing standards	Credit union law, acts of congress, rules and regulations
Professional Education	Public accountant (often they are licensed or chartered)	University degree in finance, business and/or accounting
Reporting Authority	Credit union supervisory committee	Regulatory agency, superintendency, 3rd party – federation, private rating agency and the credit union's board of directors.
Composition of Final Report	Audited financial statement along with a management letter outlining any recommendations	Examination report supported by an examination overview, plan of action, examiner findings and a

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		rating indicating financial safety and soundness (CAMEL, PEARLS, etc.)
Institutional Performance Evaluation	An opinion rendered by the accountant such as clean, qualified, or "with conditions".	A rating indicating financial safety and soundness such as CAMEL or PEARLS.
Powers and Influence	The only power the accountant has is through the rendering of the opinion. The external auditor is paid by the credit union. If management does not like the auditor's opinion then they can hire a different one next year. This situation can pose a conflict of interest for the auditor.	The examiner has considerable power through the regulatory body, except in the case of the private rating agency. Examiners can influence credit union management through the formal written agreements such as the plan of action and stronger administrative actions that may be taken by the regulator.
Costs	Negotiable	Based on assets or a formula established by the regulator.

Conclusion

Credit unions in many developing countries have been operating without formal regulation and supervision for years. Many of these institutions remain small, with little or no influence on their local economic situation. Others have successfully served their member's savings and lending needs and are now influential within their local financial environment. All of these institutions accept deposits from their members. For this reason alone these entities should be regulated and supervised by a government agency or appointed oversight body. Just because credit unions are smaller than banks and have less influence economically is no reason why their member's deposits should be subject to additional risk due to the absence of adequate supervision.

Effective credit union regulation should start with a law that is specific to credit union operations. Standardized bylaws should be mandatory for all individual credit unions. Rules and regulations aimed at improving credit union safety and soundness should be established by a government agency or superintendency. In order to monitor credit union compliance with established law and regulations and to evaluate their financial condition, a supervision program should be in place, similar to that of the banking industry, that includes both off and on-site supervision. Supervision should enforce regulation and be focused on: determining the risk posed by the credit union to the system as a whole, assessing the potential loss to an insurance fund, if applicable, and determining the threat of loss to member shares and deposits. If established regulation can not be enforced through a supervision program, it is virtually useless.

Regulation and supervision should be results oriented and carefully crafted so that it does not stifle innovation or put the regulated or unregulated at a competitive disadvantage. Lastly, may it never be forgotten that the *very best supervision* will never replace good operational management and sound internal controls.

ANNEX 1

CAMEL Rating System Used in the U.S.

The CAMEL rating system is based upon an evaluation of five critical elements of a credit union's operations: Capital Adequacy, Asset Quality, Management, Earnings and Asset/Liability Management. This rating system is designed to take into account and reflect all significant financial and operational factors examiners assess in their evaluation of a credit union's performance. Credit unions are rated using a combination of financial ratios and examiner judgment.

Since the composite CAMEL rating is an indicator of the viability of a credit union, it is important that examiners rate credit unions based on their performance in absolute terms rather than against peer averages or predetermined benchmarks. The examiner must use professional judgment and consider both qualitative and quantitative factors when analyzing a credit union's performance. Since numbers are often lagging indicators of a credit union's condition, the examiner must also conduct a qualitative analysis of current and projected operations when assigning CAMEL ratings.

Although the CAMEL composite rating should normally bear a close relationship to the component ratings, the examiner should not derive the composite rating solely by computing an arithmetic average of the component ratings. Following are general definitions the examiner should use for assigning the credit union's CAMEL composite rating:

Rating 1 - Indicates strong performance and risk management practices that consistently provide for safe and sound operations. The historical trend and projections for key performance measures are consistently positive. Credit unions in this group are resistant to external economic and financial disturbances and capable of withstanding the unexpected actions of business conditions more ably than credit unions with a lower composite rating. These credit unions are in substantial compliance with laws and regulations. Such institutions give no cause for supervisory concern.

Rating 2 - Reflects satisfactory performance and risk management practices that consistently provide for safe and sound operations. Both historical and projected key performance measures should generally be positive with any exceptions being those that do not directly affect safe and sound operations. Credit unions in this group are stable and able to withstand business fluctuations quite well; however, minor areas of weakness may be present which could develop into conditions of greater concern. These credit unions are in substantial compliance with laws and regulations. The supervisory response is limited to the extent that minor adjustments are resolved in the normal course of business and that operations continue to be satisfactory.

Rating 3 - Represents performance that is flawed to some degree and is of supervisory concern. Performance is marginal. Risk management practices may be less than satisfactory relative to the credit union's size, complexity, and risk profile. Both historical and projected key performance measures may generally be flat or negative to the extent that safe and sound operations may be adversely affected. Credit unions in this group are only nominally resistant to the onset of adverse business conditions and could easily deteriorate if concerted action is not effective in correcting certain identifiable areas of weakness. Overall strength and financial capacity is present so as to make failure only a remote probability. These credit unions may be in significant noncompliance with laws and regulations. Such credit unions require more than normal supervisory attention to address deficiencies.

Rating 4 - Refers to poor performance that is of serious supervisory concern. Risk management practices are generally unacceptable relative to the credit union's size, complexity and risk profile. Key performance measures are likely to be negative. Such performance, if left unchecked, would be expected to lead to conditions that could threaten the viability of the credit union. There may be significant noncompliance with laws and regulations. A high potential for failure is present but is not yet imminent or pronounced. Credit unions in this group require close supervisory attention.

Rating 5 - Considered unsatisfactory performance that is critically deficient and in need of immediate remedial attention. Such performance, by itself or in combination with other weaknesses, directly threatens the viability of the credit union. Credit unions in this group have a high probability of failure and will likely require liquidation and the payoff of shareholders, or some other form of emergency assistance, merger, or acquisition.

Key financial ratios are provided for the capital, asset quality, and earnings, with supporting ratios for asset/liability management components to guide examiners in assigning the appropriate ratings. Examiners will rate credit unions based on their performance in absolute terms rather than against national peer averages or predetermined benchmarks. Peer averages or benchmarks do not necessarily reflect credit unions that are being operated in a safe and sound manner. The CAMEL ratings should accurately reflect the condition of the credit union regardless of peer performance.

Key Ratios for Credit Unions with Assets of $2 Million or Less

Category	Code 1	Code 2	Code 3	Code 4	Code 5
1. Capital					
Net Worth /Total Assets	>7%	6%-6.99%	4%-5.99%	2%-3.99%	<2%
2. Asset Quality					
Delinquent Loans / Total Loans	<1.5%	1.5%-3.5%	3.5%-7%	7%-9.5%	>9.5%

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Net Charge Offs / Average Loans	<.25%	.25%-.75%	.75%-1.75%	1.75%-2.5%	>2.5%
3. Earnings					
Return on Average Assets	>1.25%	.9%-1.25%	.4%-.9%	.4%-.2%	<.2%

Key Ratios for Credit Unions with Assets of $2 - $10 Million

Category	Code 1	Code 2	Code 3	Code 4	Code 5
1. Capital					
Net Worth /Total Assets	>7%	6%-6.99%	4%-5.99%	2%-3.99%	<2%
2. Asset Quality					
Delinquent Loans / Total Loans	<1.5%	1.5%-3.5%	3.5%-5%	5%-8.25%	>8.25%
Net Charge Offs / Average Loans	<.25%	.25%-.75%	.75%-1.5%	1.5%-2.5%	>2.5%
3. Earnings					
Return on Average Assets	>1.00%	.8%-1.00%	.35%-.8%	.15%-.35%	<.15%

Key Ratios for Credit Unions with Assets of $10 - $50 Million

Category	Code 1	Code 2	Code 3	Code 4	Code 5
1. Capital					
Net Worth /Total Assets	>7%	6%-6.99%	4%-5.99%	2%-3.99%	<2%
2. Asset Quality					
Delinquent Loans / Total Loans	<1.25%	1.25%-2.5%	2.5%-3.5%	3.5%-5.5%	>5.5%
Net Charge Offs / Average Loans	<.25%	.25%-.75%	.75%-1.5%	1.5%-2.0%	>2.0%
3. Earnings					
Return on Average Assets	>1.00%	.8%-1.00%	.35%-.8%	.2%-.35%	<.2%

Key Ratios for Credit Unions with Assets of $50 Million or More

Category	Code 1	Code 2	Code 3	Code 4	Code 5
1. Capital					
Net Worth /Total Assets	>7%	6%-6.99%	4%-5.99%	2%-3.99%	<2%
2. Asset Quality					
Delinquent Loans / Total Loans	<1.25%	1.25%-2.25%	2.25%-3.25%	3.25%-4.75%	>4.75%
Net Charge Offs / Average Loans	<.25%	.25%-.6%	.6%-1.2%	1.2%-1.8%	>1.8%
3. Earnings					
Return on Average Assets	>1.00%	.8%-1.00%	.35%-.8%	.2%-.35%	<.2%

CAMEL RATIOS (Core and Supporting Ratios)

CAPITAL
* Net Worth/Total Assets
Total Delinquent Loans/Net Worth
Solvency Evaluation
Classified Assets/Net Worth

ASSET QUALITY
*Delinquent Loans/Loans
*Net Charge Offs/Average Loans
Fair (Market) Value/Book Value {for investments held to maturity}
Accumulated Unrealized Gains or (Losses) on Available for Sale Securities/Cost of Investments Available for Sale
Delinquent Loans/Assets

EARNINGS
*Return on Average Assets {new name for Net Income/Average Assets before Reserve Transfers}
Net Operating Expenses/Average Assets
Fixed Asset + OREOs/Assets
Gross Income/Average Assets
Cost of Funds/Average Assets
Net Margin/Average Assets {Gross Income/Average Assets ratio minus Cost of Funds/Average Assets ratio}
Operating Expenses/Average Assets {excludes PLL, PIL, and cost of funds}
PLL Expense/Average Assets
Net Interest Margin/Average Assets {excludes other operating and fee income}
Operating Expenses/Gross Income {excludes PLL, PIL, and cost of funds}

ASSET/LIABILITY MANAGEMENT
Net Long Term Assets/Assets
Regular Shares/Total Shares and Borrowings
Total Loans/Total Shares
Total Loans/Total Assets
Cash + Short-term investments/Assets {short term investments are less than 1 year based on estimated remaining maturity}
Total Shares, Deposits, and Borrowings/Earning Assets
Borrowings/Total Shares and Net Worth
Estimated Loan Maturity in Months {Loan Turnover}

OTHER RATIOS
Market Growth {shares}
Net Worth Growth

Loan Growth
Asset Growth
Investment Growth

*** = Key Ratios**

ANNEX 2

PEARLS Monitoring System

"In response to the need for more accurate and useful financial information, an effort was made to implement the CAMEL system in Guatemala in the late 1980s. After several attempts, it was determined that, although CAMEL was a good tool for supervisors, it did not provide all of the information that managers needed to manage their credit unions. The two greatest deficiencies of CAMEL were that it did not analyze financial structure and it did not look at growth rates of key variables.

The purpose of any monitoring system is to act as an early warning system that alerts board members, managers, accountants, and examiners to potential problems before they arise. The advantage of PEARLS over CAMEL is that it not only indicates potential problem areas, it also indicates the reasons for the problems and implicitly provides recommendations for improvements."[9]

PEARLS is an acronym that stands for Protection, Effective Financial Structure, Asset Quality, Rates of Return and Costs, Liquidity and Signs of Growth.

WOCCU INTERNATIONAL CREDIT UNION PRUDENTIAL STANDARDS OF EXCELLENCE

	P-E-A-R-L-S RATIOS	Goals
P	*PROTECTION*	
1	Loan Loss Allowances / Delinq. >12 Mo.	100%
2	Net Loan Loss Allow. / Allow. Required for Delinq. 1-12 Mo.	35%
3	Complete Loan Charge-Off of Delinquency > 12 Mo.	Yes or No
4	Annual Loan Charge-offs / Average Loan Portfolio	0%
5	Accum. Charge-Offs Recovered / Accum Charge-Offs	100%
6	Solvency	100%
7	Allowance for Investment Losses/ Non-Regulated Investments	100%
E	*EFFECTIVE FINANCIAL STRUCTURE*	
1	Net Loans / Total Assets	Between 70 - 80%
2	Liquid Investments / Total Assets	Maximum 20 %
3	Financial Investments / Total Assets	Maximum 10 %
4	Non-Financial Investments / Total Assets	0%
5	Savings Deposits / Total Assets	Between 70 - 80%
6	External Credit / Total Assets	Maximum 5%
7	Member Share Capital / Total Assets	Maximum 20 %
8	Institutional Capital / Total Assets	Minimum 10%
9	Net Institutional Capital / Total Assets	Minimum 10%
A	*ASSET QUALITY*	
1	Total Delinquency / Gross Loan Portfolio	Less Than or Equal To 5%
2	Non-Earning Assets / Total Assets	Less Than or Equal To 5%
3	Net Zero Cost Funds / Non-earning. Assets	Greater Than or Equal To 100%
R	*RATES OF RETURN AND COSTS (ANNUALIZED)*	

[9] IBID, page 105.

1	Net Loan Income / Average Net Loan Portfolio	Enterprenurial Rate
2	Liquid Inv. Income / Avg. Liquid Investments	Market Rates
3	Fin. Investment Income / Avg. Fin. Investments	Market Rates
4	Non-Fin. Inv. Income / Avg. Non-Fin. Investmnts	Greater Than or Equal to R1
5	Fin Costs: Savings Deposits / Avg. Savings Deposits	Market Rates
6	Fin Costs: External Credit / Avg. External Credit	Less Than or Equal to R5
7	Fin Costs: Member Shares / Avg. Member Shares	Greater Than or Equal to R5
8	Gross Margin / Average Assets	Amount Needed to Cover R9, R10 Increase Capital
9	Operating Expenses / Average Assets	3 -10%
10	Provisions for Risk Assets / Average Assets	Sufficient for Estimated Losses
11	Other Income or Expense / Average Assets	Amount Needed
12	Net Income / Average Assets	Enough to reach the goal for E8
L	***LIQUIDITY***	
1	Liquid Assets - ST Payables / Total Deposits	Minimum 15%
2	Liquidity Reserves / Total Savings Deposits	10%
3	Non-Earning Liquid Assets / Total Assets	Less Than 1 %
S	***SIGNS OF GROWTH (ANNUAL GROWTH RATES)***	
1	Net Loans	Sufficient to Achieve Goal in E1
2	Liquid Investments	Sufficient to Achieve Goal in E2
3	Financial Investments	Sufficient to Achieve Goal in E3
4	Non-Financial Investments	Sufficient to Achieve Goal in E4
5	Savings Deposits	Sufficient to Achieve Goal in E5
6	External Credit	Sufficient to Achieve Goal in E5
7	Member Shares	Sufficient to Achieve Goal in E7
8	Institutional Capital	Sufficient to Achieve Goal in E8
9	Net Institutional Capital	Sufficient to Achieve Goal in E9
10	Membership	Minimum 5%
11	Total Assets	More Than Inflation
	Inflation Rate (Annualized)	

ANNEX 3

ALERTA TEMPRANA

Alerta Temprana is an early warning monitoring system used by credit union managers in Chile. The Chilean federation developed this system; it is an automated mechanism that permits rapid financial evaluation by the user. The objectives of this system are to detect risk, provide a base of information for monitoring financial condition, to facilitate the external audit and on-site examinations and to provide credit union management with a strategic tool.

ALERTA is an acronym that stands for Actividad Financiera (financial activity), Liquidez de Fondos (Liquidity), Estructura Organizacional (Organizational Structure), Rentabilidad Sostenida (Sustained Profitability), Tamano Institucional (Credit Union Size) and Ambito de Operaciones (Operational Environment). This monitoring system has 2 sets of ratios broken out into Razones de Riesgo (Risk Ratios) and Razones de Gestion (Management Ratios).

ALERTA TEMPRANA

Indicadores de Gestión

Grupo/Indicador	Rango óptimo
Gastos	
Costo de Financiamiento	
Tasa Pasiva por Captación	< promedio sector
Tasa Pasiva por Deuda Bancaria	< promedio sector
Tasa Pasiva por Aportes de Capital	< promedio sector
Costo de Fondo Total	> tasa activa colocaciones
Gastos en Personal	
Gastos en Personal v/s Total de Activos	<= promedio sector
Gastos en Personal v/s Ingresos de Operación	<= promedio sector
Gastos de Administración	
Gtos. Adm. v/s Total de Activos	<= promedio sector
Gtos. Adm. v/s Ingresos de Operación	<= promedio sector
Depreciación	
Gto. Provisiones sobre Colocaciones	
Créditos Irrecuperables v/s Total de Activos	<= promedio sector
Créditos Irrecuperables v/s Márgen Bruto	<= promedio sector
Gto. No Operacionales	
Corrección Monetaria v/s Total de Activo	<= promedio sector
Corrección Monetaria v/s Total de Activo	<= promedio sector
Cobertura de Gastos con Márgen Financiero	
Margen Financiero [1]	> 0
Cobertura de Gastos en Personal [2]	> 0
Cobertura de Gastos de Administración [3]	> 0
Cobertura de Depreciaciones y Amortizaciones [4]	> 0
Cobertura de Provisiones Activos Riesgosos [5]	> 0
Cobertura de Gastos No Operacionales [6]	> 0
Cobertura de Corrección Monetaria [7]	> 0
Eficiencia	
Indice de Productividad (Total de Activos)	> promedio sector
Eficiencia en Colocaciones	> promedio sector
Indice de Gtos. en Personal	< promedio sector

Manejo de Socios	> promedio sector
Eficiencia en Captaciones	> promedio sector
Eficiencia en Capital	> promedio sector
Suficiencia	
Crecimiento de Activos	> inflación
Distribución de Remanente a Reservas	> 20%
Tamaño	
Saldo Promedio de Operaciones de Crédito	> promedio sector
Saldo Promedio Depósitos a Plazo	> promedio sector
Saldo Promedio Cuentas de Capital	> promedio sector
Ingresos	
Tasa Activa de Colocaciones	< promedio sector
Rentabilidad sobre Total de Activos	> 0
Rentabilidad sobre el Capital	> 0
Spread de Intermediación	> 0
Organizacional	
Nº de sucursales y puntos de Atención	Informativo
Nº de Funcionarios por Sucursal	Informativo
Gama de Productos de Colocación	Informativo
Innovación de Productos	Informativo
Normativo	
Encaje	Según norma vigente
Endeudamiento	Según norma vigente

Attachment 19

Papers from Supervision Best Practice Web Series

Examination Process – Lending, Collections and Allowance for Loan Loss Review
October 29, 2002

Loans usually represent the largest asset category and the most time consuming part of the examination process. The appraisal of the loan portfolio is a good measure of a credit union's financial soundness, its service to members, and the quality and focus of management.

Objective of Loan Review – The objective of the loan portfolio analysis is to determine:
- The quality of the loan portfolio;
- The risk posed by the loan portfolio to the credit union's capital;
- The collection probability of delinquent loans;
- The quality of the loan policies, procedures, and internal controls governing loan underwriting;
- That credit union employees operate in accordance with board established policy; and
- That management initiates timely corrective action when deficiencies exist.

Scope of Loan Review – A credit union's loan portfolio is usually its primary source of income as well as a major source of risk to its institutional capital. The loan analysis determines the quality and overall risk of the loan portfolio. Examiners must select and review an adequate sample of loans in order to make an informed decision on the quality and risk of the loan portfolio. If, after reviewing the prior examination report and annual audit, interviewing loan officers, evaluating lending internal controls and reviewing examination period changes to loan policies and procedures, examiners uncover no significant lending problems and no significant changes to loan policies or personnel, then examiners may review a minimum sample of the loan portfolio. Examiners should select a loan sample that is representative of the loan portfolio.

In larger, more complex credit unions, examiners should consider whether, and to what extent, a larger loan sample should be reviewed. Additionally, when examiners identify material concerns during a reduced or normal scope loan review, they should expand procedures to better determine the severity of the problems and to devise plans to correct problems.

The reduced scope review requires that the examiner select a sample from the loan trial balance that includes, at least the following:
- **Charged off Loans** – Scan the charged off loan list for unusual activity and review basic internal controls (board approval, proper accounting, procedures used to assign loans to a collection agency, etc.). Examiners are not required to review individual charged off loan files. However, where problems are noted, examiners may expand the scope to review individual charged off loans to determine the extent of the problem and to develop corrective action plans.
- **Delinquent Loans** – At a minimum, scan the delinquency list for unusual activity. Consider reviewing larger and more recently granted delinquent loans. Examiners

should review loans that were seriously delinquent at the last exam and are still delinquent. They should also determine how a sample of loans on the delinquency list at the last examination, or as of a selected month-end during the examination period were removed from the delinquency list.

- **Current and New Loans** – The examiner should select a random sample of current loans and loans granted since the last examination. Within this sample, the examiner should review all of the different types of loans granted by the credit union and the sample should also include a sample of loans granted by all of the loan officers and officials with credit granting authority.
- **Insider Loans** – All loans made since the last examination to officials, credit union supervisory staff, and their immediate family members should be examined. During the examination of larger credit unions, examiners should consider reviewing loans of non-supervisory staff. The examiner should also review the applicable savings and loans balances; any large or unusual transactions should be verified.
- **Large Loans and Concentrations of Credit** - The examiner should select a sample of loans and concentrations of credit to one borrower or a group of related borrowers that are greater than 10% of institutional capital.
- **Member Business and Real Estate Loans** – A sample of business and housing or mortgage loans should be selected. These loans generally have larger balances and pose greater risk to the credit union's institutional capital. Examiners should review different member business and real estate loan files at each examination. To provide adequate follow-up from one exam to the next, examiners should review the payment history of loans that were reviewed during prior examinations to verify that borrowers continue to pay as agreed.
- **New Loan Program** – If any new loan programs have been initiated since the previous exam, a sample of these loans should be selected for review.

Loan Policy Review –Prior to reviewing the selected loan sample, the examiner should review the loan policy. The loan policy should be reflective of current operations. The board of directors should review and revise the policy no less than annually. The date of the review should be noted on the policy and/or in the board minutes. The loan policy should address the following areas, at a minimum:

- How does a member become eligible to apply for a loan;
- Types of loans granted;
- Terms for each loan type;
- Types of collateral accepted;
- Desired loan portfolio diversification based on collateral;
- Maximum loan terms and available payment plans;
- Interest rates and applicable fees for all loan types;
- Definition of a credit concentration as compared to institutional capital;
- Loan officer authority;
- Loan approval process;
- Loan documentation requirements for each loan type;
- Requirements for co-signers;
- Debt to income ratio standards; and

- Process and documentation needed to disburse a loan.

Loan Review Workpaper - Examiners may document their review on a self-designed workpaper that includes the following information:

- The borrower name and account number;
- The outstanding loan balance as of the exam date;
- The date the loan was granted;
- Who granted the loan and was the loan within their authority;
- The type of loan;
- The collateral used to secure the loan;
- The value of the loan collateral;
- The borrower's debt to income ratio;
- Amount of insurance on the collateral, if applicable;
- If the credit union properly secured its lien against the collateral; and
- Any examiner comments.

All of this information should be noted for each loan file reviewed and clearly documented on the workpaper. The workpaper should be clear and concise so that it may be reviewed and used at subsequent exams. These workpapers should be included with the final report that is retained by the regulatory agency.

Loan Documentation Review – Adequate loan documentation is instrumental in determining the borrower's ability to repay. If examiners note a lack of documentation, especially in credit unions with serious or potentially serious financial problems, they should develop corrective action plans with management. Adequate loan documentation includes the following:

- A completed loan application along with documented approval;
- Documented creditworthiness analysis including debt ratio analysis and computation and verification of income and expenses;
- A completed note and security agreement;
- A perfected collateral lien and adequate insurance, if available;
- Evidence of collateral value (e.g. purchase invoice, appraisals); and
- Adequate information to assess the co-signer's ability to repay.

Lending Practices Review – The practices the board or loan officers follow determine the lending program's effectiveness. Examiners ascertain these practices during the loan review by reviewing policies, board minutes, loan officer minutes, and the loan files. When appraising practices, the examiner determines:

- **Adequate borrower information is obtained.** A complete and accurate application allows the loan officer to appraise the applicant's willingness and ability to repay. The loan application should document the applicant's income source and stability as well as their obligations.
- **That the loan officer has adequately assessed the borrower's ability to repay the loan.** Loan officers should include the new loan in addition to all existing obligations when calculating the expense to income ratio and the borrower should clearly

demonstrate that they are able to repay the loan based on their income as of the date of the loan.

- **Loan officers verify pertinent borrower information.** Borrower income should be verified by requesting a recent pay stub or summary, contacting the employer, requesting a tax return from the borrower, or by contacting individuals with similar employment. Large debts or expenses and their terms should also be verified if possible.
- **Collateral is owned or titled in the name of the borrower.** The borrower has sufficient equity in the collateral so that they will not surrender it easily, the loan repayment schedule reduces the loan balance as quickly as the collateral depreciates, the collateral value is known and is easily documented, and the collateral can readily be converted to cash.
- **The board established reasonable credit guidelines.** These guidelines should manage delinquency and loan losses as well as providing quality member service.
- **Board or loan officer actions are within their written authority.** If loans are approved outside of an employee's authority, there should be a clear explanation as to the reason.
- **Segregation of Duties exists.** No one employee or official should be able to take a loan application, approve the requested loan, disburse the funds, and perform the accounting transactions.
- **Loan interest rates are competitive with the market.** If loan rates are above market, the credit union risks attracting borrowers that can not obtain loans at other financial institutions, and if rates are too low then profitability could be negatively impacted.
- **Variable interest rates adjust accordingly.** If loans are granted with variable interest rates, the interest rate should be tied to an index that reflects changes in the market and the loan interest rates should be adjusted per the loan agreement.

Signs of Warning – These signs or indicators are ratios, numbers, trends, or suspicious activity that may indicate existing or potential problems. During the review of loans, the examiner should look for the following signs of warning:

- Large or increasing volume of loans granted or renewed with policy exceptions;
- Large or increasing volume of credit/collateral exceptions;
- Loans that are delinquent for extended periods of time without any payments or communication;
- Line of credit loans with balances in excess of the maximum approved amount;
- Loan balances that are greater than the value of the collateral;
- Loans granted to minors;
- Credit union employees that can both approve and collect loans;
- Large concentrations of credit to individuals or a group of related borrowers granted with or without board approval;
- Loans to officials, employees, and their relatives that are outside of policy;
- Rapid growth in total loan volume or certain types of loans;
- Growth in the Allowance for Loan Loss account that is significantly greater or less than the percentage growth in total loans;

- Non-performing loans or problem loans as a percentage of total loans increasing at a greater rate than the Allowance for Loan Loss account;
- High or increasing yield on the loan portfolio when market interest rates are flat or declining;
- Significant increase in the number or dollar amount of problem loans as a percent of loans;
- Loan files selected for the loan review sample that can not be located; and
- Numerous loan extensions and/or refinances granted.

Loan Deficiencies – During the review of the individual loan files the examiner identifies as specific loan exceptions: documentation deficiencies, loan processing exceptions, violations of rules and regulations and applicable law, violations of the credit union's lending policy, and poor loan underwriting criteria. General loan exceptions will also be noted. These exceptions are more global; they may apply to numerous loans or a loan policy. They do not discuss the exception in light of one borrower. All examiner exception comments, whether specific or general, should be disclosed on the Loan Exception document. If the problems or errors are chronic and/or could have a material effect on the credit union's financial position then these issues should be addressed in the Document of Resolution.

The loan exceptions document should be used at each examination as a tool, to follow-up and determine if the problems and errors identified at the last examination have been corrected.

Determining the Adequacy of the Allowance for Loan Loss Account – This account serves as a reserve valuation account, with the purpose of fairly disclosing the value of the loan portfolio. The examiner should review the credit union's funding of the account to determine the account balance represents a reasonable estimate of potential loan losses.

Determining the adequacy of the allowance account is part of each examination. The examiner should obtain the loan classification prepared by the credit union. In lieu of performing their own classification, examiners can review and analyze the adequacy of the credit union's classification, the reasonableness of any assumptions made, and the quality of supporting documentation. Additionally, examiners can ascertain that staff members performing the individual classifications are familiar with collection procedures and borrower payment performance. If the examiner feels that the credit union classification is adequate, it may be used as the workpaper and included in the final report retained by the regulatory agency. The examiner may add additional comments to the credit union's classification if needed.

The credit union's classification should clearly state all of the loans in which management does not expect to collect 100 percent of the loan balance. The classification should include:

- The borrower's name and account number;
- The outstanding amount of the loan as of the date of the report;
- The expected loss expressed as a percentage of the loan balance;

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- The total amount classified as a potential loss compared to the balance of the Allowance for Loan Loss account and any difference; and
- Any comments with respect to loan collectibility, value and condition of the collateral, adequacy of insurance, likelihood of collection from a co-signer, if applicable, etc.

If the loan classification is inadequate, the examiner should prepare a classification and provide a plan for corrective action in the Document of Resolution. Normally, examiners determine the amount of collection problem loans based on the number of months delinquent, although a loan does not have to be delinquent to be classified. If a loan is current and credit union staff is aware that a potential loss exists, then that loan should be classified. This classification identifies loans as substandard, doubtful, or loss:

- **Substandard Loans** – Loans classified as substandard have characteristics that jeopardize loan collection. Examiners normally classify at least 25 percent of the loan balance as a potential loss. Examples of substandard loans include:
  - Loans in which the credit union would have a loss due to collection costs;
  - Loans in which the credit union will not collect a substantial amount of the total even though the borrower makes partial or irregular payments;
  - Delinquent loans with inadequate co-signer information,
  - Loans in which the lien on the collateral was not properly secured; or
  - Loans in which the payments are current but represent a potential loss because of the payment terms or past payment history.

- **Doubtful Loans** – Loans in this category possess all the weaknesses inherent in a loan classified as substandard, with the added characteristic that the weaknesses make full collection improbable. Loans classified as doubtful should be considered a 50 percent loss. Examples of doubtful loans include:
  - Delinquent loan balance that exceeds the collateral value; or
  - Delinquent borrowers who have not been able to consistently make payments.

- **Loss Loans** – Loans classified as a loss are of such little value that they should no longer be considered a loan on the balance sheet. Unless management can support collectibility, they should classify loans in this category as a 100 percent loss. Examples of loss loans include:
  - Any loan six months or more past due without a payment in the last 90 days of at least 75 percent of a regular monthly installment;
  - Delinquent loans with an attorney or at a collection agency;
  - Delinquent loans in which the borrower can not be located; or
  - Loans in which a deficiency balance remains after the sale of the collateral.

Examiners then compare the total of the classified amounts to the balance in the allowance account. If the loan classification differs significantly from the balance of the Allowance for Loan Loss account, the Document of Resolution should include a directive to immediately increase (or decrease) the account to meet full and fair disclosure.

Signs of Warning – These signs or indicators are ratios, numbers, trends, or suspicious activity that may indicate existing or potential problems. During the review of the adequacy of the Allowance for Loan Loss account, the examiner should look for the following signs of warning:

- The account balance is consistently less than the classified loan amount;
- Management is repeatedly over optimistic with regards to the amount that can be collected on the classified loans;
- Loans were charged off (a debit in the allowance account) that were not approved for charge off in the board minutes; and
- The external and/or internal auditor does not periodically review the allowance account activity.

Objective of Collections Review– The principles of safety and soundness require the board of directors to establish and supervise an effective loan collection program. The review of the credit union's collection policy and operations is imperative during the examination to determine:

- Causes of delinquent loans;
- If collection techniques are results-oriented;
- If the collections department provides all the necessary information concerning the collectibility of the delinquent loans to management and officials;
- If the collection department staff is manipulating delinquent loan accounts to reduce delinquency; and
- Any corrective action plans needed to improve collections.

Collection Policy – Prior to reviewing the operations and results of the collection department, the examiner should review the written collection policy. The policy should be reviewed and revised by the Board no less than annually. The date of the review should be documented on the policy and/or in the board minutes. The policy should include the following, at a minimum:

- Who is responsible for collections;
- When a loan is considered delinquent;
- Reporting requirements to the board for delinquent loans;
- Timeframes for making collection contacts with delinquent borrowers;
- When the co-signer will be notified, if applicable;
- How and when collateral is to be repossessed;
- How the collateral should be sold;
- Collection system used to document contacts with delinquent borrowers;
- The approved use of loan extensions and loan refinances;
- Who has the authority to approve loan extensions and refinances;
- When loans are to be charged off;
- How recoveries on charged off loans will be handled; and
- Any fees and penalties associated with delinquent loans.

Collection Procedures Review – An accurate list of delinquent loans must exist for the examiner to evaluate collection policies and practices. The delinquency list should provide the following information:

- Borrower name and account number;
- The outstanding loan balance;
- Date the loan was granted;
- Breakdown of delinquency in categories – 0-30 days delinquent, 30-60 days, 60-90 days, 90-120 days, 120-180 days, 180-360 days, and greater than 360 days delinquent (the outstanding loan balance is considered delinquent, not just the delinquent amount);
- Date of the last payment received;
- Amount of the last payment received; and
- Comments and additional information.

Examiners should select a sample of the loans on the delinquency list and test the accuracy of the credit union's delinquency calculations. If the sample tested reveals loans improperly categorized on the delinquent loan schedule, this should be addressed either in the Examiner Findings or the Document of Resolution, depending on the severity of the problem.

Examiners should also compare the delinquent loan list as of the examination date to another month-end delinquency list and determine how loans were removed from the list. Examiners must keep in mind that loans can only be removed from the delinquent loan list by:

- Paying the loan current;
- Extending the loan maturity date or refinancing the loan; or
- Charging the loan off to the Allowance for Loan Loss account.

Lastly, the examiner should interview the collection department manager to learn about the collection procedures used. This step could be brief, if delinquent loans are not a problem or quite lengthy if delinquent loans are increasing, reducing loan income, and/or negatively impacting the credit's institutional capital. The purpose of this interview is to develop corrective action plans that will be addressed in the Examiner Findings or Document of Resolution, depending on the severity of the problem.

Signs of Warning – These signs or indicators are ratios, numbers, trends, or suspicious activity that may indicate existing or potential problems. During the review of the collection area, the examiner should look for the following signs of warning:

- Credit union employees that have the authority to approve and disburse loans, and collect delinquent loans;
- Numerous loan extensions and/or refinances granted;
- Adequate time is not given to loan collections, if collections is performed by an employee with other job duties;
- Collection personnel does not have adequate training;
- Collection personnel that lack the attitude and personality needed to collect loans;
- Collectors that have access to credit union cash;

- Collection agencies or outside third parties that do not provide a monthly activity report; and
- Suspicious relationships or activities between the collector and third party agents used to sell repossessed collateral.

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Examination Process – Asset Liability Management Review
October 30, 2002

Asset liability management (ALM) can be broadly defined as the continual rearrangement of both sides of the credit union's balance sheet in an attempt to maintain reasonable profitability, to minimize interest rate risk, and to provide adequate liquidity. All credit unions perform some sort of ALM analysis; however, the level of involvement and understanding of the officials and management, and the quality of their analysis decisions varies widely. When the officials declare a dividend or change interest rates on loans, they are engaging in ALM. These decisions can impact liquidity and profitability. ALM strategies and techniques vary depending on the credit union's capital structure, the products and services offered, the terms of loans and deposits, and the level of the official's and management's understanding. In a small credit union with basic services ALM can consist of:

- Awareness of the member's share and loan needs;
- Access to a line of credit for short-term liquidity needs;
- Relatively short-term investments;
- Ability to adjust dividends and loan rates to changes in the market; and
- Adequate earnings and capital.

Daily management is usually responsible for analyzing the ALM position. The examiner's role is to review the ALM process and identify weaknesses or problems that could have a negative impact on the credit union's financial position.

Objective of the ALM Review – The objective of the ALM review during the examination is to:

- Determine the credit union has sufficient liquidity to handle normal savings and loan needs and that management is aware of any cyclical changes that can effect liquidity;
- Analyze management's approach to ALM and determine that interest rate risk is minimal; and
- Ascertain the ability of the ALM process to adapt to significant changes in the market.

Scope of the ALM Review – The scope of the ALM review will vary widely. Credit unions with a conservative, short-term maturity structure for savings, loans, and investments often only need a basic understanding of ALM. The review will be much more in-depth in larger credit unions that offer a wide array of products, services, fixed and variable interest rates and longer-term maturities on loans and savings.

If the examiners noted no major problems during the prior examination and no significant changes have occurred during the examination period, examiners will review the ALM program and the monitoring of liquidity to determine if all risks are adequately managed. Keeping the size and complexity of the credit union in mind, examiners should:

- Review the credit union's underlying assumptions used to develop their ALM analysis to determine if they are realistic and reasonable;
- Determine that credit union staff understands and adheres to its ALM program; and
- Assist management in developing corrective action plans, as needed.

While smaller and less complex credit unions may not have a formal ALM program, examiners should determine that credit union staff understands the mix of the balance sheet and its impact on the income statement.

If the credit union has had a key ALM personnel change or if ALM problems or potential problems exist, examiners will expand the analysis to a point where they are able to satisfy their concerns, and can develop reasonable, effective plans for corrective action.

ALM Policy – The ALM policy will vary depending on the sophistication of the credit union and the services and products offered. Credit unions that offer only basic products such as short-term consumer loans and regular savings may be able to address the very basic ALM considerations of sufficient daily liquidity and/or sources of short-term liquidity in the investment policy. Credit unions that offer more than the basic loan and savings products should have a written ALM policy that addresses the following, at a minimum:

- **Objectives** - that discuss the need to provide adequate liquidity and profitability while minimizing interest rate risk;
- **Responsibility** – who formulates and implements the policy, who analyzes the ALM position of the credit union and how frequently, what reports are used to provide the board with the ALM position, and who recommends changes to policy;
- **Monitoring** – this section documents how the credit union will monitor its ALM position, what reports will be reviewed, which ratios the credit union will calculate to analyze ALM, how often the ratios will be calculated and reported to the board, and the goals for each of the ratios;
- **Specific Guidelines** – the policy should define minimum goals such as:
    - The credit union will not allow a negative net interest spread for more than 3 consecutive months, or
    - Operational management will monitor and report to the board monthly the following 3 ratios - Core Deposit Ratio, Loan Term Assets to Total Assets, and Liquid Assets to Total Assets.

Qualitative Analysis – After reviewing the ALM policy, the examiner should begin with the ALM qualitative analysis. The focus should be on the credit union's exposure to interest rate changes, specifically on management's awareness, ability, and willingness to make adjustments to minimize the effect on profitability and capital. To perform the qualitative analysis, examiners should answer the following questions:

1. Has management developed an ALM plan and is the credit union following it?
2. Is it commensurate with the credit union's size and complexity?

3. Is the credit union measuring and monitoring its ALM position? Are the credit union's assumptions for this reporting mechanism reasonable and documented?
4. Does the present ALM structure pose material safety and soundness concerns?
5. Do the board and staff have sufficient training to understand ALM reports and their implications?
6. Is the board using the ALM report as a tool in the decision-making process or is the report "for the examiner" only?
7. Has management identified the core or stable member deposits that may be used to fund longer-term assets?
8. Has management documented the liquidity needs throughout the year to meet operating expenses, loan demand, and share withdrawal?
9. Are cash flow or potential liquidity problems indicated?
10. Has the board established reasonable targets for loan and investment portfolio diversification?
11. Does the credit union have a suitable mix of long and short-term assets in relation to its size, complexity, and share structure?

Quantitative Analysis – Quantitative analysis can assist in determining the level of exposure. Examiners should perform this analysis as a part of each exam. Ratios and trends are the focus of quantitative analysis. The following ratios are used to assist examiners in judging the ALM position of the credit union:

1. Net Loans / Total Assets – This ratio measures the percentage of total assets that are invested in the loan portfolio. Management should have established a maximum goal ratio to avoid a liquidity problem.
2. Core Deposit Ratio – This ratio is used to identify stable deposits that the credit union can rely on, regardless of seasonal swings, which can be used to fund longer-term assets. The more stable the funds, the easier it is to control liquidity and ALM. Therefore a high percentage is desirable and indicates a solid credit union.
3. Liquid Assets / Total Assets – This ratio measures the percentage of total assets that are invested in liquid assets. Liquid assets often pay no interest or have a lower yield because there is very little risk. Only enough funds to meet liquidity needs should be maintained in liquid assets.
4. Liquid Assets – Short-term Payables / Member Deposits – The adequacy of the credit union's liquid cash reserve to satisfy client savings withdrawal after paying all immediate obligations is measured by this ratio. The goal is to have just enough liquid funds to meet all member requests and operating expenses, with any excess funds invested in interest bearing accounts.
5. Loan Turnover Ratio – This ratio estimates how quickly the credit union will convert the loan portfolio to cash. The lower the result the faster the loan portfolio matures. ALM should be easier because the loan portfolio repayment is high, thus allowing management access to funds to provide for sufficient liquidity and funding of new loans and investments. The examiner can also analyze the changes to the ratio over various timeframes, this would provide an indication of the effect of recent decisions on the average term of the loan portfolio.

6. External Credit / Total Assets – This ratio measures the level of external credit. Examiners should ensure that the credit union is not dependent on external credit sources to fund normal daily operations and long-term needs; external credit should be used only to fund short-term liquidity shortfalls.
7. Net Interest Margin – This calculation starts with gross income and determines the amount available to cover operating expenses and contributions to capital after all interest and dividends on savings have been paid. Management should determine the minimum net interest margin that must be maintained in order to meet all operating expenses and capital contributions. Analyzing the net interest margin trend provides insight to the effect of management's past pricing decisions.

Information gathered while performing both the qualitative and quantitative analysis' should be placed in the workpapers and included in the regulatory agency's final report.

GAP Analysis – Gap analysis is a tool used by credit unions to analyze the match between rate sensitive assets (RSA) and rate sensitive liabilities (RSL). If RSAs and RSLs are evenly matched the effects of interest rate changes will be minimized while profitability is maximized. RSAs and RSLs are those assets and liabilities that mature or can be priced either upward or downward in the short-term. RSAs are loans or investments with yields that respond to changing short-term interest rates. The change may be contractual in nature such as a variable rate loan and/or due to maturity of the asset. RSLs have terms that respond to changing short-term interest rates such as certificates of deposit or money market accounts.

Gap analysis is performed on a spreadsheet. The assets and liabilities are assigned to time periods (0-1 month, 1-2 month, etc) based on their maturities. This is relatively simple for components such as investments and certificates of deposit in which the total amount matures on a specific date. But more complex if the RSA or RSL does not have a stated maturity such as a savings account or the total outstanding balance of the RSA or RSL does not mature all at once, but over a specified time period such as member loans.

Gap analysis also considers the repricing opportunities of the assets and liabilities, when all or part of the assets and liabilities will be available for reinvesting at the prevailing interest rates. The culmination of the analysis is the:

- **Gap** or the total of RSAs – RSLs for each time frame; and
- **Gap ratio,** which divides the above result, or gap by total assets. The gap ratio puts the gap in perspective to the credit union's size. A gap of $500,000 would not be material for a credit union with $10 million in assets, but it would be for a credit union with $2 million in assets.

The gap and gap ratio results can be positive, negative, or zero. A credit union with a positive gap assumes a more asset sensitive position (RSAs reprice quicker than RSLs). With a negative gap, RSLs are repricing more quickly than RSAs within the time period. A gap of zero indicates that the RSAs and RSLs for the time period are evenly matched.

While gap analysis provides an important tool for judging RSAs as compared to RSLs, it has limitations:

- The gap ratio assumes that all rate sensitive accounts reprice equally;
- It is not useful in determining how RSAs and RSLs should be positioned with regards to maturity to maximize profitability.
- It is similar to a balance sheet as it is only a snapshot in time, it does not measure the effect of multiple interest rate changes over time; and
- It relies heavily on the assumptions that were used to create the report, if the assumptions are incorrect, then the information is useless.

The examiner's responsibility when reviewing a credit union's gap analysis is to determine:

- The soundness of the assumptions used by management to draft the gap analysis report;
- That the gap and the gap ratio are within an acceptable range given current earnings and the credit union's capital position; and
- That management uses the gap analysis in conjunction with the items discussed under the qualitative and quantitative analysis sections to make decisions.

To assess the quality of the gap analysis and the management's overall understanding of the concepts, examiners should provide answers to the following questions and document the results and any additional comments in the workpapers:

1. Does management have a good understanding of the gap analysis along with the benefits and limitations of the analysis?
2. Are the assumptions used to draft the analysis reasonable, specific to the credit union and documented in writing?
3. Are the credit union's earnings and capital positions strong enough to withstand the risk exposure revealed in the gap analysis?
4. Could the asset and liabilities structure be changed should it be necessary to diminish the risk exposure?
5. Does management and the officials consider the results of the gap analysis prior to making decisions that will effect it, such as changing loan and savings interest rates or offering a new longer-term loan product?

Signs of Warning – These signs or indicators are ratios, numbers, trends, or suspicious activity that may indicate existing or potential problems. During the review of asset liability management, the examiner should look for the following signs of warning:

- Significant mismatch of the asset/liability maturities;
- Borrowing funds for normal business operations;
- Lack of adequate ALM policy considering the sophistication of the credit union;
- Officials that are reluctant to lower savings rates or increase loan rates;
- ALM analysis that is not used as a management tool, but rather is performed for the examiner only;
- High level of long-term assets to total assets;
- Declining net interest margin;
- Increasing loan turnover ratio;

- Rapid savings growth and/or above market interest rates on savings;
- Constant liquidity problems; and
- Lack of diversification of loans and savings types.

ALM Deficiencies – Problems that cannot be resolved during the exam, and are not material, should be noted in the final report in the "Examiner Findings". This document lists operating exceptions, violations of law or regulation, unsafe and unsound policies, practices, and procedures. Relatively minor or infrequent infractions should not be discussed within this document; they distract from the more important matters. Immaterial issues should be discussed orally with the manager or appropriate employee.

When identifying a finding, the examiner should include a precise description of the problem or violation, who is responsible for correcting the problem, the specific section of the Law, bylaws, rules and regulations, or other authority which the finding violates. In the event that the credit union violates more than one of the aforementioned, the examiner should cite the highest authority. Examiners should also include on this document exceptions that were noted at previous exams that have yet to be corrected. These findings should be cited under a heading of a similar nature. Issues and problems of a material nature should be addressed in the Document of Resolution.

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Examination Definition,
Objectives, Scope, and Process
October 29, 2002

For regulatory agencies around the world it is critical to perform on-site examinations for the financial institutions. No one tool is more useful in determining risk than the on-site examination performed by the regulatory body. This examination can be adapted and its scope reduced or expanded based on institutional risk, number of qualified individual available to perform an exam, and monetary resources available.

Full Scope Examination Definition - The examination process is a series of procedures used to determine the economic and financial status of credit unions. Examinations focus on key trends, ratios, management, and operations.

Established examination procedures should provide the examiner with considerable flexibility in tailoring the examination according to the complexity and relative risk of each individual credit union. Examinations are generally performed on an annual basis, but this time frame can be reduced or increased based on credit union risk, identified problems, and/or staffing of the regulatory agency.

During the on-site examination and throughout the period between examinations, the importance of discussing credit union operations with management including goals, plans, policies and internal controls cannot be overemphasized.

Full Scope Examination Objective – Examination has five overall objectives:

- Evaluate the credit union's financial soundness;
- Appraise the quality of management and their adherence to regulations and agreements;
- Determine the asset quality and degree of risk that the credit portfolio poses to the integrity of the credit union;
- Develop plans with officials to correct problems and obtain their approval of the corrective actions; and
- Follow-up with the credit union to ensure timely correction in the areas of concern.

Scheduling Examinations – Examination frequency is scheduled taking into consideration the size and complexity of the credit union and the geographic location. Examiners should consider the following when prioritizing and scheduling examinations:

- Financial conditions and trends in the credit union;
- Potential risk to the integrity of the overall credit union system and risk of loss to an insurance or stabilization fund, if such exists;
- Date of the last examination;
- Information pertaining to the credit union received from outside sources; and
- Number of examiners needed to perform the exam.

Scope of Examination– The examination should concentrate on five major areas of importance. These areas are:

- Analysis of the general ledger;
- Analysis of the loan portfolio;
- Analysis of management capabilities and decisions;
- Analysis of investments; and
- Analysis of liabilities.

The scope of an examination can be flexible and is defined in one of three categories:

1. Reduced;
2. Normal; or
3. Expanded.

Flexible examination scope gives the examiner reasonable latitude in setting the scope and establishing the major areas of review for the exam. The flexible exam allows examiners to perform the examination procedures they deem necessary assess a credit union's operational integrity, financial condition, and the extent to which problems may exist.

When examiners begin the on-site examination process, they should perform the following procedures to gain the information needed to determine the scope of the exam:

- Review the external audit;
- Review financial information and ratio trends;
- Calculate preliminary PEARLS key ratios as of the exam date;
- Review the previous examination results, adherence to agreements between credit union management and regulatory officials and recent correspondence;
- Review written credit union policy and procedure;
- Scan the board minutes;
- Determine if there has been significant changes since the previous exam such as: key personnel changes, significant new programs, decrease in institutional capital, computer system conversion, material changes in the investment or loan portfolio, record keeping problems, lawsuits, and/or regular need for borrowed funds.

Performing these procedures allows the examiner to become familiar with the related policies, procedures, and internal controls while making an initial assessment of risk and determining appropriate examination procedures necessary to test or review a particular area.

The use of reduced scope of work exams depends on the quality of management, the internal audit, external audit, as well as the current economic and financial situation of the credit union. When the initial review of an area indicates that there are no serious problems, the examination should continue with reduced procedures. For example – if problems have been corrected and management is competent and responsible, then the examiner should use minimum procedures on the examination. But, if the reduced exam procedures were used during the previous exam, the examiner should not use the reduced procedures on the subsequent exam. Reduced procedures can not be used two consecutive years. Examiners should expand their scope of work when the initial stage of the exam reveals problems. For example – a rapid rise in the delinquent loan ratio

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triggers a more detailed review of delinquent loans to determine the causes for the delinquency, and of current loans to determine whether the problems continue in the recently granted loan portfolio.

A normal full scope examination usually consists of a review of the following operational areas:

- General Ledger and Financial Statements
- Cash Analysis
- Investment Analysis
- Capital Adequacy and Profitability
- Asset Liability Management
- Administration and Management
- Risk assessment of the loan portfolio
- Evaluation of the adequacy of the Provision for Loan Loss account
- Review of the Supervisory Committee work and effectiveness
- Review of Internal Controls
- Member deposits and other debt obligations
- Computer System

Based on the risk assessment addressed above, a reduced scope exam would review each area but the work performed would be reduced as compared to the normal or expanded scope exams. The extent of audit procedures for reduced scope exams are limited to assessing risks in each area and determining that the risk to the financial system and the insurance or stabilization fund, if such exists, are very limited. Expanded scope examinations are used as conditions warrant. If initial examination procedures disclose major concerns in one or more areas, examiners should expand the analysis; completing additional examination procedures to a point in which the extent of the problems can be identified and effective plans for corrective action developed.

Initiation of the Examination Process – Examiners begin planning for an examination before entering the credit union office, and adjust the examination plan as necessary throughout the examination to address problems as they arise. By analyzing qualitative data (including data obtained from recent correspondence, prior examination and supervision reports, and discussions with the prior examiner) and quantitative data (including key trends and ratios and financial statement information) examiners determine if they need to perform additional examination steps.

➢ **Pre-Examination Planning** consists of:
  - A review of the credit union file maintained by the regulatory body that should include previous exam reports and correspondence, with the objective of identifying and understanding previous problems, issues, and weaknesses.
  - An analysis of financial data from pervious periods to identify negative trends and areas of concern.
  - A review of the most recent external audit and contacting the auditor to set a meeting to discuss the audit, their workpapers and findings.

- Establishing the date of the examination. The exam may be conducted on a surprise basis or management can be contacted in advance.
- Contacting credit union management (if the exam is not conducted on a surprise basis) to advise them when the examination will start, how many examiners will be there, how long the exam will last and when the exit meeting should be scheduled.
- Preparing a list of reports and information that will be needed to conduct the examination and delivering it to the credit union (if the exam is not conducted on a surprise basis) at least one week prior to the commencement of the exam.
- Notifying team members (if applicable) of location, time, security precautions, anticipated length of exam, and other pertinent information.

➢ **Upon arrival** at the credit union the examiner will:
- Discuss the examination objectives and process with management;
- Ensure that all the information requested prior to arrival is easily accessible;
- Determine the scope of the examination based on the aforementioned review process;
- Select the loan files to be reviewed;
- Obtain the most recent organizational chart so that each examiner participating in the exam knows who they should communicate with based on the work they are performing;
- Obtain a list of the names, account numbers, loans and savings balances of all officials, employees and their immediate family; and
- Determine if any one person or group of people appears to control or dominate the credit union.

Total Analysis Process – In conducting total analysis, the examiner considers both qualitative and quantitative data. The total analysis process consists of six steps:

1. Collect Data – The examiner collects financial information from the credit union's accounting records such as the balance sheet and income statement. Qualitative data is gathered through observations, reading board minutes, policies, recent correspondence and prior exam reports, and by discussions with officials and employees.
2. Review Data – To review the data the examiner breaks down and reassembles the data, relating the individual parts to the whole, notes all of the positive and negative trends, and evaluates the data.
3. Interpret Data – Interpreting the data is the most complex phase of the total analysis process. The examiner should:
   - Inquire about the local economic conditions and other relevant facts not directly available within the confines of the credit union;
   - Listen to employees and officials;
   - Observe the strengths and weaknesses of personnel;
   - Observe the attitudes of the members who transact business at the credit union;
   - Differentiate between important and unimportant data; and
   - Place all of the data in proper perspective.

4. Reach Conclusions – After collecting, reviewing and properly interpreting the data, the examiner arrives at a conclusion. The examiner should identify concerns, explain the causes, and arrive at an institutional rating.
5. Make Recommendations – Recommendations are based on the conclusions reached after analyzing the operation. The recommendations are usually general statements addressing what the credit union should do to overcome the problem.
6. Develop Plans for Action – Well-designed, achievable, and measurable plans for action should correct existing problems and prevent problems from recurring. Since management is responsible for implementing the plans for action, the examiner and officials or key employees should develop the plans jointly. A plan for action should specify:
   - Who will take the action;
   - Description of the action;
   - Start and completion dates; and
   - Which official or group of officials will oversee the action.

The results of the total analysis process are valid only if the examiner considers all pertinent data and interprets it accurately. If examiners have not properly applied the total analysis process, the recommendations and plans for action may not be appropriate. To reduce this possibility the examiner should:

- Make a final review of all data;
- Discuss analysis and conclusions with management;
- Determine that the recommendations and plans for action are practical, specific, and understandable; and
- Determine that the plans will prevent problems from recurring.

Limited Scope or Follow-up Examination – Examinations can also be performed that concentrate on the review of specific areas of concern. These are referred to as limited scope or follow-up examinations. These examinations are a part of overall examiner supervision just as full scope exams are. Supervision is the on-going monitoring of a credit union's financial and operational condition. Examiners supervise the credit unions assigned to their districts as needed through telephone contacts, review of submitted financial information, and follow-up examinations.

To ensure the prompt, effective correction of problems, the examiner who identified the problems and developed plans for corrective action should maintain supervisory responsibilities and perform all follow-up examinations and contacts.

➢ **The purpose** of follow-up examinations is to:

- Review with management the progress on plans for action to correct previously identified problems and develop additional plans for action for problems identified during the follow-up examination within a reasonable time;
- Detect emerging financial trends that could threaten the credit union's solvency,
- Determine the credit union's economic viability and, where necessary, explore other options to continue member service;

- Recommend administrative actions when necessary to protect the interests of the members, creditors, and the insurance or stabilization fund; and
- Recommend future supervision plans and contact dates.

➢ **The main difference** between a full scope and a follow-up examination is that the focus is on the problem areas previously identified. Examiners should review the progress made on solving the problems previously identified. They should also identify and document new and evolving problems discovered while performing the exam. Examiners should then amend and/or develop plans for action with the officials to correct unresolved and serious new problems. Upon completion of the follow-up exam, the examiner will hold an exit meeting to update management and the officials on the status of the problems, the recommended corrective actions, and to attain the official's approval of all recommended actions.

➢ **Scheduling** of follow-up examinations should take into consideration the seriousness of the problem.

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Examination Process – Final Examination Report
October 28, 2002

The examination report is the official report from the regulator to the credit union. It is an important part of the communication process, as it allows the regulatory body to communicate its assessment of the credit union's overall condition. The report should document all significant items discussed during the examination and describe in great detail the credit union's strengths, weaknesses, and the corrective actions needed to resolve any problems. The examination report should be viewed as a diagnostic tool, which is used to clearly communicate the overall safety and soundness of the credit union.

The lead examiner (if there is more than one examiner performing the exam) prepares the report and delivers it to the key officials no later than two weeks after the close of the examination. The officials are the primary users of the report and its audience, therefore, the examiner should make the report specific to each credit union. Two reports should be generated upon the termination of the exam. Examiners should retain a copy of the official or field report, including all workpapers, schedules, checklists, forms, and examiner developed documents. This copy will be a part of the official file maintained within the regulatory agency for each credit union. The other copy will be delivered to the credit union and should include, at a minimum, the documents discussed below.

Examination Report Components – Required examination workpapers as outlined in the table below, form the basis of the examination report. Additional workpapers, checklists, and/or examiner-developed documents may be included, at the discretion of the examiner. This auxiliary information should provide in-depth information concerning problem areas or evaluate specific problems, provide support for examination findings, and assist in the resolution of the identified problem(s).

Name of Form or Workpaper	Credit Union Report	Regulatory Report
Balance Sheet	Yes	Yes
Income Statement	Yes	Yes
PEARLS Ratios	Yes	Yes
Examination Overview	Yes	Yes
Examination Scope	No	Yes
Examiner Findings	Yes	Yes
Confidential Section	No	Yes
General Ledger Review Workpapers	No	Yes
Investment and Cash Review Workpapers	No	Yes
Management Review Workpapers	No	Yes
Loan and Collection Analysis Workpapers	No	Yes
Asset Liability Management Analysis Workpaper	No	Yes
Savings/Reserves/Profitability Analysis Workpapers	No	Yes

Loan Exceptions	Yes	Yes
Document of Resolution	Yes	Yes
Other examiner developed workpapers	Yes/No Examiner Discretion	Yes

Final Report Organization – The documents that concisely present the financial and operational condition of the credit union should be placed at the beginning of the report. These forms include the Examination Overview, the Document of Resolution, Examiner Findings, Loan Exceptions, and PEARLS ratios. All of the other workpapers should follow and be organized as to their importance to the reader of the report.

Examination Overview – This document organizes and presents, in a clear and concise manner, all of the examiner's major or material observations, comments, recommendations and conclusions. Examiners can use the overview, which discusses and supports the examiner's analysis and findings, to place examination findings into proper perspective. The lead examiner (if more than one examiner performs the exam) writes the overview and it should be directed to the credit union's management and officials. The depth and complexity will vary depending on the severity of the problems. If no material risks exist, the overview should be brief, usually less than three pages. Conversely, if the credit union has serious problems, the overview should be more detailed. Comments in the overview should fully support the assigned regulatory rating as of the exam date.

Normally the overview is written as the examination comes to a close, but prior to the exit meeting with the officials. If an examiner learns of additional information during or after the exit meeting that would effect the content of the overview, it can be amended.

Document of Resolution – This is the key document for resolving problems in the credit union. While the overview discusses the credit union's financial condition, examiner conclusions and recommendations, it is the Document of Resolution (DOR) that lays the groundwork for corrective action. As such, it must clearly convey the problem areas, their significance, and the how the corrective actions should be taken. The greater the credit union's problems the more extensive, detailed, and specific the DOR should be.

Examiners should develop the DOR jointly with officials and credit union management. The DOR will specifically state the corrective action needed to solve the problem, who is responsible for correcting the problem, and the timeframe in which the problem should be resolved. Essentially, the DOR contains the agreements reached with officials to correct major areas of concern and will be used at the next contact or examination as a means to follow-up on problem resolution. Examiners discuss corrective action for minor problems with the officials or management and in the Examiner's Findings document. For example – if the general ledger account for computer equipment was out of balance with the subsidiary ledger, this problem would be noted in the Examiner Findings. However, if the Bank account had not been reconciled for the last 2 months, the corrective action for this problem would be addressed in the DOR. In other words, the DOR is limited to major problems, those that could effect the credit union's financial condition or interfere with daily operations.

The keys to drafting a results-oriented DOR are:

- Open lines of communication between credit union officials and management and regulatory authorities,
- Involvement of credit union management and officials in developing the corrective actions to be taken to solve the identified problems,
- Realistic solutions and time frames to solve the identified problems, and
- Discussions between management, officials, and examiners throughout the examination concerning all of the problem areas and the corresponding corrective actions so that there are no surprises at the exit meeting when the DOR is discussed.
- The DOR should be SMART, or in other words,
  - Actions to be taken should be Specific,
  - The timeframes Measurable,
  - The corrective actions Achievable, and
  - The document Results-oriented and Timely.

The DOR should be succinct. Each item or directive on the DOR should start with an action verb such as – reconcile the bank account general ledger balance to the bank statement (subsidiary ledger) or contact all delinquent borrowers within 10 days of a missed payment. The DOR should not include acronyms, abbreviations, and/or jargon; it must be understood and clear so that the corrective actions are undertaken as anticipated by the examiner. The items or directives on the DOR should be prioritized; the most serious problems should be addressed first. The examiner should also establish follow-up steps in the DOR. He/she should request that the credit union send financial statements, copies of board minutes, credit union policies, etc. to demonstrate that the requested corrective steps are being taken as agreed upon and within the established time frames.

The examiner, credit union officials, and management discuss the DOR in-depth at the exit meeting. The DOR may be modified during this meeting if all parties agree with the document and the changes. The modified DOR would then become a part of the final report. When the DOR is satisfactory to all parties, it should be approved at the exit meeting by a vote of the board of directors.

Examiner Findings – The Examiner Findings document lists operating exceptions, violations of law or regulation, and unsafe and unsound policies, practices, and procedures. When identifying a finding, the examiner should cite the specific section of the Law, bylaws, rules and regulations or other authority. In the event that the credit union violates more than one of the above, the examiner should cite the highest authority.

This document will also be used as the DOR, as a follow-up tool for the examiner at the next contact or examination. During the next contact or examination, the examiner will review all of the findings cited at the previous examination and determine if they were corrected. Examiners should list exceptions noted during previous examinations but not yet corrected under a heading similar to: "Findings Noted at Previous Examination That Are Not Yet Corrected".

Credit union management should be allowed to correct as many exceptions as possible before the close of the examination. The examiner will then note on the document that these items have been corrected.

Examples of examiner findings are:

1. The loan policy did not state that a credit report older than 6 months should not be used to qualify a member for a loan,
2. The cashier left her drawer unlocked on four occasions during working hours, or
3. The accounts payable general ledger balance was not supported by a subsidiary ledger.

Loan Exceptions – This document is used to note the specific borrower loan exceptions to policy and procedure and the general exceptions to sound loan underwriting. Within this document the borrower's account number should be referenced, along with the current loan balance, the date of the loan, and the specific borrower loan exception.

Examples of specific loan exceptions are:

1. The borrower's debt to income ratio was 47% with no explanation why the loan was granted when the maximum debt ratio noted in the loan policy is 45%,
2. The co-borrower did not complete an application, or
3. The credit union did not secure a lien on the used vehicle that was taken as collateral.

Examples of general loan exceptions are:

1. The loan policy does not state that the borrower's income must be verified prior to the loan approval,
2. The loan policy does not state that the co-signer's ability to repay the loan should be determined just as that of the primary borrower, or
3. The loan policy does not state the maximum number of borrowers any co-signer can sign for.

Confidential Section – This document is for the internal use of the regulatory agency. The confidential section discloses what the prior exam did and did not accomplish and can be used to relate information that was not disclosed in the Examination Overview of the current examination. Examiners should comment briefly about results of all meetings and discussions held with management, the formal actions the board took to resolve the major problems, and agreements reached with officials outside of the DOR.

Examiners should cover pertinent matters of a private or restricted nature in the confidential section including personal opinions based on the examiner's observations. However, the examiner should not make statements based on gossip or hearsay. Examples of material covered in the document include: an appraisal of a new credit union's prospects, comments concerning the attitudes and abilities of the officials or daily management, further difficulties facing the credit union, and plans for monitoring the progress of the SCU (e.g. supervision contacts, follow-up examinations). The confidential section should be used as extensively as is necessary, but it should not be cluttered with inconsequential or irrelevant facts and opinions.

Examination Workpapers - Workpapers are the written documents prepared or obtained by the examiner while performing an examination. Included in the workpapers are schedules, memos and other items, along with the analysis used by the examiner to reach his/her conclusions. The workpapers serve as the basis of the work performed and support the results of the examination and the opinions of the examiner. Because of the importance of the workpapers, they must provide sufficient detail and support to allow an independent reader to understand how each conclusion was reached, including a detailed description of the methodology used to calculate certain ratios or prepare financial statements or similar reports. The workpapers should provide sufficient information so that the reviewer does not have to obtain any additional information from the credit union to support the conclusions, once the examination has been completed.

Workpapers should be organized in sections that correspond with the examination work performed, such as: general ledger review, employee loan analysis, delinquent loan analysis, cash review, etc. As a result, each section should include the following at a minimum:

- Specific identification of the person who performed the work including the exam date and the date the work was performed;
- The objective, scope, and nature of the work performed;
- The name and title of the employee at the credit union who is familiar with and/or provided the information needed to complete the work;
- All documents used to support the conclusions of the examiner, including detailed support indicating where figures were obtained or explaining how each one was calculated; and
- An indexing system that allows the work to be filed and retrieved in an orderly manner.

Upon termination of the examination, the workpapers should be maintained within the regulatory agency, in a safe place, along with the final report. They should be available for review and used at the next examination.

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Examination Process – General Ledger Review

October 29, 2002

The review of a credit union's general ledger and its related subsidiary ledgers is a key area of the examination and should give the examiner a clear impression of the credit union's financial position and its relative financial stability.

Objective of the General Ledger Review – The purpose of the general ledger review is to determine that:

- The credit union has adequate policies, practices, procedures, and internal controls regarding its assets, liabilities, and equity;
- Accounting personnel operate in conformance with established bylaws, rules and regulations, and accounting norms;
- Assets are properly recorded;
- Liabilities and equity are properly recognized and recorded on the books; and
- Credit union management initiates corrective action when made aware of deficiencies or violations in policies, practices, procedures, or internal controls.

Scope of General Ledger Review – Early in the exam process, examiners should review the reports of the internal and external auditors, and if necessary, the workpapers along with the prior examination report to assist them in determining the scope of the general ledger review.

When the previous examination or supervision contact discloses no material record keeping problems, interviews with management and staff disclose no internal control or other concerns, and examiners note no material concerns in the initial review of the books and records, the examiner can use a normal scope review. Additionally when the credit union has had an acceptable external audit, examiners may reduce the general ledger review to the complexity and risks involved.

Similarly, if initial examination procedures disclose major concerns examiners will expand the analysis of the general ledger to a point where they can determine the extent of the problem and develop effective plans for corrective action. The level of analysis depends upon the complexity of operations and the seriousness of adverse conditions.

At a minimum the accuracy, documentation, and timeliness of the accounting for the following accounts should be reviewed:

- Loans
- Provision for Loan Losses
- Accounts Receivable
- Cash
- Investments
- Material Fixed Assets
- Accrued Income

- Accrued Dividends Payable
- Suspense and Clearing Accounts
- Member Shares and Deposits
- Equity or Capital Accounts
- Any accounts with large monetary transactions
- Any accounts associated with new programs initiated since the last examination

Examination Procedures – When analyzing general ledger accounts, examiners should:
- Determine that the general ledger accounts and balances are supported by an independent subsidiary ledger;
- Determine that the account is in balance with the total of its subsidiary ledgers;
- Review the debits and credits to analyze any unusual activity; and
- Determine the propriety of entries in each account.

Verifying source documents (such as the member share and loan trial balance or the bank statement) or actual receipts is an effective method of reviewing general ledger accounts. Normally, an examiner does not audit or verify individual entries in either the subsidiary ledger or the general ledger account, this is the work of the internal and external auditors. The examiner normally does not attempt to balance subsidiary ledgers to their general ledger accounts. Instead, the examiner should determine why the account is out of balance or unreconciled and bring the problem to the attention of the credit union officials and management both verbally and in writing using the Examiner Findings document.

The examiner may choose to perform additional examination procedures when records are out of balance or internal controls are weak. The depth of each general ledger account will vary from one general ledger account to another. The most critical elements in determining the depth of the review are:
- Account materiality - with regard to the credit union asset size and effect of the account on the credit union's capital (if a potential loss exists) and profitability (e.g. if accrued income is overstated the effect on the balance sheet could be minor while the effect on the income statement and profitability material);
- Unusual activity - is that which is out of the ordinary such as a large amount of deposits to the bank account as compared to credit union asset size, or that which might adversely affect the credit union which could include clearing accounts that do not clear to zero timely or bank accounts that are not reconciled and/or reconciling items on the bank reconciliation that are not researched and corrected quickly; and
- Quality of the external audit.

General Ledger Review Process – The examiner who is performing the review of the general ledger should perform the following steps to ensure that the financial position of credit union is fairly stated:

1. Verify that the financial statements balance and are correct by calculating total assets, liabilities, and equity.

2. Verify that each one of the balances in the financial statement concurs with a balance in the general ledger.

3. Determine that all financial reports (such as a call report) submitted to the regulatory agency since the last examination are accurate.

4. Determine the subsidiary ledgers balance with the supporting account in the general ledger. The credit union should have a subsidiary ledger for each account in the general ledger and the accountant should balance the subsidiary ledgers with their respective general ledger account no less than monthly.

5. Review the bank reconcilements for the last two months to determine that:
   - The account and any other negotiable cash account is in balance between the credit union and the bank;
   - No checks have been outstanding for more than six months, all checks are written in sequential order, and that the checks have been signed by authorized personnel;
   - Blank checks are not signed in advance;
   - Deposits are made timely and deposits in transit from the previous bank reconcilement have cleared and are accounted for both on the credit union's and the bank's records;
   - All entries to the account both by the bank and the credit union are correct and have supporting documentation;
   - All canceled and voided checks have been accounted for properly;
   - There are no suspicious checks written to creditors, members, or others;
   - All checks have been written for authorized and reasonable expenses, member withdrawals, member loans, or investments and that they have been signed by authorized individuals only; and
   - Dual controls exist on all cash transactions and wire transactions.

6. Review the entries in the Provision for Loan Loss account to determine that the accounting is proper. To that end, the examiner should ensure that the charge off loans have been approved by the board of directors and are equal to the amount noted in the board minutes and there are no other entries to the account outside of the approved charged off loans, recoveries on charged off loans, and expense adjustments to increase or decrease the account.

7. Ensure that the amount of cash on hand or in possession of the Cashier is equal to the amount stated in the general ledger.

8. Compare the investment subsidiary ledger(s) (statements received from the firms holding the investments) and ensure that the balance on the ledger(s) is equal to the amount in the general ledger.

9. Determine the Accounts Receivable balance represents funds that are 100% collectable. If not, a reserve account should be established in the amount of the potential loss.

10. Verify that the Accrued Income accounts are accurately stated. Overstatement of these accounts can have a material effect on the income statement and credit union profitability.

11. Verify that the depreciation on all fixed assets is equal to the asset lives and is reasonable. Ensure the amortization of prepaid and deferred expenses is correct.

12. Determine if there are any suspense accounts, entries or amounts in the accounting records that can not be identified. If so, the age of the entry and amount should be documented. If the unidentified entry can not be resolved during the examination and it is a potential loss, it should be reserved for or written off.

13. Ensure all entries to clearing accounts are cleared from the account in a timely fashion. Items in clearing accounts that do not clear timely are indications of accounting problems.

14. Determine if the credit union has any material contingent liabilities that could effect profitability and if they have been accounted for correctly.

15. Assess the correctness of the Accounts Payable. The account balance should represent amounts due and payable within the next 30 days.

16. Verify that the accrued dividends payable on member deposits is accurate. If this amount is understated, the effect is an overstatement of net income.

17. Determine that the amounts of member loans and shares are equal to the amount on the general ledger.

18. Ensure that the board of directors has approved all of the entries in the equity accounts and that they are in compliance with credit union law and regulatory guidelines.

19. Verify the correctness of all other accounts that are material as compared to total assets.

Signs of Warning – These signs or indicators are ratios, numbers, trends, or suspicious activity that may indicate existing or potential problems. During the review of the general ledger and the financial statements, the examiner should look for the following signs of warning:

- Continual account problems;
- Bank reconcilements that are incomplete, in arrears and/or out of balance;
- Frequent bank account overdrafts;
- Cashier(s) is out of balance between his/her record's and the general ledger,
- Lack of due control over cash transactions;
- Numerous corrections to accounting records;

- Numerous voided checks and checks written to persons or entities with no connections to the credit union;
- Large number of outstanding checks;
- Deposits in transit that do not clear within 1to 2 days;
- Checks written out of sequential order;
- Bank account deposits that are made outside of established procedures;
- Lack of a clear audit trail in the accounting records;
- No subsidiary ledgers, subsidiary ledgers that are not current and/or out of balance;
- Clearing and/or suspense accounts that do not clear to zero in a timely fashion;
- Overstated accrued income, understated accrued dividends, depreciation of fixed assets, or amortization of prepaid expenses greater than their useful lives;
- Unauthorized entries to the Provision for Loan Loss account or any of the equity accounts;
- Incorrect use of accounting forms or using accounting forms that have not been designed for the specific purpose in which they are being used; and
- Account activity that is in excess of the normal amount of transactions for the operational needs of the credit union.

Examination Workpapers – Workpapers are the written documents prepared or obtained by the examiner while performing an examination. The workpapers serve as the basis of the work performed and support the results of the examination and the opinions of the examiner. They should provide sufficient information so that the reviewer does not have to obtain any additional information from the credit union to support the conclusions, once the examination has been completed. General ledger workpapers should consist of the financial statements, the general ledger balances, copies of the subsidiary ledger balances and all examiner developed workpapers used to support and/or clarify the work performed. The workpapers should clearly state the scope and objective of the review, the account being reviewed, the date of the examination, who performed the work and the date, the general ledger balance, the subsidiary ledger balance, any differences between the balances, and appropriate notes and explanations.

An easily understandable index system should be used to organize the general ledger workpapers. All workpapers should be maintained within the regulatory agency, in a safe place, along with the final report. They should be available for review and used at the next examination.

General Ledger Deficiencies – Any problems that can not be resolved during the exam should be noted in the final report in the "Examiner Findings". This document lists operating exceptions, violations of law or regulation, unsafe and unsound policies, practices and procedures. Relatively minor or infrequent infractions should not be discussed within this document; because they distract from the more important matters. Immaterial issues should be discussed orally with the manager or appropriate employee.

When identifying a finding, the examiner should include a precise description of the problem or violation, who is responsible for correcting the problem, the specific section of the Law, bylaws, rules and regulations or other authority which the finding violates. In the event that the credit union violates more than one of the aforementioned, the examiner should cite the highest authority. Examiners should also include on this document exceptions that were noted at previous exams that have yet to be corrected. These findings should be cited under a heading of a similar nature.

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Examination Process – Investment and Cash Analysis
October 26, 2002

Credit unions continue to improve their mobilization of member savings and, in some cases, the demand by members for loans does not keep pace with the savings growth. Under this scenario the investment portfolio increases and represents a substantial percentage of the assets. This makes management's ability to wisely invest its excess funds increasingly important.

Objective of Investment Analysis – The objective of the investment analysis during an examination is to determine:

- The adequacy of investment policies, procedures, and internal controls;
- The legality of investments, as well as compliance with related regulations, accounting procedures, and other guidelines;
- The suitability of the investment and management's understanding of the investment;
- The fair value of the investment portfolio and the effect of a potential loss on the credit union's earnings and financial position; and
- That management quickly corrects investment related problems.

Scope of Investment Analysis – The extent of the examiner's review of investments will depend on:

- The quality and comprehensiveness of investment policies, procedures, and internal controls;
- The presence of illegal or inappropriate investments taking into consideration the sophistication of the credit union and management's understanding of the current investment portfolio;
- The condition of investment records;
- The volume and materiality of investment transactions; and
- The degree of problems disclosed by previous external and internal audits and/or examinations.

Examiners may reduce the physical review of investments if the credit union has not changed its investment policy since the last examination, the previous examiner or auditor noted no investment internal control weaknesses, and the credit union has not changed the investment mix substantially. If the credit union has never been examined by the regulatory agency, all outstanding investments should be reviewed.

Investment Policy Review – The board of directors of each credit union must have a written investment policy that complies with the Law, rules and regulations and other applicable laws. The Board should review and update the policy no less than annually. Each credit union should also have a monitoring and reporting program to ensure that the investment process adheres to the written policies.

Examiners should start the investment review by reading the written investment policy and procedures. Examiners should ensure that the investment policy, at a minimum, addresses the following:

- **Objectives** – Objectives balance the need for safety and liquidity against the need for yield while remaining flexible enough to respond to rapid changes in interest rates. Thus, the investment objectives should closely coordinate with internal asset-liability goals and long-range plans. In addition, officials should state the intentions regarding the securities purchased, and state whether they purchased the securities to hold to maturity, sell, or trade.
- **Permissible investments and legality** - The policy should state the types of investments that credit union management is allowed to invest in. Examiners should ensure that these investments are legal, that management has a good knowledge of the investments, and that the investment is appropriate for the size and sophistication of the credit union.
- **Diversification** - The board should also establish the maximum amount that may be in any one type of investment and the maximum maturity or term for investments. These policy elements assist in diversifying the investment portfolio and reducing the risk of concentrating funds in one type of investment.
- **Liquidity** – The board must give consideration to future liquidity needs, asset-liability management strategy, capital adequacy, and management of interest rate risk when drafting the investment policy. The policy should be flexible enough to allow for changes in the balance sheet's largest accounts – member savings and loans. Examiners should ensure that the policy addresses the liquidity needs of the credit union and that the policy is reflective of the operational environment and cyclical cash in and out flows.
- **Accountability** – The board of directors may delegate its authority for authorizing the investment of credit union funds to the manager, investment committee or third party. The examiner should ensure that the board:
    1. Investigates the integrity and financial condition of a third party prior to delegation of authority;
    2. Reduces the delegation of authority to writing and explicitly states the level of authority delegated;
    3. Understands that they are ultimately responsible for all investment decisions, the Board cannot abdicate their fiduciary responsibility to maintain a safe and sound portfolio; and
    4. Receives an investment report and reviews the investment decisions made, no less than monthly.
- **Internal Controls** – The policy should require adequate internal controls and the examiner should ensure that they are in place. Internal controls should separate the responsibilities of approving, disbursing, reconciling and accounting for investment activities.
- **Safekeeping** – The board should establish investment policies, which will protect securities held in safekeeping by a third party. A third party (bank or other financial institution) should hold all securities not in the physical possession of the credit union in a safekeeping account. Safekeeping agreements should provide that all transactions will be initiated only by an authorized employee or official of the credit

union and that funds will not be transferred until the securities are received by the credit union.

- **Reporting Requirements** – Examiners should verify that the policy requires management to report to the board monthly as to changes in the investment portfolio and ensure that management provides the Board a detailed monthly investment report. At a minimum, the report should include:
  - The name of the investment;
  - The current balance as of the report date;
  - The market value compared to the amount on the credit union's general ledger;
  - The interest rate, whether it is fixed or variable, and yield;
  - The investment maturity;
  - Who made the investment;
  - An indication of any new investments made since the last report;
  - A summary of investments by type so that officials can determine that the portfolio is properly diversified; and
  - Any comments or observations regarding the investment portfolio.

Physical Review of Investments – Examiners should use a workpaper, or similar form such as the monthly board report that includes all of the investments and correct balances as of the examination date. At a minimum, the examiner should include the following information in writing:

- Name of investment;
- Date investment was made;
- Amount of initial investment;
- Current investment balance;
- Interest rate;
- Current market value of investment;
- Who made the investment;
- Type of investment; and
- Examiner comments.

For all subsequent examinations, the prior exam workpaper should be reviewed noting any changes to existing investments such as market value. Investments made since the last examination should be noted on the existing workpaper, if information can easily be added or noted on a new workpaper.

When reviewing the investment documentation, the examiner should review the originals of all investment transactions and should ensure that: all investments are in the credit union's name, all information provided on investment documentation is the same as that on the monthly investment report, the investments comply with all aspects of credit union policy, and the individual making the investment was authorized to do so. Examiners should observe that all investments are stored in a safe, secure, fireproof location. Any differences that can not be reconciled must be included on the Examiner Finding document or, if material, in the Document of Resolution.

Examiners may review 100% of the investments in the portfolio or sample the investments in the portfolio if the credit union is large. For example – if the credit union has 100 certificates of deposit, the examiner may review a sample of ten deposits. If problems exist, examiners must then expand their analysis to determine the severity of the problem and develop corrective measures.

Investment Subsidiary Ledger Records - While all credit unions must maintain adequate investment records, the sophistication of these records will depend on the level of activity and the types of investments involved. Credit unions with a substantial portion of their assets in investments, or that have substantial investment activity, should maintain adequate individual subsidiary ledgers for each investment. The subsidiary ledger, a record of all transactions involving that security should record the following information:

- Name, type, and identification of investment;
- Par value and any premium/discounts;
- Date of issue;
- Date of maturity and if there is a call date(s);
- Date of purchase and sale;
- Current book value;
- Interest rate;
- Timing of any interest rate adjustments;
- Interest rate caps and floors;
- Interest payment dates;
- Current fair value (as of each month end); and
- Location of Document.

Examiners should ensure that total investments noted on the subsidiary ledger are equal to the general ledger amount, the subsidiary ledgers are current and that they provide officials with sufficient information to manage their investment needs.

Investment Valuation – If the credit union does not plan or can not hold an investment to maturity, then examiners should ensure that a reserve for investment losses has been established as to fully and fairly disclose the true asset size. Examiners should also compare the potential loss to the credit union's institutional capital to determine the impact the loss would have on the financial condition.

In determining the fair value of the credit union's investment portfolio, examiners may use data supplied by the credit union as of the examination's effective date, if available. If examiners doubt the data's accuracy, they should test the data to determine the accuracy of the stated fair value. This may include reviewing the business section of a newspaper for quotes or investment prices or contacting a knowledgeable third party. Material miscalculations or inaccurate disclosures of the fair value of the investment portfolio are signs of weak internal controls and requires immediate corrective action.

Foreign Currency Investments – If a credit union has investments dominated in foreign currencies, the investment policy should state the specifically approved currencies for holding foreign investments and the authorized third parties for executing these transactions.

During an examination, the examiner should determine:

1. The nature of all foreign currency investments;
2. The currency in which the investment is made is authorized under the credit union's investment policy;
3. The amount invested in foreign currency as compared to total investments;
4. The expected gross yield on the investment;
5. All of the data described above under the heading "Investment Subsidiary Ledger Records" is documented for each individual investment;
6. Foreign exchange risk is controlled through asset-liability management by funding a similar amount of liabilities in the same currency;
7. That in converting the investment to the local currency for accounting purposes, the credit union recognizes the appropriate gain or loss on conversion in accordance with International Accepted Accounting Principles.

Signs of Warning – These signs or indicators are ratios, numbers, trends, or suspicious activity that may indicate existing or potential problems. During the review of the investments, the examiner should look for the following signs of warning:

- Purchase of investments that do not meet board guidelines with respects to risk, quality, or quantity;
- Significant changes in the type, quality, or maturity distribution of the portfolio; and
- Investment returns that are well above or below the market.

Investment Deficiencies – Problems that can not be resolved during the exam, and are not material, should be noted in the final report in the "Examiner Findings". This document lists operating exceptions, violations of law or regulation, unsafe and unsound policies, practices and procedures. Relatively minor or infrequent infractions should not be discussed within this document; they distract from the more important matters. Immaterial issues should be discussed orally with the manager or appropriate employee.

When identifying a finding, the examiner should include a precise description of the problem or violation, who is responsible for correcting the problem, the specific section of the Law, bylaws, rules and regulations or other authority which the finding violates. In the event that the credit union violates more than one of the aforementioned, the examiner should cite the highest authority. Examiners should also include on this document exceptions that were noted at previous exams that have yet to be corrected. These findings should be cited under a heading of a similar nature. Issues and problems of a material nature should be addressed in the Document of Resolution.

Objectives of Cash Analysis – The objectives of reviewing cash and cash-like items are to determine that the officials and management have the following:

- Adequate policies, practices, procedures and internal controls for all phases of cash operations;
- Established guidelines within which officials and employees operate;

- Procedures for prompt corrective action when deficiencies are noted; and
- Adequate security measures for replenishment, deposit activities, and transportation of cash-like items.

Scope of Cash Analysis – The scope of the cash analysis will depend on the following:
- The quality of policies, procedures, and internal controls;
- The condition of the cash records;
- The degree and materiality of cash transactions;
- The complexity of operations; and
- The degree of problems disclosed by previous internal and/or external audits or examinations.

Examiners should design, and expand as necessary, the scope of the cash analysis to uncover major weaknesses in a credit union's cash operation. The scope should also incorporate a review of management's corrective actions taken to address weaknesses noted at prior examinations and annual audits. If examiners find weaknesses, they should expand their analysis to satisfy their concerns.

Cash and Cash-like Items – The following are cash and cash-like accounts established by the board of directors for specific purposes. The board should authorize the maximum amount for each account type:
- **Petty Cash** – Used for making incidental or small payments (purchase of a few postage stamps, coffee for the office, birthday cake for an employee, etc.).
- **Cashier Change Fund** – Established and used for processing member transactions; may vary in amount based on temporary, seasonal, and projected demands.
- **Vault Change Fund** – Replenishes the cashier's change fund; may vary in amount based on temporary, seasonal, and projected demands.
- **Bank Cash** – These accounts generally replenish the vault change fund, cover loan disbursements, and make expense payments, payroll, and large savings withdrawals that can not be met by the cashier change fund. Included in bank cash are transaction-type accounts such as checking accounts and liquid savings accounts at other financial institutions. Note – The examination procedures for bank cash are addressed under the Examination Process- General Ledger Review.

Petty Cash Review – Although the amount of the petty cash fund is generally immaterial, in cases where examiners note problems they may want to review the fund to determine that:
- The balance of the fund does not exceed the authorized amount;
- Management has physically segregated it from other cash funds and provides accountability by limiting access;
- Valid receipts (initialed by the employee making the purchase) evidence payments made from petty cash, and the sum of the funds and receipts total the authorized amount;
- Management replenishes the fund in a timely manner and records the expenses monthly;

- The Board approves any changes in the fund's balance; and
- The internal and external auditors periodically verify the fund's balance.

If examiners review internal controls and activity in the petty cash, they should design a workpaper that notes the date of the review, who performed the review, if a physical count was performed, if the amount in the fund was equal to the general ledger balance and any examiner findings or observations. Any weaknesses involving petty cash should be brought to the attention of the officials and management during the course of the exam and documented on the Examiner Findings document.

Cashier Change Fund Review – The teller change fund may represent a large percentage of cash depending on transaction volume and temporary, seasonal, and projected demands. The examiner's review of the change fund should include the following, at a minimum:

- Review of the summary for all cashier's change funds – The summary total of all the cashier's should be equal to the general ledger total for cashier change fund as of the effective date of the exam and each cashier's individual total should be a component of the total summary.
- Review at least one month of system-generated cashier activity reports that reflect the system's beginning and ending cash balances, and all cash and check transactions – The cashier end of day activity reports should balance with the next day's beginning balance for each cashier. If they do not balance, the manager and employee should initial the report and it should be noted on the report why it does not balance and in what general ledger account the difference was accounted for.
- Verification of a sample of individual cashier change funds – Examiners may verify the amount of the cashier change funds by performing a physical count. This should be performed on a surprise basis, on a day other than month-end, and all documentation included in the exam workpapers. Examiners should also review surprise cash counts by the internal and external auditors to ensure they are being executed correctly, conducted on a surprise basis, and performed periodically throughout the year on all the cashier's change funds.

In addition to the verification procedures, examiners should determine the following during the review of cashier change funds:

- The amount in the cashier change funds does not exceed the maximum established by the Board, the amount established by the Board is reasonable, and the individual teller change funds do not exceed the amounts established by management.
- Cashiers sell their excess cash (above the established maximums) to the vault.
- Management has procedures in place to immediately remove terminating cashiers' access to cash operations and to audit and restrict access to vacationing cashier's change funds.
- Cashiers are restricted by policy and computer authority from processing transactions on their own accounts and accounts of family members and relatives.
- Management restricts cashiers' computer authority, in terms of access levels, and has controls in place to identify cashier transactions by teller codes or identification numbers.

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- Management instructs employees to keep confidential their cashier log-on password and requires that passwords are changed periodically.
- Cashiers lock their drawers when they are away from their work area and secure their locked drawer in the vault overnight.
- Management restricts a cashier's access to an individually assigned drawer and uses dual controls to prevent unauthorized access to teller drawers.
- All checks or negotiable items received are cleared from a cashier's drawer daily and cashiers are prohibited from holding checks, IOUs, etc. as part of their change fund balance.
- Debit/credit memos signed by both parties evidence cash purchases between the vault and cashier drawers or between cashiers.
- Cashiers are required to balance their drawer's daily, with respect to the physical amount in the drawer as compared to the computer's end of day balance.
- All members receive transaction receipts for all business performed with the cashiers.
- Management maintains a clear audit trail by promptly and accurately recording to the general ledger all cash activity, including teller differences.
- The "bait money" is properly segregated so that cashier's do not use the funds except in the case of a robbery.
- Management maintains dual control access to night depository funds and mail, and requires the presence of both persons when removing, processing and documenting the contents.

Internal control weaknesses, cashier errors, and breaches of cash policy are generally reported as Examiner Findings. All of the findings noted should be discussed with management prior to noting them on the Examiner Findings document. If the error or problem is material (would cause a negative impact on the credit union's financial position) then it should be included in the Document of Resolution.

Vault Change Fund Review - The vault change fund generally represents the largest part of the cash amount on the credit union's premises. Because of the volume and fluctuation, the vault should be balanced daily; a physical count should be performed by the vault cashier and compared to the computer total. Examiners should review vault activity by:

- Reviewing the end of day vault change fund counts signed by the vault cashier and manager to determine they were performed daily under dual control, and
- Reviewing the vault change fund general ledger detail to ensure that the end of day counts balance with the general ledger balance and that there is no unusual activity.

Examiners normally do not perform vault counts, only when fraudulent or suspicious activities exist. The vault is normally counted by the internal and/or external auditor on a surprise basis.

In addition to the verification procedures, examiners should determine the following in their review of the vault:

- The amount maintained in the vault is reasonable for the credit union's operations;
- Management adheres to the maximum vault limit established by the Board;

- The internal and/or external auditors are performing periodic surprise vault counts;
- Management limits vault access to the vault teller only and physical access to the vault to combination and/or key;
- That the vault remains locked during and after business hours;
- Management requires dual control for opening and counting vault change fund replenishments and a signed bank receipt as evidence the cash shipment was shipped and received by a credit union employee;
- A clear audit trail is maintained by accurately recording to the general ledger all vault change fund activity and differences in the vault are either resolved timely or recorded to an expense account;
- Two part debit/credit memos signed by both parties evidence cash purchases from and cash sales to the vault;
- Policies exist that do not allow a cashier that is responsible for a drawer and the vault to co-mingle the finds; and
- That vault policies, procedures, controls, and balancing procedures provide for adequate safeguards and accountability over vault cash operations.

Any errors or problems during the review of the vault should be discussed with management and documented in the Examiner Findings. If the problem is material in nature then it should be addressed in the Document of Resolution.

Signs of Warning - These signs or indicators are ratios, numbers, trends, or suspicious activity that may indicate existing or potential problems. During the review of cash, the examiner should look for the following signs of warning:

- Cashiers that have access to other cashier's drawers;
- Cashier drawers and the vault are left open and unlocked;
- Amounts in the cashier drawers and vault are in excess of the established maximums;
- Debit/credit memos are incomplete or completed incorrectly;
- Cashier drawers are out of balance, a difference exists between the physical count and the computer system total;
- Lack of adequate dual controls when counting cash received at the credit union or counting the cashier drawers, and/or vault;
- Cashiers that transact business on their own accounts, or that of family members and relatives;
- Cashiers who reveal their computer passwords to others
- Cashiers that do not sign off the computer when away from their work area;
- Cashier drawers that are not balanced daily;
- Numerous transaction errors;
- Cashiers that do not issue receipts for each transaction they process; and
- Lack of surprise cash counts by external and/or internal auditors.

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Examination Process – Management Review
November 4, 2002

Evaluating the quality and effectiveness of management is a major examination step. This examination step is aimed more at the future than the current condition of the credit union and determines if current management is capable of responding to financial pressures and economic and local market changes. The assessment of management should not be solely dependent on the financial condition of the credit union. The quality of overall management should be evaluated by determining the effectiveness of the board of directors, the committees and operational management. The assessment of overall management should be based on reviews of the following four areas:

1. Internal Controls;
2. Management Conduct;
3. Service to Members; and
4. Business Strategy / Financial Performance.

The board approves policies that direct daily management and delegate the necessary authority to staff so they can fulfill all job responsibilities. Specifically, board and committee effectiveness can best be evaluated by reviewing board and committee minutes, the credit union's policies, the business plan and financial results.

Objective of the Management Review - Management is responsible for current operations and future planning. The objective of the review should determine that:

- Officials fully understand their duties and responsibilities and all important actions taken are documented in the minutes and policies;
- Officials are carrying out their responsibilities appropriately and are complying with laws and regulations;
- Officials have developed adequate goals and policies for all financial and operational areas;
- Conflicts of interest do not exist;
- Service to members, market penetration, and the rate structures are appropriate;
- Management is flexible, adapts to change, and keeps abreast of changes in the industry and the local market; and
- Management makes well-informed, sound decisions.

Scope of the Management Review – Depending on the size, complexity, and organizational structure of the credit union, examiners will discuss with the appropriate individual(s) or observe the following:

- Key personnel changes since the previous exam and future plans;
- Significant new programs or services and future plans;
- Significant acquisitions of new facilities and future plans;
- Computer conversions;
- Problems with the field of membership (e.g. - layoffs at a larger employer within the field of membership, strikes, etc.);
- Working relationship between the manager and the board of directors;

- Material changes in the investment portfolio and future plans;
- Material changes in the loan portfolio and future plans;
- Material changes in key policies, procedures, or future plans;
- Record keeping issues (e.g.- accounts out of balance, unreconciled accounts, etc.);
- Off-balance sheet risk areas, including lawsuits or contingent liabilities;
- Capital accumulation and maintenance strategy;
- Succession plan for key management positions;
- Systematic review of policies and procedures;
- Business plan (focusing on a 2-3 year future time frame) and the annual budget;
- Regular need for external credit; and
- Results of external and internal audit(s).

If no material changes have occurred since the last examination, examiners may use the following procedures in reviewing management:
- Scan the board meeting minutes for significant items and document in writing the review by recording material board actions only;
- Review the changes to policy and procedures made since the last examination;
- Review the credit union's annual budget, budget assumptions, and budget variance analysis;
- Review the business plan for the next 2-3 years;
- Review the committee minutes and activities only when problems are noted; and
- Review corrective actions taken to address problems identified at prior exams and audits.

All of the review steps should be documented in writing and included in the workpapers. The review should document: the area being reviewed, the scope or objective of the review, the examiner performing the review, the employee(s) who took part in the review, the results of the review, and any corrective actions needed.

Board Minute Review – The analysis of the minutes helps to draw conclusions about how officials and daily management interact and perform their job responsibilities. Much of this information can be useful in determining the adequacy of management and the effectiveness of their policies. The board minutes are vital records used to record board actions and information from board meetings. The following are considered significant actions and should be documented during the review:
- Loan policy changes;
- Agreements on collection problem loans and the approval of loan charge offs;
- Loans and savings/deposits rate changes;
- Record keeping problems;
- Discussion concerning new program proposals;
- Investment activities;
- Capital accumulation and maintenance strategies;
- Asset liability management and budget reviews;
- Financial statement reviews;
- Material fixed asset purchases;
- Loans to officials; and

- Progress towards meeting established goals and instituting corrective actions.

Minutes should be kept for all board and committee meetings along with minutes from the annual and reorganizational meetings. If meeting minutes are missing or incomplete, the examiner should discuss this with management and include it as an examiner finding.

Internal Control Review – Sound internal controls are a means of preventing fraud and quickly detecting errors. Without proper controls in place, management will not be able to identify and monitor operational risks. *Internal controls should ensure that the credit union:*

- Establishes and maintains accurate and reliable accounting and operational data;
- Properly safeguards its assets;
- Establishes adequate policies and adheres to them; and
- Enforces proper segregation of duties.

Examiners should review the following eight areas to assess the quality of the established internal controls.

1. **Information System** – It is crucial that the information system is secure and protected from unauthorized use to protect the integrity of credit union data. Examiners should ensure access is limited to those employees that work with the computer system and there is a permanent system record of employee ID access codes along with the transactions performed.

   Examiners should review all of the internal control reports generated by the system. These report names will vary by system. Examples of these reports include:
   - File Maintenance or Non-financial Transaction Report – identifies all changes made through the computer to member accounts;
   - Paid Ahead Loans Report – *identifies loans for which the credit union advanced* the due dates.
   - Supervisory Override Report – documents system overrides, based on established parameters, by personnel who have the authority to make the changes.
   - Negative Savings and Checking Accounts – identifies accounts with negative balances as of the report date.
   - Dormant Accounts – identifies accounts with no activity for more than one year (or selected time frame).

   There should be a written computer contingency plan available for review that specifically states the actions to be taken should a system failure occur. Examiners should ensure that the plan appears to be effective and that it has been tested.

   If the credit union has undergone a computer conversion since the last examination, this area of review should be expanded to ensure the credit union has adequate security measures in place and that the conversion did not adversely effect the internal control environment.

2. **Segregation of Duties** – The participation of two or more persons or departments in a transaction creates a system of checks and balances and considerably diminishes the possibility of fraud. Examiners should ensure that the credit union assigns duties so that no one person can perform a transaction from beginning to end. Examples include – a person handling cash should not post entries to general ledger accounts, a loan officer should not disburse loan funds, and those having authority to sign checks should not reconcile the bank accounts. In small credit unions with only one employee, this is more difficult to achieve. In this case, volunteers or officials should perform one or several of the steps in a transaction or the internal and/or external auditors should perform additional procedures to offset the lack of sufficient controls.

   Examiners should also determine that dual control is used wherever necessary. Accessing vaults, files, or other storage devices should require at least two keys or combinations under the control of at least two different people. Effective dual control mandates that all employees carefully guard their key or combination. Examples of items that should be under dual control include: vault cash, negotiable collateral, investment securities, safekeeping items, reserve supply of checks, unused traveler's checks, unused money orders, the night depository, mail receipts, dormant savings accounts, ATM cash, safe deposit box locks and keys, and spare teller drawer keys.

3. **Audit Program** – Every credit union should have an adequate audit program commensurate with its size. An active supervisory committee may be adequate for very small, limited service credit unions, while small to medium-size credit unions offering more than basic services should employ the expertise of an external auditor. Ideally, larger credit unions should consider a program that consists of a full-time, internal auditor reporting to the supervisory committee and an annual external audit performed by a third party.

   An effective audit function and process should be independent and report to the Supervisory Committee without conflict or interference from management. Each credit union should have an annual audit plan to ensure that all risk areas are reviewed and those of greatest risk receive priority.

   Examiners should review the annual audit plan, all reports, and any workpapers to gain additional understanding of the audit steps used. Examiners should ensure that both the internal and external audit programs are sufficient with scopes that are adequate to access the financial and operational soundness of the credit union. Upon the completion of an external and/or internal audit, a report should be issued to management and officials. Examiners should ensure that the reports are reviewed and corrective actions taken. Additionally, examiners should review the procedures of the annual member account verification. Member share and loan account balances should be verified annually and it should be performed without the participation of any operational employees.

4. **Accounting** – The accounting records of every credit union should be kept in accordance with established accounting principles. Examiners should ensure a credit union's records and accounts reflect its actual financial condition, are current, and provide an adequate audit trail. The audit trail should be clear and supported by sufficient documentation to follow a transaction from beginning to end. All general ledger account balances should balance to a subsidiary ledger that is independent of the general ledger.

5. **Protection of Physical Assets** – A principal method of safeguarding assets is to limit access to authorized personnel. Examiners should ensure that assets are adequately protected through operating policies and procedures that require dual control and that limit physical access where needed.

   Examiners should also determine that the credit union and its operations are adequately insured by reviewing all insurance documentation. The board should review the credit union's insurance coverage, at least annually, to determine it is adequate and document the review in the board minutes.

6. **Training of Personnel** – Examiners should determine that credit union staff is thoroughly trained with regards to their job duties and cross-trained in the job responsibilities of other staff positions as to enhance member service and internal controls.

7. **Succession Planning** – The on-going success of credit unions will be greatly impacted by the ability to fill key management positions in the event of resignation or retirement. Succession plans are usually only present in medium to large credit unions. Examiners should determine that a detailed succession plan exists. This plan should provide trained management personnel who are able to takeover quickly should the need arise so that the credit union's long-term stability is not adversely effected. A succession plan should address the manager or president and other senior management positions.

8. **Written Policies and Procedures** – The board of directors is responsible for the approval and revision of policies. Management usually develops the policies or at the very least makes suggestions as to what should be in the policies and presents the draft policies to the board for approval. Written policies should be present for: loans, investments, collections, asset liability management, personnel, capital accumulation, savings and deposits, and fixed asset purchases.

   Procedures describe "how" employees perform their job duties. Management and employees write the procedures and perform a review no less than annually. Procedures normally are not approved by the board. Examiners should ensure that adequate written policies and procedures are present, they are reflective of current operations and are followed by the employees. Without written policy, the employees can not provide consistent member service, as each employee will perform their job as they want, not as officials and management desire.

Management Conduct Review – The board of directors and management have a fiduciary responsibility to members to maintain high standards of professional conduct. Examiners must verify that management:

- Complies with the laws, rules and regulations, and established policies and procedures;
- Establishes appropriate compensation policies and practices for senior management. The board should have written performance standards for the manager and perform an annual written evaluation prior to salary increases, the manager should establish the performance standards for the employees and perform evaluations prior to their pay increases;
- Avoids conflicts of interest; and
- Uses professional ethics and behavior. Management should not use the credit union for personal gain and should treat each employee and member equally.

Business Strategy/ Financial Performance Review– A business plan that focuses on the next two to three years should be in place at every credit union. This plan should state the credit union's mission, it's goals and objectives, the action steps needed to meet the stated goals, and the projected financial results for the time period. The board should review, approve, and periodically revise the plan as unexpected changes warrant.

In assessing the adequacy of a business plan, the examiner should determine the following:

1. **Does the business plan have a strong foundation based on an assessment of the environment in which the credit union will operate over the medium term (next 2-3 years)?** Management should evaluate the external and internal factors influencing its business, including economic and regulatory issues, its member base, its competition, and its competitive opportunities. Credit union management should also consider different scenarios while planning such as changing interest rate environment, full employment, lay-offs, etc. The analysis should produce a set of assumptions that will be incorporated into the business plan.

2. **Is there a clear, written statement of key goals and objectives?** These goals and objectives should be realistic in regards to the credit union's analysis of the external and internal factors. The goals and objectives can be expressed in terms of income and expenses, projected balance sheet numbers, other performance indicators and/or products, services, or programs to be introduced.

3. **Are the mission and objectives incorporated with specific plans of action to attain the stated objectives and goals?** The plans of action should be accompanied by the individual(s) responsible for completing the action plan and the time frame for completion.

4. **Have projected financial statements (balance sheet and income statement) been developed for the business plan's time frame based on the mission, objectives,**

and established action plans? The projected financial statements are nothing more than a financial road map used to chart where the credit union is and where it wants to be. The projected financial statements and the underlying assumptions should be reviewed and compared to the actual results, no less than quarterly and revisions made when necessary so that the business plan is reflective of the current operating environment.

5. **Was the business plan and projected financial statements submitted to the board for their review and approval?** The review, suggested revisions, and the approval of the plan should be documented in the board minutes.

6. **Has the business plan been implemented satisfactorily?** The board is responsible for oversight of the business plan. Management is in charge of implementing the plan on the operational level. The mission, objectives, and action plans should be clearly communicated to staff at every level to ensure adherence to the business plan.

7. **Is the business plan monitored?** Periodically management and the officials should review the progress made towards achieving the stated goals and objectives and meeting the financial projections. Management should ensure that the credit union's policies and procedures and the credit union's resources (employees, capital, and equipment) are consistent with the plan and are capable of achieving the desired results.

   In addition to the business plan, management should develop an annual budget at the end of each business year for the upcoming year. The balance sheet numbers should be projected and the income statement numbers based on the balance sheet projections. All of the assumptions used to derive the numbers should be placed in writing. The board should approve the budget upon review. Periodically, the actual results should be compared to the budgeted figures and any variances discussed. Revisions should be made to the budget for any unexpected events or changes. Budgets and business plans are not mutually exclusive; each should be considered when developing the other.

Signs of Warning – These signs or indicators are ratios, numbers, trends, or suspicious activity that may indicate existing or potential problems. During the review of management, the examiner should look for the following signs of warning:

- Supervisory committee that is not independent of the board and/or manager;
- Internal audit function that reports to the board instead of the supervisory committee;
- High or increasing employee turnover;
- Regular vacations not taken, employees work late hours;
- Nepotism;
- Abuse of official position or preferential treatment;
- Limited personnel; lack of segregation of duties;
- Lack of adequate segregation of duties when the credit union is sufficiently staffed;
- Failure to provide, or delays in providing, standard reports, records, and/or documents;

- Records not maintained at the credit union;
- Management or staff provide copies of documents rather than originals;
- Inactive supervisory committee;
- Lack of, unacceptable, or non-independent audit;
- Unacceptable member account verification;
- Inadequate internal controls and information system controls;
- No internal review of computer system generated internal control reports;
- Use of external credit for inappropriate uses, or in spite of large cash balances;
- Lack of a conflict of interest and fraud policies;
- Extravagant management or employee lifestyle relative to salary;
- Inadequate or lack of board approved policies;
- Lack of, or inappropriate corrective action taken with regards to problems and issues identified by examiners and external auditors; and
- Chronic, unresolved problems.

Management Deficiencies – Issues and problems of a material nature should be addressed in the Document of Resolution. The solution to the problem or the action that needs to be taken should be noted along with the individual responsible for taking the corrective action and the time frame in which the action or correction should occur. To enhance follow-up from one exam to the next, examiners should also include on this document action plans that were noted at previous exams that have yet to be corrected. These unresolved issues should be cited under a heading of a similar nature.

Problems that can not be resolved during the exam, and are not material, should be noted in the final report in the "Examiner Findings". This document lists operating exceptions, violations of law or regulation, unsafe and unsound policies, practices and procedures. Relatively minor or infrequent infractions should not be discussed within this document; they distract from the more important matters. Immaterial issues should be discussed orally with the manager or appropriate employee.

When identifying a finding, the examiner should include a precise description of the problem or violation, the individual responsible for correcting the problem, the specific section of the Law, bylaws, rules and regulations or other authority which the finding violates. In the event that the credit union violates more than one of the aforementioned, the examiner should cite the highest authority. Examiners should also include on this document exceptions that were noted at previous exams that have yet to be corrected. These findings should be cited under a heading of a similar nature.

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Examination Process –
Institutional Capital and Profitability
November 6, 2002

Institutional capital is defined as the total of the credit union's regulatory reserve accounts, undivided or retained earnings, special reserves (designated for a specific purpose), and net income that has yet to be closed to the retained earnings account. The stronger the overall capital position, the easier it is for the credit union to deal with future uncertainties such as asset losses and adverse economic cycles.
Capital accounts exist to:

- Provide a base for future growth;
- Enable the credit union to meet competitive pressures as they arise;
- Provide protection against operating losses; and
- Ensure the credit union remains an on-going concern.

Objective of Capital Review – The examiner reviews the area of capital to determine that:

- The board has established a capital accumulation strategy that states the capital goal ratios, financial plan, and time frames for achieving the goals;
- There is sufficient capital as compared to operational risk;
- The credit union has adequate capital policies, practices, and procedures in place;
- Officials and employees follow the requirements of the law, rules and regulations, bylaws, and established guidelines;
- Activity in the capital accounts is periodically reviewed; and
- Management promptly corrects deficiencies or violations.

Scope of Capital Review – The examiner should review the capital position and the official's philosophy toward building and maintaining capital when determining the scope. If the capital position falls short of established goals and needs, the examiner should expand the review to determine if the shortfall poses a threat to the financial condition and discuss corrective action with management.

When determining the adequacy of capital and the scope of the review, the examiner should consider the following factors:

- Size of the credit union;
- Complexity of products and services offered;
- Level of management expertise;
- Involvement of officials;
- Operational risks present (interest rate risk, long-term assets, high-risk investments, etc.)
- Lack of adequate internal controls;
- Presence of sufficient insurance;
- Current and anticipated earnings capacity of the credit union;
- Quality of the loan and investment portfolios;

- Contingent liabilities;
- Compliance with regulatory reserve requirements, if applicable;
- Stability and diversity of the field of membership; and
- Concentration of loans and savings to only a few members.

If the examiner determines that the level of capital is not sufficient to ensure the credit union's long-term future, then the examiner should develop goal ratios and time frames with management and present these in the Document of Resolution.

Institutional Capital Review – In the review of the capital accounts the examiner should consider the adequacy of capital, apparent trends, and any unusual account activity. Examiners should document their review on self-designed workpapers. The workpaper should include the beginning balance (date of last exam), all entries made to the account along with adequate descriptions, the ending balance (as of the exam date), and any examiner comments.

Examiners should use the following procedures to review the capital accounts:
- Obtain the activity in all the capital accounts for the exam period;
- Ensure that the ending subsidiary ledger balances of the capital accounts are equal to the respective general ledger accounts and the account balances on the financial statements as of the examination date;
- Determine that all of the entries made to the capital accounts were approved by the board for the same amount prior to the date of the entry and documented in the board minutes; and
- Verify that all entries to the capital accounts were made in accordance with the law, rules and regulations, bylaws, and applicable guidelines.

In addition to the above, examiners should calculate the following ratios (see the discussion of the PEARLS ratios for additional information) to determine the adequacy of the credit union's capital, how it compares to similar sized credit unions, and any negative trends:
- Capital (regulatory reserves, special reserves, undivided earnings, and net income) Growth versus Asset Growth
  - Are the trends of both ratios in the same direction or opposite and is the growth of each ratio similar?
- Capital to Assets;
  - Is this ratio at least 10%?
- Total Delinquent Loans and Other Classified Assets / Total Capital;
  - Is this amount of delinquent and classified assets less than total capital?
- Solvency Evaluation; and
- Balance of the Allowance for Loan Loss account / Collection Problem Loans;
  - Is the amount of collection problem loans less than the balance of the Allowance for Loan Loss account?

Signs of Warning – These signs or indicators are ratios, numbers, trends, or suspicious activity that may indicate existing or potential problems. During the review of capital, the examiner should look for the following signs of warning:

- Entries made to the capital accounts without board approval;
- Entries made to the capital accounts for amounts different than the amounts approved in the board minutes;
- Entries made to the capital accounts by unauthorized individuals;
- Negative trends or decreasing ratios;
- Asset growth that is greater than capital growth;
- An allowance for loan loss account that is not adequate for collection problem loans;
- Consecutive operating losses;
- Adverse economic conditions that effect the member's ability to repay their loans;
- High risk investments; and
- A few members with concentrations of credit and savings.

Objective of Profitability Review – The objective of the profitability review is to determine:

- Income and expense trends;
- Adequacy of policies and procedures regarding income and expenses;
- Actual operating results as compared to the budgeted amounts and institutional capital goals;
- Sufficiency of the credit union's earnings to increase institutional capital to established goals;
- Compliance with applicable laws, rules and regulations, bylaws, and guidelines; and
- Prompt correction by management of errors or problems.

Scope of Profitability Review – The scope of the review should include a review of the Income Statement, income and expense accounts with negative trends or unusual activity, and ratios that assess profitability. If problems are detected, then the scope should be expanded so that the examiner can determine the source of the problem and develop corrective action plans.

Profitability Review – The review of profitability should include a review of the credit union's general financial condition. A credit union with weak capital requires strong, stable profitability to improve the capital position. In contrast, a credit union with a solid capital position may only require enough profitability to maintain the capital position. Other factors to consider when analyzing profitability include: asset growth as compared to capital growth, loan loss history, expense trends, growth projections and goals, and economic factors.

Examiners should document their review of profitability on self-designed workpapers. The workpaper should document the purpose of the review, the individual performing the review, the account, ratio or issue reviewed, the credit union staff member that took part in the review, and any comments or findings.

Examiners should perform the following when analyzing profitability:

- Compare the previous year's income statement to the income statement as of the exam date to determine changes in income and expense accounts and negative and positive trends;
- Review a sample of income and expense accounts with numerous transactions, large dollar transactions, suspicious activity, and/or erratic trends;
  - Determine that adequate documentation exists for expenses, the expense was approved by an authorized employee, is reasonable, and is associated with credit union business;
  - Determine that income is not overaccrued to fictitiously improve profitability; and
  - Determine that above average fee income is not due to inefficient credit union operations;
- Calculate the fundamental profitability ratios (see PEARLS ratio discussion for additional ratio information) and compare the results to credit union's of a similar size for the following: Yield on Assets, Cost of Funds to Average Assets, Operating Expenses to Average Assets, Net Income to Average Assets; and
- Discuss with management strategies to increase income or decrease expenses and note these in the Document of Resolution.

Signs of Warning – These signs or indicators are ratios, numbers, trends, or suspicious activity that may indicate existing or potential problems. During the review of the profitability, the examiner should look for the following signs of warning:

- Increasing expenses, and decreasing gross and net income;
- Erratic income and expense amounts as compared to other time periods;
- Large variances between budgeted numbers and the actual results;
- Lack of adequate expense documentation;
- Personal expenses included in credit union expenses;
- Above average fee income due to inefficient credit union operations;
- Expenses paid without proper approval;
- Profitability is inadequate to maintain or increase institutional capital; and
- Profitability is inadequate to pay local market interest rates on savings and deposits.

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Off-Site Supervision
November 13, 2002

Supervision is the ongoing monitoring of a credit union's financial and operational condition. Examiners monitor their assigned credit unions as needed through on-site examination, supervisory contacts, and off-site through submitted regulatory reports and financial statements, and periodic trend analysis of selected ratios. In credit unions with more serious financial problems, supervision may also include follow-up examinations and monthly monitoring of financial trends and ratios.

The objective of off-site supervision is to quickly identify negative trends and emerging problems and to resolve the issues before they become so serious that they could negatively effect the credit union's financial condition. Examiners should contact a credit union immediately upon the detection of a problem to ensure that management is aware of the problem. To correct the problem(s) the examiner should not only report the problem, but work with management in determining the best workable solutions to the problem.

Data Collection - Credit unions are generally required to submit financial information and/or statements to the regulatory agency on a periodic basis. The periodicity will vary depending on the credit union's problems. Newly chartered credit unions and those with severe operational problems are generally required to submit financial information monthly. The examiner that is responsible for performing the on-site supervision can perform off-site supervision or the supervision duties can be divided between on and off-site supervision departments.

Data can be collected through the use of a required regulatory form that is to be completed no less than semi-annually (data as of June 30 and December 31). This report collects the following information:

- Balance Sheet account balances for - all the outstanding loan types, Allowance for Loan Loss, Cash, Investments, Fixed Assets, Prepaid and Deferred Expenses, Other Assets, Total Assets, Accounts Payable, External Credit, Accrued Dividends, Taxes Payable, Accrued Expenses, all the savings and share types, Regular Reserve, Special Reserves, Undivided Earnings, Net Income, and Total Liabilities and Equity.
- Income Statement account balances for – Interest on Loans, Income from Investments, Fee Income, Other Operating Income, Total Gross Income, Employee Compensation, Employee Benefits, Travel and Conference Expense, Office Occupancy Costs, Office Operations Expense, Educational and Promotional Costs, Loan Servicing Expense, Provision for Loan Loss, Member Insurance Costs, Miscellaneous Operating Expenses, Total Operating Expenses, Gain on Sale of Fixed Assets, Other Non-operating Income (Expense), Interest on External Credit, Interest on Deposits, Dividends on Shares, Net Income.
- Breakout of Delinquent Loans – the number of delinquent loans and delinquent loan balances between 1-2 months delinquent, 2-3 months delinquent, 3-6 months delinquent, 6-9 months delinquent, 9-12 months delinquent, greater than 12 months.

- Miscellaneous Loan Information – loans outstanding to credit union officials and management, loans granted year-to-date, total amount of loans charged off year-to-date, and total amount of recoveries on charged-off loans year-to-date.
- Investment Information – types of investments and a maturity distribution of investments – 0-1 month, 1-2 months, 2-3 months, 3-6 months, 6-9 months, 9-12 months, 1-2 years, 2-3 years, and greater than 3 years.
- External Credit Information – types of external credit and maturity distribution.
- Savings Information – types of savings and share accounts, a maturity distribution, and the interest rates and dividends paid on the accounts.
- Off-balance Commitments and Contingent Liabilities – such as unused lines of credit (both member lines of credit and external credit union lines of credit), potential and pending lawsuits, etc.
- Miscellaneous Information – who performed the last annual audit, the effective date of the last annual audit and member account verification, the type of system used to maintain the loan and savings records of the member, the name of the software or processor used (if the EDP system is computerized), number of current members, number of potential members, number of male and female members, number of members who have declared bankruptcy year-to-date and the number of full and part time members.

This data is collected using a standardized format. Standardization is imperative to make the data useful and comparable and to eliminate individual interpretation and incorrect information. All interested parties must use the same information for the calculation and review of ratios otherwise any comparison is useless. Along with a standardized format for reporting, there should be a line by line explanation of how the report is to be completed. The individuals completing the report should be adequately trained so that they provide reliable data.

Financial data can also be collected periodically, in addition to, the regulatory report. This can be done on a case by case basis. Examiners should contact credit unions that need additional supervision (more than is provided during the annual examination and in the review of the regulatory report information described above) and advise them of the information that needs to be collected, how often it is to be submitted, where it is to be submitted, and the deadline for receiving the requested information. The information requested by examiners usually includes:

- Balance Sheet;
- Income Statement;
- Delinquency List;
- Loan Classification performed to determine the adequacy of the Allowance for Loan Loss account; and
- Breakdown of the outstanding balance for all loan and savings types.

Examiners will then use this information to perform ratio, financial statement, and peer group analysis.

Financial Statement Analysis - The financial reports, including the balance sheet, income statement and the loan delinquency report allow the regulatory agency to measure and analyze the performance of the credit union over a period of time and compare it to similar size credit unions or a peer group. This information should be entered on a spreadsheet to analyze the numbers over a given time period (monthly or quarterly). The spreadsheet should contain at least 12 months of data so that the information can be analyzed between periods and compared to similar size credit unions. Data should be maintained on the spreadsheet long enough to identify positive and negative trends, seasonal fluctuations, and any inconsistencies.

When performing financial statement analysis the spreadsheet should include the following information and all trends, fluctuations, and inconsistencies should be noted in a comments section provided at the end of the spreadsheet:

- Number of Members;
- Total Loans balance;
  - Balances for each loan type offered;
- Allowance for Loan Loss balance;
- Cash;
- Investments;
- Fixed Assets;
- Other Assets;
- External Credit;
- Other Liabilities;
- Total Share, Savings, and Deposit account balances;
  - Balance of each type of share, savings and deposit accounts offered;
- Regulatory Reserve balance,
- Special and Other Reserve account balances;
- Undivided Earnings balance;
- Year-to-date Net Income balance;
- Income from Loans;
- Income from Investments;
- Fee Income;
- Total Gross Income;
- Total Operating Expenses;
- Total Provisions for Potential Losses;
- Non-Operating Income (Expense);
- Total Interest and Dividends paid on shares, savings, and deposits;
- Interest paid on external credit;
- Net Income;
- Delinquent loan balance from 1-2 months delinquent;
- Delinquent loan balance from 2-3 months delinquent;
- Delinquent loan balance from 3-6 months delinquent;
- Delinquent loan balance from 6-9 months delinquent;
- Delinquent loan balance from 9-12 months delinquent;
- Delinquent loan balance greater than 12 months delinquent;
- Total loans charged off for the period; and

➢ Total loan recoveries for the period.

Ratio Analysis - The most widely used and effective form of off-site supervision is ratio analysis. The financial statement information is used to calculate the ratios. Financial ratios give the numbers an added dimension. Ratios allow the examiner to objectively relate two individual numbers to measure specific areas of credit union operations. Ratios can be used effectively in a trend analysis to monitor credit union performance and determine the presence of negative and positive trends and changes.

No ratio is isolated from operational changes or problems. Changes will effect various ratios, so the ratios must be analyzed with their interdependence in mind. For instance, if delinquency increases, the delinquent loan to total loan ratio will increase as long as total loans have not grown faster than delinquent loans. Interest income will decrease because interest in not being collected on time. Fees may increase if penalties are charged for late payments and are collected. Collection expenses may rise due to the costs associated with collecting loans. Net income and, therefore, institutional capital will also be adversely effected.

The ratio analysis should be performed on a spreadsheet and it may be the same spreadsheet in which the financial statement analysis is performed. The following ratios from the PEARLS monitoring system are key ratios needed to determine a credit union's financial condition:

- Allowance for Loan Losses / Delinquent Loans > 12 months – This ratio measures the adequacy of the credit union's allowance for loan loss account for all loans that are delinquent more than 12 months. One hundred percent of the delinquent loans more than 12 months past due should be provided for in this account. If the account is not adequate, a loan charge off will reduce institutional capital and the financial strength of the credit union.
- Allowance for Loan Losses / Delinquent Loans from 1-12 months – This ratio measures the adequacy of the credit union's allowance for loan loss account for loans that are between 1-12 months. The allowance account balance should be adequate for 100% of the loans greater than 12 months delinquent and at least 35% of the outstanding loan balances between 1-12 months delinquent. If the account is not adequate, a loan charge off will reduce institutional capital and the financial strength of the credit union.
- Loan Charge-Offs / Total Loan Portfolio – This ratio measures the amount of loans charged-off from the loan portfolio in the period. This ratio should be analyzed with the result of the Total Delinquency > 1 month / Total Loans ratio. The credit union could have a low delinquency ratio because loans are charged-off quickly or a high delinquency ratio because loans are rarely charged off. There are only 4 ways in which a loan can be removed from the delinquency list:
  - Paying the loan current;
  - Charging it off to the Allowance for Loan Loss account;
  - Manipulating the terms; or
  - Refinancing or extending the loan.

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- Total Loans / Total Assets – This ratio measures the percentage of assets that are invested in member loans. If the majority of assets are invested in loans, generally gross and net income are higher if delinquency, cost of funds, and operating expenses are under control.
- Savings and Deposits / Total Assets – This ratio measures the percentage of total assets that are financed by member's savings and deposits. A large percentage indicates an effective marketing program and is a good indicator that the members are saving for reasons beyond access to loans.
- External Credit / Total Assets – This ratio measures the percentage of assets that are financed by external credit. The use of external credit should be well thought out and part of the business plan. External credit should be used as an initial source of funds or short-term funding. Management should not be reliant on external credit for a medium or long-term source of funds. The receipt of external funding is often unreliable and the cost of these funds varies tremendously. These two factors could seriously effect the credit union's liquidity and profitability. Instead, management should concentrate on developing and promoting attractive savings products for its membership.
- Institutional Capital / Total Assets – This is one of the most important ratios because it measures the overall financial soundness of a credit union provided that the allowance for loan loss account is adequately funded. If the allowance for loan loss account is inadequate for potential loan losses then institutional capital will be reduced when loans are charged-off. The larger the institutional capital ratio the more capital the credit union has to absorb losses. Capital is the difference between a solvent and insolvent institution. Capital is defined as those funds within a credit union over which no person or institution has any legal claim. More specifically, capital is retained or undivided earnings, regulatory reserves, charity and donations, and net income or loss after all operating expenses, interest costs, provisions, taxes and dividends have been paid.
- Total Delinquency > 1 month / Total Loans – This ratio measures the total percentage of loans that are delinquent more than 30 days. This ratio is a very good indicator of not only the quality of the credit union's loan portfolio, but also the collection efforts. The age of the delinquent loans should also be analyzed. If there are numerous loans that are delinquent 1-2 months this could indicate:
  - The collection department is not starting collection efforts in a timely fashion;
  - An economic downturn; or
  - An adverse change in loan underwriting.
- Non-earning Assets / Total Assets – This ratio measures the percentage of the total assets not producing income. This ratio should be minimized, as these assets do not contribute to net income or institutional capital.
- Operating Expenses / Average Total Assets – This ratio measures the cost associated with the management of all credit union assets. This cost is measured as a percentage of total assets and indicates the degree of operational efficiency.
- Net Income / Average Total Assets – This ratio measures the adequacy of the credit union's earnings and its capacity to build capital. This ratio should be analyzed with the result of the Institutional Capital to Total Assets ratio in mind. If net income is

insufficient to sustain or increase capital, the credit union's survival in the future may be questionable.

- Liquid Short-term Assets – Short-term Payables / Savings Deposits – This ratio measures the adequacy of the liquid cash reserves to satisfy deposit withdrawal requests after paying all immediate obligations < 30 days. The goal of successful liquidity management is to have enough liquid funds to meet all member requests and operating expenses with any excess funds invested in interest bearing accounts and/or investments.
- Growth in Total Assets – This ratio measures the growth of total assets from one period to the next. In order to have real growth the ratio must be at least the inflation rate.
- Growth in Institutional Capital – This ratio measures the growth of the credit union's capital from one period to the next. Institutional capital growth that is the same or greater than the growth in assets insures the credit union's financial future. The more capital a credit union has the more able it is to withstand loan losses, economic downturns, costs associated with offering new member services, and financing of fixed assets. Capital can also make a credit union more profitable if operating expenses and the cost of funds are under control. There is no interest cost to attract these funds to the credit union as there is with member deposits.

(For more information on the ratios discussed above please see the information provided on the PEARLS Monitoring System.)

Peer Group Analysis – A peer group is group of similar sized credit unions. For instance all credit unions with assets less than $2 million would be a peer group. From the peer group data received peer averages can be calculated for all of the above data. Peer averages are a very helpful tool to both supervisors and credit union managers as they can take ratio analysis one step further. They can compare their financial operations and results to similar credit unions, in addition to, reviewing the trends in their operations. When using peer comparisons, examiners have to keep in mind that not all credit unions are alike even though they are in the same peer group. So there might be credit unions that have ratios that vary from that of the peer average but their operations and financial condition are sound.

Peer group ratios are normally produced by the regulatory agency. They are an end product of the required standardized data collection discussed above.

Signs of Warning - These signs or indicators are ratios, numbers, trends, or suspicious activity that may indicate existing or potential problems. While conducting off-site supervision, the examiner should look for the following signs of warning:

- Financial reports or standardized reports that are not received or received late;
- Financial reports or standardized report that are completed incorrectly;
- Management avoids examiner contacts, can not answer the questions and address concerns, and/or is evasive when questioned;
- The Allowance for Loan Loss is not adequate to cover potential loan losses;
- Management and officials do not want to increase the allowance for loan loss account as instructed;

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- Loans are not charged off when they are considered a loss and/or when they are greater than 12 months delinquent;
- Accounts Receivables balance increases over the time period;
- Accrued Interest on Member Deposits continually increases;
- Fixed assets are depreciated over a time period greater than recommended in accounting standards;
- The loans to assets ratio is greater than 85% or less than 60%;
- Savings deposits are a small percentage of total assets;
- External credit as compared to total assets is greater than 10% and is used to fund medium to long-term liquidity needs;
- Institutional capital to total assets ratio decreases or is following a negative trend;
- Delinquent loans as compared to total loans is increasing and/or the ratio is erratic over a period of time;
- Delinquency between 1-2 months increases rapidly;
- Total delinquency decreases over a short time period;
- Non-earning assets increases as a percentage of total assets above 5%;
- Operating expenses as compared to average assets is increasing and/or the ratio is greater than 10%;
- Gross Income, operating expenses, and/or net income are erratic from one month to the next;
- Fee income is greater than 25% of gross income;
- The short-term liquid assets – short-term payables / savings deposits is less than 10%; and
- Asset growth is greater than institutional capital growth.

Follow-up on Off-Site Supervision – Upon identifying a potential problem or a negative or erratic trend the examiner should contact credit union management and the on-site supervision department if the supervision aspects are separate. Contact should be made by phone first to alert management of the problem or trend. Solutions should be developed jointly with management. If the problem is serious and it persists then an on-site supervision contact should be scheduled. On-site supervision contacts differ from the annual examination as they are focused on the problem or negative trend identified. Any kind of supervision contact that is made, whether it is by phone or an on-site visit, should be documented in writing and retained in the credit union's field file. At a minimum, the following information should be placed in writing:

- Identify what prompted the contact;
- Who performed the contact and who at the credit union was contacted;
- Identify the problem;
- Determine the cause of the problem;
- Report on the present financial condition of the credit union;
- Discuss corrective action completed, initiated, or planned; and
- Outline future plans for supervision.

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Examination Process – Savings Review

November 6, 2002

Objective of Savings Review – Savings accounts are the primary source of funds for credit unions. Management must monitor the savings structure and make appropriate changes as dictated by the asset liability management analysis, member needs, and local market competition. In reviewing the savings structure, the examiner should determine that:

- Savings policies are realistic;
- The member's needs are met;
- Interest rates are competitive with the local market;
- Internal controls are adequate;
- The savings program meets all legal requirements; and
- Management takes timely, corrective action when problems are noted.

Scope of Savings Review – The extent of the examiner's analysis depends upon the complexity of a credit union's savings structure. The examiner considers such factors as the savings policy (e.g. savings and deposit terms, interest rates, maturities, fees, etc.) and the effect of the policy and practices on net income, short and long-term goals, and asset liability management. Examiners having concerns should expand the review and perform additional steps to address and resolve any concerns.

Savings Review Process – At a minimum, the examiner should:

1. Verify the general ledger savings balances and ensure that they are equal to the subsidiary ledger and financial statement balances.
2. Determine that the board of directors approves all interest rate changes (before or after the action) and the approval is documented in the board minutes.
3. Determine if any member or group of related members owns a large percentage (10%) or concentration of the savings funds.
4. Determine the different types of savings accounts offered and the total amount in each type.
5. Review the interest rates, terms, fees, and maturities on each account and ensure that they are competitive.

- If rates are below or above market, determine the reason(s) for the difference and document the information in the workpapers.

6. Compare the savings account balances by type over a 12-month period to determine negative and positive trends.
7. Compare the effective cost of savings (based on the actual interest rates advertised) to the actual amount of interest paid.
    - A significant difference may indicate that the credit union computed the interest incorrectly or overstated total savings.
8. Review the internal control procedures to ensure that employees with access to member accounts do not misappropriate the funds.
    - Each transaction performed should generate a receipt with the date of the transaction, the cashier ID number, the amount of the transaction, the balance of

the account after the transaction, and the account number and member name effected by the transaction.
- Members should be educated to request a receipt and check the transaction amount and account balance on the receipt or, in the case of a manual record keeping system, members should verify the deposit or withdrawal made with the entries in the passbook.
- All activity in dormant accounts should be reviewed to determine that the owner of the account initiated the activity.

9. Review the operational procedures for checking accounts, if applicable. The examiner should determine the extent of control over check processing, balancing, and posting, including prompt (daily) review and processing of overdrafts and any processing exceptions.

Signs of Warning – These signs or indicators are ratios, numbers, trends, or suspicious activity that may indicate existing or potential problems. During the review of savings, the examiner should look for the following signs of warning:

- Interest rates significantly above or below the local market rates;
- Concentration of savings in one account type;
- A few members own a large percentage of the savings funds;
- Management changes interest rates without board approval;
- Fees are not sufficient to offset the cost of the savings program;
- Receipts are not generated for each transaction and/or are not given to the member;
- Dormant savings account activity is not reviewed;
- Members write checks on accounts without sufficient funds and they are not returned within the required time frame;
- Check writing privileges are not denied to members who write checks without sufficient funds in their account;
- The credit union can not attract sufficient savings to fund the loan demand or attracts more than is needed for the loan demand; and
- Members obtain loans at the credit union but save at other financial institutions.

Capital, Profitability, and Savings Deficiencies – Issues and problems of a material nature should be addressed in the Document of Resolution. The solution to the problem or the action to be taken should be noted along with the individual responsible for taking the corrective action and the time frame in which the action or correction should occur. To enhance follow-up from one exam to the next, examiners should also include on this document action plans that were noted at previous exams that have yet to be corrected. These unresolved issues should be cited under a heading of a similar nature.

Problems that can not be resolved during the exam, and are not material, should be noted in the final report in the "Examiner Findings". This document lists operating exceptions, violations of law or regulation, unsafe and unsound policies, practices and procedures. Relatively minor or infrequent infractions should not be discussed within this document; they distract from the more important matters. Immaterial issues should be discussed orally with the manager or appropriate employee.

When identifying a finding, the examiner should include a precise description of the problem or violation, the individual responsible for correcting the problem, the specific section of the Law, bylaws, rules and regulations or other authority which the finding violates. In the event that the credit union violates more than one of the aforementioned, the examiner should cite the highest authority. Examiners should also include on this document exceptions that were noted at previous exams that have yet to be corrected. These findings should be cited under a heading of a similar nature.

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Internal Control Requirements

December 11, 2002

Internal controls are mechanisms, policies, and procedures used to minimize and monitor operational risks. In order to deter employees and/or members from committing a dishonest or fraudulent act the controls must be thorough and comprehensive. However, internal controls by themselves are not enough. They will be effective only if they are reinforced by the credit union's culture, policies and procedures, information systems, training, and supervision of staff.

Usually fraud is perpetrated by falsifying or altering documents, embezzling funds, omitting the effects of transactions, recording nonexistent transactions, and/or incorrectly using accounting policies and procedures. Weak internal controls not only allow for the perpetration of fraud but allow for errors and unintentional mistakes to go undetected for a long period of time. Usually, these errors individually do not represent a large amount of funds. However, the cumulative total can be material and the time needed to correct the error significant.

The primary objectives of internal controls are to:

- Safeguard assets and member savings;
- Verify the efficiency and effectiveness of the operations;
- Assure the reliability and completeness of financial and management information;
- Prevent fraud and mistakes; and
- Ensure compliance with applicable laws and regulations.

Internal controls can be broken down into two categories – accounting and administrative controls. These two categories are not mutually exclusive, some of the procedures and records involved in accounting control also apply to administrative control.

Accounting Controls - Accounting controls should provide reasonable assurance that staff performs transactions according to management's direction and their authorization level. In addition, transactions should be recorded and financial statements prepared according to accepted accounting principles. A credit union's records must reflect its actual financial condition, structure, and results of operation. Accounting controls may differ with the size and complexity of a credit union. The following controls should be part of the internal control environment and should be helpful both to inform the credit union's board and to enhance managerial effectiveness:

1. Daily Posting – Posting records daily will maintain each day's activities separate and distinct from another day's work. This makes it much easier to locate errors and make corrections. At least monthly, staff must individually prove and balance each general ledger account with its supporting subsidiary ledger, including zero balance accounts with activity during the month.

2. Subsidiary Records – No less than monthly accounting staff should balance subsidiary records such as share and loan ledgers, bank and investment statements and individual cashier records with the respective general ledger control accounts. A staff member, other than the preparer of the subsidiary and reconciliations between the subsidiaries and general ledger accounts, should review the periodic reconciliations and document their reviews.

3. Internal Reports – Credit unions should design their accounting systems to facilitate the preparation of internal reports (e.g. Non-amortizing Loans, Dormant Savings Accounts, Negative Share Accounts, etc.) necessary to review key areas of operation. A staff member who is not involved in the transactions should regularly review all of the reports. The review of the reports should be documented and any irregularities discussed immediately with a supervisory or general manager.

4. Recording of Transactions – All credit unions should use transparent accounting practices that are prescribed by accepted accounting principles to record all their transactions. The recording of transactions should be consistent from one accounting period to the next. Credit unions may not defer expenses or accelerate income for the purpose of manipulating earnings.

5. Sequential Numbering – Sequentially numbered instruments used for items such as checks, cash receipt vouchers, journal vouchers, and share certificates assists in reconciling and controlling used and unused items. Credit unions should retain unissued, pre-numbered items under dual control.

6. Audit Trail – Credit union records and systems should provide an audit trail (i.e. paper documentation) that allows for the tracing of each transaction from its inception to completion. The documentation should include the name of the individual making the transaction, the date of the transaction, how much it is for, and what general ledger accounts it effects. Some of the more common record keeping deficiencies include:
   - General ledger entries that fail to contain an adequate description of the transaction;
   - Lack of permanent and satisfactory records pertaining to cash items and overdrafts;
   - Teller cash sheets that do not contain adequate details;
   - Investment subsidiary ledger that fails to list all necessary information;
   - Bank account reconcilements that are not current or fail to reflect the description and disposition of outstanding items;
   - Inadequate details concerning debits and credits to the cash account;
   - Correcting record keeping errors by erasing instead of crossing through the error;
   - Numerous corrections each month;
   - Failure to make daily postings to the accounts and records;
   - Failure to promptly close the books each month; and
   - Failure to review exception and other internal control reports.

7. Audit Program – Every credit union should have an adequate audit program. An active supervisory committee may be adequate for small, limited service credit unions, while medium-sized institutions offering more than basic services should employ the expertise of an external auditor to perform the annual audit. The supervisory committee can perform the account verification and internal audit functions. Ideally, larger credit unions should consider a program that consists of a full-time internal auditor reporting to the supervisory committee and an annual external audit performed by an independent third party accounting firm.

   The scope of the internal audit depends on the size of the credit union and the number and complexity of the services offered. Because of cost constraints, many credit unions can not afford a full-time internal auditor. In this case, periodically the supervisory committee can perform: bank reconcilements, cash counts, review of employee and official's loans, review of activity within accounts designated as dormant, and review of expenses and the supporting documentation.

Administrative Controls – Administrative control is a managerial responsibility that directly affects the success or failure of the credit union. These controls establish lines of authority and responsibility, segregate the operating and recording functions, and provide for the hiring of qualified employees.

Although the uniqueness of each credit union defies one set of internal controls for all, an effective plan for administrative control should contain the following at a minimum:

1. Accounting System – The board should adopt an accounting system that is flexible in its capacity and rigid in its controls and standards. The system should provide timely, accurate, and useful data to all employees. All staff should be adequately trained on the system prior to performing transactions that affect general ledger and member accounts.

2. Written Policy and Procedure – Credit union policy is established by the board to direct operations and establish clear limits and authority. Operational staff develops procedures, they are normally not approved by the board. Procedures describe "how" to do a job. Regardless of the credit union's size, written policies and procedures are imperative. Policies and procedures let all employees know what is expected of them, how they should perform their job duties, and what the consequences are if they do not perform them as required. Written policies and procedures also enable the credit union and its employees to treat each client consistently. These policies and procedures should be included in a regularly updated operations manual. The manual should clearly define the steps required for each transaction, explain how to handle exceptions, and delineate lines of authority. Employees should be required to review all policies that pertain to their position during initial job training and annually thereafter.

3. Board Approval and Monitoring of Information – In addition to policy, the board establishes control and direction through the annual budget and the longer-term

business plan that they are a part of developing, approving, and reviewing on a periodic basis. The board should request, at least monthly, the following reports to monitor the financial condition of the credit union:

- Balance Sheet;
- Income Statement;
- Cash Flow and Liquidity Analysis;
- Comparison of Actual Results to Budgeted Figures;
- Outstanding Investments;
- Delinquent Loans; and
- Savings and Lines of Credit Overdrafts.

4. Cash Control – Cash is the most liquid and accessible asset to most employees. As such, controls to prevent the conversion of this asset by officials or employees for their own personal use should be established. Adequate cash controls include:
   - Surprise cash counts that are performed routinely;
   - Cashiers that are required to balance the contents of their cash drawer with the general ledger total daily, additionally, cashiers should not be allowed to leave the credit union until the drawer balances or the difference has been recorded as income or expense;
   - Cash limits established for the total amount that can be kept on the credit union premise, in the vault, and in each cashier's drawer;
   - Limited access to the vault and cashier drawers to those individually responsible for the funds in the vault or drawer;
   - Immediate verification under dual control of cash upon receipt;
   - Counting of cash under dual control if tellers buy or sell funds to the vault or another teller;
   - Documentation of all transactions made by and between cashiers with a receipt;
   - Vault and cashier drawers equipped with adequate, functioning, locking devices; and
   - Prohibiting cashiers and employees to transact business on their own accounts or those of related persons.

5. Segregation of Duties – The participation of two or more persons in a transaction creates a system of checks and balances and reduces the opportunity for fraud considerably. The credit union should assign duties so no one person dominates any transaction from beginning to end. For example – A person handling cash should not post to the accounting records; a loan officer should not disburse loan proceeds for loans they approved; and those having authority to sign checks should not reconcile bank accounts. In situations where this separation of duties is not possible, because of a limited staff, the supervisory committee should perform additional procedures to offset the lack of adequate control.

6. Dual Control – Accessing vaults, files, or other storage devices should require at least two keys or combinations under the control of at least two different people. Effective dual control mandates that all employees carefully guard their key or combination;

thus, only collusion can bypass this important control feature. Examples of items that should be under dual control are: vault cash, negotiable collateral, investment securities, reserve supply of checks, unissued travelers' checks, credit cards and money orders, the night depository, mail receipts, ATM cash, dormant savings accounts, and spare keys to cashier drawers.

7. Protection of Assets – A principal method of safeguarding assets is to limit access to authorized personnel only. Protection of assets can be accomplished by:
   - Developing operating policies and procedures for cash control;
   - Establishing dual control over cash;
   - Conducting periodic physical inventories of credit union assets;
   - Protecting assets by purchasing adequate insurance;
   - Requiring the use of passwords to access the computer system and changing passwords no less than quarterly; and
   - Limiting physical access to cash and the computer system.

8. Zero Tolerance – The credit union should have a culture that supports internal controls and does not tolerate excessive errors or fraud. These values can be promoted by establishing:
   - Severe consequences for fraud that are written, conveyed verbally, and strictly followed. All fraudulent acts should be met with swift and permanent action;
   - Clear negative consequences for staff with excessive error rates;
   - A performance based incentive system that rewards high productivity and low error rates;
   - Competitive salaries that reduce the motivation to commit fraud; and
   - Training that explains the reasons behind internal controls and emphasizes how fraud and errors hurt the institution and its members.

9. Personnel Policies – Personnel policies should specifically state the consequences for fraudulent acts and excessive errors so each employee understands the ramifications of such actions. Employees should be familiar with the personnel policy; a review of this policy should be part of each employee's initial training. The policy at a minimum should:
   - Require management to check references of prospective employees;
   - Include written position descriptions that define the duties, responsibilities, and performance standards for each position; and
   - Require written performance appraisals of all employees annually.

10. Rotation of Personnel – From time to time, employee job functions should be rotated unannounced. The rotation should be of sufficient duration to discover any fraud. Besides being an effective internal check, rotation of personnel is a valuable aid in the credit union's overall training program as employees learn how to perform other jobs. The cross-trained employee can substitute when other employees take vacations, are absent, or are rotated.

11. Succession Planning – The on-going success of credit unions will be greatly impacted by the ability to fill key management positions in the event of resignation or retirement. Succession planning should address the general manager and other senior management positions. The existence of a detailed succession plan that provides trained management personnel to step in at a moment's notice is essential to the long-term stability of a credit union.

12. Mandatory Vacations – Credit unions should have a vacation policy that requires all employees to take at least 5 consecutive working days off. During this time they should have no access to credit union records. An uninterrupted work schedule frequently is needed to embezzle funds unnoticed.

13. Quality Control – The board of directors should establish a review process, also known as internal auditing, to determine that management and staff comply with credit union policies and procedures.

Signs of Warning – The following are possible indicators that internal controls are not adequate to discourage dishonest or fraudulent acts. Credit union officials or management should take corrective action to reduce the chance of fraud. Regulatory authorities should address these shortfalls with the officials and management and develop plans to enhance internal controls.

- Little or no internal controls in place;
- Inadequate segregation of duties with limited internal controls in place;
- Inactive supervisory committee;
- Unacceptable or lack of external audit or member account verification;
- Numerous record keeping problems;
- Accounting records and financial statements in arrears;
- Management reports and accounting records destroyed or missing;
- Employees or officials with financial problems;
- Multiple family members or related parties control operations;
- Inadequate or no review of internal control reports provided by the computer system;
- Computer entries do not identify the employee that performed the transaction;
- Employees share their password with other individuals;
- The computer system lacks adequate controls and audit trail and it is easily manipulated;
- High employee turnover; and
- Poorly trained staff.

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Regulatory Standards

December 10, 2002

The credit union law is the ultimate legal authority. It is usually general in nature. The legislative body that makes law within a country must approve any changes. This is usually a very slow process. For this reason, specific operational, financial, and administrative issues are usually addressed in bylaws and rules and regulations. The bylaws and rules and regulations are usually drafted, amended, and revoked by the regulatory authority. The law should grant the regulatory body the authority to supervise credit unions through the issuance of model bylaws, rules and regulations, and prudential standards.

To facilitate credit union organization and supervision the regulatory agency frequently makes available to all potential credit unions a set of standardized or model bylaws. Model bylaws serve as a guide in drafting a credit union's individual bylaws. Bylaws, at a minimum, define:

- the credit union's field of membership,
- the requirements for membership,
- the scope of the credit union's activities,
- the services a credit union can offer, and
- the duties and responsibilities of its officials and operational management..

Rules and regulations are established by the agency charged with the supervision of credit unions. These prudential regulations are extremely important and establish minimum operational requirements. Rules and regulations should be drafted specifically to address credit union operations and their mutual-based ownership structure. Regulators should ensure:

- that adherence with the rules and regulations is not overly burdensome for the credit unions or its members,
- they are appropriate for the size of the institutions regulated, and
- they are clear and understandable.

To effectively regulate and supervise credit unions, prudential regulations should be developed that address, at a minimum, the following areas.

Capital Adequacy – Capital adequacy requirements are the single most important regulatory requirement for the effective management of risk taking by financial intermediaries. This regulation normally specifies that a credit union should maintain an institutional capital to total assets ratio of at least 10%. Institutional capital is defined as regulatory reserves, other reserves, monetary donations and grants, undivided earnings, and year to date net income that has not been closed to undivided earnings. Ownership shares should not be included as institutional capital. These shares are withdrawable upon membership termination and in some cases can be used to secure a loan. Shares should only be considered capital if they cannot be withdrawn by members and the funds are available to absorb losses.

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Asset Classifications/Allowance for Asset Losses - Capital adequacy and provisioning for asset losses can be addressed in separate regulations or together in one regulation. A credit union can have a respectable institutional capital ratio, but be insolvent if the allowances for assets losses are not adequately funded for potential losses. Allowance accounts are used to fully and fairly disclose the true financial condition of the credit union.

Credit unions should be required to fully fund the allowances for investment, loan, and other asset losses for all potential losses. No less than monthly, management should determine that the allowance accounts are adequate. Management can determine the adequacy of the allowance account by estimating the potential loss based on current information (value of collateral securing the loan, member's current ability to repay, market value of investment, etc.) or the regulations can establish the amount or percentage to be classified based on loan delinquency or the age of the assets.

The allowance accounts are funded through an expense account. If recently identified potential losses increase substantially in an accounting period, the credit union may show a net loss, if gross income is not sufficient to cover the expense increase. Because a net loss will be shown, many credit unions do not adequately fund the allowances. The regulation should not permit this to happen.

Licensing and Entry Requirements – The process to be followed to apply for and receive an operating license should be specifically addressed in regulation. This will help both the individuals and the regulators. All parties will know exactly what is required. The regulation should include:

- the education and background requirements for founding members and officials;
- required documentation to apply for a license;
- minimum institutional capital;
- minimum number of members and any other entry requirements;
- requirements for the management information system; and
- reasons for the denial of a license.

Currently regulations addressing entry requirements are minimal in most countries. It is not uncommon to have 20 or fewer individuals starting a credit union with only a small amount of capital.. This has led to a large number of institutions that can not offer their members the services they want and are unable to compete financially because they do not have the economies of scale. Licensing such institutions that can not demonstrate sustainability is a mistake and a burden on the agency in charge of regulation and supervision. Prior to licensing any credit union, the regulator should be satisfied that the institution would be viable. Groups applying for a license should have to prove their economic viability through a business plan that is supported by written assumptions, survey results, and initial membership numbers that meet the required minimum.

Liquidity Risk – In many countries credit unions do not have access to a liquidity facility. Because of this credit unions are subject to severe liquidity risks. To confront liquidity risks many credit unions have developed centralized liquidity pools. These pools are adequate to meet demands posed by seasonal liquidity needs in individual credit unions. They are not adequate to meet liquidity risk on a larger scale. To strengthen the liquidity position of credit unions, regulations should establish minimum liquidity standards. Liquid assets can be measured against total assets or total deposits. Total deposits are frequently used to ensure there is adequate liquidity for satisfying member withdrawal requests. If there is a shortfall of liquidity, the granting of loans and the payment of expenses can be slowed but this tactic does not work with member withdrawals. If a member learns that they can not access their funds this could cause panic among the members and loss of confidence in the credit union. The goal ratio for liquid assets as compared to total deposits is between 10% and 15%.

Fixed Assets – The total value of fixed assets should be restricted so that credit union funds are invested in productive rather than non-productive assets. Investments in fixed assets can be limited to the amount of capital or a percentage of assets. Often fixed assets are limited to 5% of total assets, unless a waiver is obtained from the regulator. For small or newly chartered credit unions, there will have to be some exceptions to this rule because total assets are limited; and the purchase of information systems, office space or other assets might be a necessity. The regulator should grant these waivers or exceptions on a case by case basis.

Member Loans and Portfolio Diversification – Member loans are the credit unions largest asset. To enhance the quality of loans the regulation should state:

- the maximum maturity for any member loan;
- acceptable types of credit;
- interest rate maximums;
- if fixed and variable interest rates can be offered and fees and penalties assessed;
- if variable loans are offered, the allowable index or basis to be used for calculating variable interest rates;
- requirements and restrictions for accepting collateral;
- who approves the official's and management loans; and
- the items and issues to be addressed in the loan policy and who is responsible for developing the policy.

Prudential regulation should also address the diversification of risk within the loan portfolio by limiting the concentration of loans granted to individuals and groups of related individuals. Frequently, the total amount of loans allowed to any one member or group of related members is limited to no more than 10% of assets and the total amount of unsecured loans is limited to 10% of institutional capital.

Calculation of Loan Delinquency – It is important that certain processes are standardized within a credit union so that data generated and received by the regulator is valid, useful, and allows for comparisons between institutions. The loan delinquency calculation should be standardized. In order to do this, a regulation should specifically state:

- when a loan is considered to be past due;
- the entire loan balance is considered delinquent, not just the delinquent amount;

- how loan delinquency is calculated; and
- what delinquency information should be reported to officials and the regulatory agency. Useful delinquency reporting includes:
  - member name,
  - account number,
  - date the loan was made,
  - the original amount of the loan,
  - the current loan balance,
  - when the last loan payment was received and if it was a full payment,
  - the loan collateral and value, and
  - delinquency categorized as between 1-2 months delinquent, 2-3 months delinquent, 3-6 months delinquent, 6-9 months delinquent, 9-12 months delinquent and greater than 12 months.

External Credit – The amount of external credit should be strictly limited; it should only be used to meet short-term liquidity needs or long term financing. External credit changes an institution's focus from savings mobilization to a dependence on borrowed funds, and frequently has a negative impact on profitability because the interest rate is higher and terms are dictated by outside sources. If external credit is to be used, the amount, maturity, interest rate, and the reasons for its use should be addressed in the business plan. If the use of external credit fits within the credit union's business plan, it should be limited to no more than 10% of assets. There should be a definite "exit strategy" so that a credit union does not become dependent on the funds or "held hostage" by the terms of the credit.

Investment Activities – Credit unions are chartered to meet member savings and credit needs; because of this the type of permissible investments outside of member loans should be closely regulated. Regulation should state: the types of investments that a credit union may and may not invest in, the board of directors investment responsibilities, the general practices and procedures that must be followed in conducting transactions, how the risk is to be monitored for investments made, and the method used to value investments periodically.

Standardized Accounting – Credit unions should be required to use standardized accounting procedures, including a standardized chart of accounts. Full and fair disclosure of the balance sheet should be required so assets are not over or understated. Without standardized accounting, it is impossible for a regulator to determine the financial safety and soundness of an institution or compare the financial performance amongst credit unions.

The calculations used for loan and savings interest should be standardized and addressed in regulation so net income is not over or understated. In addition, the regulation should not permit loan interest to be accrued when a loan is more than 2 months delinquent or the repayment in full of principal and interest is not expected, no matter if the loan is delinquent or not. If the interest accrual is not discontinued, gross income can be seriously overstated.

External Audits – An annual audit performed by an independent third party should be mandatory for all credit unions. There are several options for the selection of an individual or organization to perform the audit. Credit unions, through their supervisory committees may:

- choose any auditor, preferably one who is affiliated with the national professional auditing association;
- choose only those auditors that are authorized by the regulatory authority; or
- select the auditing services provided by the credit union association.

In some countries the supervisory committee is allowed to perform the annual audit. This should only be allowed in small credit unions with cost constraints. This is not a preferred method; committee members rarely have the expertise or related experience and the spare time needed to perform an acceptable audit.

Regulation should allow the regulatory authority to request that an audit be performed again if it is found to be unacceptable.

Multipurpose Cooperatives – Financial intermediation carried out by cooperatives should be restricted to specialized institutions. Credit unions should be specialized in and credit department. It is difficult enough to run a purely financial cooperative (that is, a credit union) well without introducing the complications and distractions of additional business lines.

Nonmember Deposits – As a result of credit union ownership structure and the implications that this has for the prudential management of the institution, deposits from nonmembers should be prohibited. Transactions with nonmembers call into question the entire notion of a mutual ownership structure. Such transactions also undermine the single most important stabilizing element, the vigilance of depositors who are active within the credit union and concerned about the safety of their savings.

Records Preservation Program – Each credit union should be required to implement and maintain a records preservation program to identify, store, and reconstruct vital records in the event that the records are destroyed. The regulation should identify:

- the individual responsible for the implementation of the program;
- how often the records should be stored;
- what records are considered vital;
- what is an acceptable medium for record storage; and
- the need for a log to be kept that documents what records were stored, where they were stored, when they were placed in storage, and who sent the records to storage.

Voluntary and Involuntary Liquidation and Merger – From time to time credit unions may encounter serious weaknesses or changes in a credit union's membership group, its own leadership, or the regional economy in which it operates that force the credit union to restructure itself or to cease operations completely. Voluntary liquidation and merger is used as long as the credit union is solvent. Involuntary liquidation and merger is used in the case of credit union insolvency, when the action must be taken to reduce member losses and the impact on public confidence in the credit union system. Regulation should specifically state the process that the credit union and the regulatory authority must follow to liquidate or merge after the appropriate approval has been received.

Supervisory Body Sanctions – There are numerous administrative actions that can be taken by a regulatory authority. An administrative action may be necessary if:
- Management is involved in unsafe or unsound practices that place the credit union assets and member deposits at risk of loss;
- The credit union has committed a serious violation of law, bylaws, or the rules and regulations;
- Management makes no attempt to correct serious problems; or
- Management or officials are unresponsive or unwilling to take the necessary corrective actions discussed during previous examinations or contacts.

Regulation should identify the: various administrative actions, basis for their issuance, authority given by the action, additional actions to be taken if the action does not have the desired effect, process used to follow up on assessing the compliance with the action, and circumstances under which the administrative action can be terminated. Administrative actions usually include the following (listed by degree of severity):
- Letter of Understanding and Agreement;
- Cease and Desist Order;
- Monetary Penalties;
- Removal of Officials;
- Prohibitions;
- Establishment of Special Reserves;
- Conservatorship;
- Merger;
- Liquidation; and
- Revocation of License.

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Administrative Actions

December 12, 2002

Administrative actions are those actions that the regulatory authority can take or enforce against a problematic credit union in order to reverse negative trends or operational results, remove officials, or take over management of a credit union. Generally these actions are time consuming and expensive. Examiners working with a problem credit union should try to resolve problems through off and on-site supervision. Often problems can be resolved and the necessary changes affected through a well-written Document of Resolution that is a part of every annual examination.

The Document of Resolution (DOR) is the key document for problem resolution within the examination report; it lays out the groundwork for corrective action. Examiners develop the DOR jointly with officials and management. The DOR should specifically state the corrective action needed to solve the problem, the individual responsible for correcting the problem, and the time frame in which the problem should be resolved. If the problems can not be resolved through the DOR and extensive supervision then there are numerous actions that can be taken based on management and official's abilities, effectiveness, and willingness to make the necessary changes.

In deciding what action to take the examiner, along with their supervisor, should consider the following:

- Financial condition of the credit union;
- Interests of the membership;
- Interest of management and officials in the continuation of the credit union;
- Ability of management and the officials to manage the credit union effectively; and
- Local economic conditions.

Letter of Understanding and Agreement – The Letter of Understanding and Agreement (LUA) is the least serious of the actions that can be taken and is used when the DOR proves ineffective. The LUA, similar to the DOR, should describe all of the corrections to be made, who is responsible for making the corrections, and the time frames in which the corrections are to be made. If a credit union has a serious loan delinquency problem, an LUA item to address the delinquency might read this way:

- Reduce the delinquent loan to total loan ratio to:
  - 8% by 12/31/02
  - 6% by 3/31/03
  - 5% by 6/30/03
  - Maintain the ratio at no more than 5% for the long term.
  - Responsible party – Head of Lending/Head of Collections.

The LUA, unlike the DOR, will be addressed to the board of directors of the credit union. It will be drafted and signed by the head of the credit union regulatory body and the examiner in charge of the credit union's supervision. Upon presentation and review of the LUA, the board of directors and credit union manager should sign and date the document. The LUA should clearly state that if the necessary corrections are not made then the regulatory authority can take a more forceful action to safeguard the credit union's assets.

Examiners should make regular on-site supervision contacts to all credit unions with an LUA. During each supervision contact, the examiners shall determine and document credit union compliance with the LUA. Compliance should be assessed by discussing each LUA item with management and the officials. They should have a definitive plan in place to address each problem identified. The LUA should be removed only upon correction of all material issues addressed in the document. Removal of the document should be approved by the head of the credit union regulatory body.

Cease and Desist Order – The Cease and Desist Order (C&D) is more serious in nature than the LUA. A C&D allows resolution of problems in a solvent credit union while preserving and strengthening the credit union's managerial and financial integrity. A C&D is usually effective in compelling the credit union to take the needed action. If, however, examiners believe that issuance of a C&D order would not affect compliance, they should consider an alternative administrative action.

C&Ds are frequently used if a credit union is:

- Engaging in or has engaged in, or the examiner has reasonable cause to believe that the credit union or the persons involved are about to engage in, an unsafe or an unsound practice in conducting the business of the credit union; or
- Violating or has violated, or the examiner has reasonable cause to believe that the credit union or persons involved are about to violate a law, a bylaw, or a rule or regulation issued by the regulatory authority.

A C&D is useful and effective because it allows the regulatory authority to stop a current harmful practice or anticipate and prevent harmful practices from occurring. Although a C&D normally resolves a persisting or recurring problem, the regulatory authority may use a C&D for a first time problem that could seriously affect the credit union's operations and where the officials have indicated they will not take corrective action.

The C&D will state the specific action that shall be ceased, the individual(s) that is to cease from doing the action, and identify the time frame in which the action is be ceased. The C&D is more negative in tone than the LUA. If the credit union has a serious agricultural loan delinquency problem, the C&D item to address the delinquency problem might read in this way:

- Cease making loans for agricultural purposes and/or secured by agricultural collateral immediately and until further notice.
- Responsible party – General Manager/Head of Lending

The C&D should be drafted and signed by the head of the credit union's supervisory body and the examiner in charge of the credit union's supervision. The C&D will be addressed to the credit union's board of directors. Upon presentation and review of the document, the board of directors and general manager should be required to sign and date the document. The C&D becomes effective upon delivery and signing by the officials and remains effective until all actions addressed in the document have been resolved or a more forceful action is taken because of noncompliance. The C&D should clearly state that the regulatory authority may at any time take a more forceful action to safeguard the credit union assets.

Examiners should make regular on-site supervision contacts to all credit unions with a C&D. During each supervision contact, the examiners shall determine and document credit union compliance with the C&D. Compliance should be assessed by discussing each C&D item with management and the officials. It should be clear by management's actions that all required actions have been ceased. The C&D should be removed only upon compliance with all material issues addressed in the document. Removal of the document should be approved by the head of the credit union regulatory body.

Monetary Penalties – The credit union law should grant the regulatory authority the right to assess monetary penalties. Usually there are different penalty amounts depending on the severity of the action committed. For example:

- Level One – Any credit union that violates a law or regulation, an LUA, a C&D, submits late or substantially incorrect reports to the regulatory authority can be fined no more than ______________________.
- Level Two – If a credit union commits any of the violations described in level one, exhibits reckless conduct or a breach of fiduciary duty and the violation, practice, or breach is part of a pattern of misconduct, or causes more than an minimal loss to the credit union the regulatory authority may assess a penalty not greater than ______________________.
- Level Three – Any credit union that knowingly commits any of the violations described in level one, knowingly engages in unsafe or unsound practices, breaches any fiduciary duty or knowingly or recklessly causes a substantial loss to the credit union may be assessed a penalty by the regulatory authority not greater than ______________________.

The Monetary Penalty Order should be addressed to the board of directors of the credit union and drafted and signed by the head of the credit union supervisory body and his/her superior. It should specifically state the reason for the penalty, the amount of the penalty, when and where the penalty is to be paid, and the actions the credit union may take if they do not agree with the penalty.

Removal of Officials – The credit union law should grant the regulatory authority the right to remove members of the board of directors, credit committee, and supervisory committee. The removal of an official by the regulatory authority is used when the official will not voluntarily resign. Any party who has been removed or suspended from office is also automatically removed, suspended, and prohibited from participating in the affairs of any financial institution without the written consent of the regulatory authority.

The regulatory authority can remove an official from office when they have:

- Directly or indirectly violated the law, bylaws, or rules and regulations;

- •• Engaged or participated in any unsafe or unsound practice in connection with the credit union, or
- •• Committed or engaged in any act, omission, or practice which constitutes a breach of fiduciary responsibility, and

Because of the violation, practice, or breach described above:

- •• The credit union has or will suffer financial loss or other damage;
- •• The interest of the members have or could be prejudiced, or
- •• The party receives financial gain or other benefits because of the violation, practice, or breach, and

Such violation, practice, or breach:

- •• Involves personal dishonesty by the party, or
- Demonstrates the party's unfitness to serve the credit union or to participate in its affairs.

The notice to remove an official from office should be addressed to the credit union and the official to be removed. The notice should be signed by the head of the credit union supervisory body and his/her superior. It should contain a specific statement of facts constituting the grounds for removal and that this removal is immediate. The official to be removed may, if allowed by local law, have the right to bring the matter before the court if they do not agree with their removal by the supervisory authority.

Prohibitions – A prohibition action is similar to, but broader in scope than a removal action. A removal action removes a person from a specified official position in a credit union, while a prohibition action stops any institution-affiliated party from participating in the affairs of a credit union. Because credit union affiliated parties are not always elected or appointed officials, they may not always be removed as officials. Instead, the regulatory authority must prohibit them from further participation in the affairs of a credit union.

If permitted in the credit union law, the regulatory authority may prohibit any individual seeking to be an official from participating in credit union activity and affairs if it is found that the individual has been charged with a crime involving monetary loss, fraud, breach of contract, or a crime that may pose a threat to the interest of the credit union members or threaten to impair public confidence in the credit union.

The regulatory authority may also recommend to all credit unions that they not do business or discontinue doing business with any individual or legal entity that has been charged with any of the crimes discussed above. If the credit union wants to do business or continue to do business with such prohibited parties, they must provide the regulatory authority with written justification and receive approval from the supervisory authority prior to transacting business or continuing to do business with the prohibited party.

The Prohibition Order should be addressed to the credit union and the prohibited party and drafted and signed by the head of the credit union regulatory body and his/her superior. It should state specifically the reason(s) for the prohibition and that it is immediate. If the prohibited party does not agree with the action taken against them, they may bring the matter before a court if allowed by local law.

Establishment of Special Reserves – The regulatory authority, if permitted by law, may require a credit union to establish special reserves to protect the interest of credit union members. The special reserves are designed to prevent further deterioration of a credit union's financial condition.

Special reserves may be necessary:

- when the established reserves do not provide sufficient protection against a condition that threatens the credit union's soundness; or
- when the regulatory authority believes that the credit union may avoid establishing sufficient reserves by refinancing or extending loans or intentionally misrepresenting facts that, if properly disclosed, would have a material effect.

The order should be addressed to the credit union's board of directors and drafted and signed by the head of the credit union supervisory body and his/her superior. It should state the specific reason for the reserve, how the reserve is to be established and maintained in the accounting records, the amount of the reserve, and that the reserve should be established immediately. The reserve may only be removed from the accounting records upon approval by the head of the credit union regulatory body and his/her superior.

Conservatorship – Conservatorship is the procedure whereby the regulatory authority takes immediate possession and control of a credit union's business and assets and may operate the credit union until:

- the regulatory authority permits it to resume business on its own, subject to any terms and conditions the regulatory authority may impose; or
- the regulatory authority merges or liquidates the credit union.

When deciding to establish conservatorship the regulatory authority should consider the probability of improving the financial condition of the credit union to a level that is sustainable without outside assistance and the possibility of retaining a large part of the membership, assets, and liabilities of the credit union.

A conservatorship allows the regulatory authority to influence more actively the operations of a credit union to reduce any further dissipation of assets. Conservatorship is a useful tool when:

- the credit union violates legislation or rules and regulations of the regulatory authority;
- unsafe or unsound business practices exist;
- there is willful and continuous failure to comply with requirements or instructions issued by the regulatory authority;
- credit union management refuses to submit required or requested reporting documents to the regulatory authority;

- management has abandoned the credit union or is totally incapable of coping with severe financial problems that should be immediately brought under control;
- evidence exists of illegal or unsafe practices but the activities can not be readily identified;
- the credit union member's interests need protection;
- the credit union has willingly violated previous orders or actions taken against it by the regulatory authority;
- management conceals or refuses to make available the books and records for an examination; or
- deposit insurance funds are at risk (if a fund exists).

Ideally, a conservatorship will result in the credit union being returned to the member's control.

The Statement of Conservatorship should be addressed to the credit union's board of directors and drafted and signed by the head of the credit union regulatory body and his/her superior. The statement should state:

- grounds for conservatorship;
- the name of the individual or custodian that will be in charge of managing the daily affairs of the credit union until the conservatorship is terminated;
- the starting date and duration of the conservatorship; and
- any restrictions on the custodian's powers.

Effective from the moment the conservatorship is ordered by the regulatory authority the powers of executive management, the board of directors, and the general meeting of members are suspended and transferred to the custodian. In addition, the credit union should be required to suspend all transactions and business until the custodian is in charge of operations. Management of the credit union should be obliged to hand over all forms, seals, stamps, items of value, keys, as well as any other credit union property and documents.

Depending on local law, the regulatory authority's conservatorship may be able to be appealed before a court.

Mergers – Mergers can be both voluntary and involuntary. A voluntary merger is performed in a solvent credit union and initiated by an affirmative vote of the membership. A voluntary merger is completed by credit union management and officials without "hands on" assistance from the regulatory authority. However, final approval by the regulatory authority is usually required. An involuntary merger is carried out by the regulatory authority without a membership vote. The merger is usually due to insolvency, loss of the credit union's field of membership or sponsor, or loss of interest in the credit union by the field of membership.

A merger occurs when two or more credit unions join together and operate as one financial institution for the purpose of continuing and improving service to members and in some cases to reduce or avoid a loss to the deposit insurance fund. Mergers are a viable alternative when a credit union can not feasibly continue operations.

In a merger, the continuing credit union absorbs the members and creditors and all of the credit union's assets, liabilities, and equity. In other words, the merging credit union is simply made a part of the continuing credit union. Accordingly, the continuing credit union must honor all legal commitments of the merging credit union. Crucial in every merger is management's ability to successfully resolve the problems in the merging credit union. Their ability to cope with the merging credit union's problems should be carefully analyzed along with the effect of the merger on the financial condition of the continuing credit union. This documentation should be in writing and included in the permanent credit union file.

Prompt action is especially important in cases where financial stability, membership confidence, and service are in jeopardy. The supervisory authority must be aware of the negative consequences involved with the merger and work to ensure that the merger is completed quickly and without interruption of member service.

For involuntary mergers, the process begins as of the date of the merger order issued by the regulatory authority. The order should be addressed to the credit union's board of directors and drafted and signed by the head of the credit union regulatory body and his/her superior. The order should be delivered to the credit union immediately after the merger decision is made.

The credit union will continue to be supervised by the regulatory authority until the merger is complete. The regulatory authority has the right to conduct examinations or on-site contacts as desired. If allowed by local law, the merger order may be contested in the court system.

Liquidation– The objective of the liquidation process is to reduce the loss to the deposit insurance fund, if applicable and to satisfy all demands made by the creditors of the credit union. Liquidation can be voluntary or involuntary. It can occur by a revocation of the credit union's license by the regulatory authority or by a decision or vote at a general membership meeting to voluntarily liquidate the credit union, if subsequently approved by the supervisory authority. Voluntary liquidation occurs when a credit union has the ability to meet its obligations to creditors and members. If the liquidation is voluntary, credit union management and the officials are responsible for the liquidation upon approval by the regulatory authority.

For involuntary liquidations, the process begins as of the date of the liquidation order issued by the regulatory authority. The order should be addressed to the credit union's board of directors and signed by the head of the credit union regulatory body and his/her superior. The order should be delivered to the credit union immediately after the liquidation decision is made.

The involuntary liquidation process usually consists of the following steps:

- Taking control and making an inventory of assets;
- Examination and valuation of assets;
- Sale of assets;

- Allocation of the sales proceeds; and
- Completion of liquidation process.

If there are any proceeds or assets remaining after the payment of the credit union's creditors, operational expenses, member savings and deposit accounts, and ownership shares (payments made in that order) then the proceeds should be distributed to the credit union's members proportionally to the size of their membership shares.

The credit union will continue to be supervised by the regulatory authority until the liquidation is complete. The regulatory authority has the right to conduct examinations or on-site contacts as desired. Depending on the law, the involuntary liquidation order may be able to be appealed in the court system.

Revocation of Deposit Insurance, License, or Charter – The credit union law should allow the regulatory authority to suspend or revoke deposit insurance and/or the license of a credit union that has violated any provision of the law, bylaws, or rules and regulations. A revocation order may be issued for:

- Abandonment by the officials of the credit union operations and affairs;
- If the officials refuse to liquidate the credit union voluntarily;
- Serious operational deficiencies that the officials have not acted to correct and which, if allowed to continued, may cause insolvency; and
- Other serious violations of the law, bylaws, and rules and regulations that cannot be reversed and that may cause insolvency.

The revocation order should be addressed to the credit union's board of directors and should be drafted and signed by the head of the credit union supervisory body and his/her superior. It should contain: a statement that explains the reason(s) for the revocation of the deposit insurance and/or license, that the revocation is immediate, and the steps the officials may take if they do not agree with the order. Upon issuance of the order, the assets, books, and records of the credit union immediately become the property of the regulatory authority.

Any official at a credit union in which the deposit insurance and/or license is revoked is prohibited from participating in the affairs of any financial institution without the written consent of the regulatory authority.

Chartering New Credit Unions
December 27, 2002

New credit union chartering is a very time consuming, demanding, and worthwhile activity both for the individuals seeking the charter or license and the body or agency granting the charter. The goals of any organizational body in charge of credit union chartering should be to:

- encourage the formation of credit unions in accordance with existing law and rules and regulations;
- promote the formation of economically feasible, safe and sound financial institutions that will remain a going concern well into the future;
- promote savings and grant access to credit for credit union members; and
- make quality credit union service available for all eligible people.

Types of Charters – Generally credit unions can be formed based on an occupational, associational, or community charter. The occupational charter usually includes all persons and entities that share the identified occupational common bond or are employed by a common employer. Depending on local law, an associational common bond may include in its charter, regardless of location, all-natural person members, non-natural person members, and employees of a recognized association whose members participate in activities that generate mutual benefits and interests. Community charters are usually based on a well-defined local community, neighborhood, or rural area. Individuals who live, work, attend school, or worship in the designated area would be eligible for membership.

Founders of the Credit Union – Credit unions are generally organized by persons who volunteer their time and resources and are responsible for determining the interest, commitment, and economic advisability of forming a credit union. This requires considerable time and effort. Persons interested in organizing a credit union should contact the chartering organization to inquire about the requirements and receive the documentation needed to apply for a credit union charter.

The founders of a credit union should be of legal age and eligible for membership within the proposed credit union. The number of founding members must be at least the minimum amount identified by the chartering body. Each founding member should be required to purchase at least the minimum amount of ownership shares required for membership. The founding members will elect from among themselves, until the first annual general meeting, officials to fill the positions of the board of directors, supervisory committee and credit committee, unless the credit committee is appointed by the board of directors who should designate the committee members upon being appointed to the board. Each elected or appointed official should be required to review a job description that specifically outlines their duties and responsibilities and discusses the necessary prerequisites to fulfill the job requirements. Founding members who will serve in an official capacity shall confirm in writing their voluntary membership and that they have agreed to fulfill duties relative to their position.

Each founding member shall have a business and personal reputation beyond reproach. The following individuals are always unsuitable to be credit union officials:

- persons who have committed crimes against property or violated legislation while conducting their activity;
- former financial institution or legal entity general managers, board members, credit or supervisory committee members that caused, as a result of their actions, an institution's insolvency or a legal entities' bankruptcy;
- persons whose management style and/or business ethics are considered to be questionable or dishonorable and/or dangerous resulting in losses at other financial institutions; and
- persons who have had criminal charges brought against them.

Member Support – The charter applicant should be able to demonstrate that membership support is sufficient to ensure viability. Therefore, the chartering body should have strict entry requirements for new credit unions. Currently regulations addressing entry requirements are minimal in most countries. It is not uncommon to have 20 or fewer individuals starting a credit union with only a small amount of capital. This has led to a large number of institutions that can not offer their members the services they want and are unable to compete financially because they do not have the economies of scale. Licensing such institutions that can not demonstrate sustainability is a mistake and a burden on the agency in charge of regulation and supervision. Prior to licensing any credit union, the chartering body should be satisfied that the institution would be viable.

Required Capital Formation prior to Chartering – As previously stated, it is currently not unusual for very small groups of individuals to receive credit union charters because entry requirements are minimal to non-existent. If minimum capital formation requirements are not established for chartering then few, if any newly chartered credit unions, will have the ability to meet member needs because the credit union will not have the funds necessary to meet loan demand and offer the services desired.

Capital formation and entry requirements are the most important requirements for the formation of sustainable financial intermediaries. The minimum allowable capital amount should be clearly identified as an amount that must be collected by the founding members prior to chartering. Initially the funds that are needed to apply for a charter will come from the ownership share deposits made by the members and donations. Upon receiving a charter, then the credit union will be subject to institutional capital requirements as other existing credit unions are. This regulation normally specifies that a credit union should maintain an institutional capital to total assets ratio of at least 10%. Institutional capital is defined as regulatory reserves, other reserves, monetary donations and grants, undivided earnings, and year to date net income that has not been closed to undivided earnings. Ownership shares should not be included as institutional capital. These shares are withdrawable upon membership termination and can be used to secure a loan. Shares should only be considered capital if they can not be withdrawn under any circumstances by members and the funds are available to absorb losses.

Required Documentation for Chartering – Required documentation for a charter application will vary from country to country, however, the following written documentation is usually required:

- Completed application for charter as provided by the chartering body that usually includes the following information:
  - the name and location of the proposed credit union;
  - the proposed field of membership;
  - the names and addresses of the founding members along with the number of ownership shares purchased by each member;
  - the total amount of ownership share capital as of the formation of the credit union;
  - the names, positions, and number of officials that will make up the board, credit and supervisory committees;
  - the type of facility in which the credit union will be located; and
  - the services to be offered when the credit union opens for business.
- Proposed bylaws that were either modified model bylaws provided by the chartering body or drafted independently by the founding members;
- Resumes or educational and employment information for the members of the board, credit and supervisory committees, and the proposed general manager;
- Signed and dated job descriptions by each elected or appointed official that outlines the duties and responsibilities necessary to fulfill their job requirements;
- Proposed organizational chart detailing the positions within the credit union and the proposed individuals that will fill the positions;
- Proposed credit, collections, capital accumulation, investment, and personnel policies; and
- A business plan.

Economic Advisability/Business Plan – Prior to chartering a credit union, the chartering body should assure that the institution will be viable and that it will not materially affect existing credit unions. In general, the success of any credit union depends on:

- the character and quality of daily management and the officials;
- the depth of member support; and
- the present and projected market conditions.

Groups applying for a charter should be required to prove their economic viability through a business plan that is supported by written assumptions, survey results, and initial membership numbers that meet the required minimum. The business plan is the union between the ideas, goals, and objectives of the founding members with financial numbers. The business plan has three main objectives:

- It documents support for the credit union. This support may be in the from of letters of commitment, survey results, and pledges from potential members pertaining to the amount of savings and shares that they would most likely place in the credit union.

- It describes what the credit union intends to do and how and when it proposes to meet the goals and objectives.
- The plan demonstrates that these goals are achievable. The financial projections should show that the credit union could generate sufficient income to cover the cost of providing services, paying interest on member deposits, and building up financial reserves.

At a minimum the business plan should include the following information:
1. The mission statement;
2. Analysis of market conditions – economic prospects for the potential membership group, information on the other financial institutions currently serving the area, current availability of financial services from other credit unions and financial institutions;
3. Summary of survey results;
4. Financial services needed/desired;
5. Financial services to be provided;
6. How and when the services will be implemented;
7. Staffing of the credit union and background information on key employees;
8. Operating facilities – office space, equipment, supplies, insurance coverage, etc.;
9. Type of management information system to be used;
10. Operating budget for year one and two including the written assumptions used to draft the budget;
11. Pro forma balance sheet for year one and two including the written assumptions used to draft the pro forma;
12. Goals for savings, loans, and number of members;
13. Goals for operating independently – i.e. without subsidies or grant funds;
14. Source of funds to pay expenses during initial months of operations; and
15. Evidence of sponsor support if subsidies are critical to the success of the credit union.

Sometimes the business planning process produces a red flag or warning signal such as:
- the credit union would not be self-sustaining;
- the credit union lacks support from the potential membership;
- the desired services to be offered appear too costly and should be scaled back at the onset of operations; and/or
- the founders are unable to decide on one common vision for the credit union.

These red flags are very important and should be addressed prior to applying for a charter or the chartering process discontinued because the chances of the credit union remaining a going concern are significantly reduced.

Requirements for the Management Information System – If it is financially possible, new credit unions should start operations with an automated management information system. The selected hardware and software should be:
- suitable for credit union operations;
- able to handle the anticipated level of operations;
- able to provide transparent accounting information that is comparable to similar institutions;

- able to produce internal control and required regulatory reports;
- understandable to management and the employees; and
- supported by adequate formal training and maintained by the providers of the hardware and software.

If it is not possible to begin credit union operations with an automated system, credit unions should use a manual accounting and record keeping system that has been approved by the chartering body. Whatever the type of system that is used, automated or manual the issues that should not be overlooked are:
- the system generates information as prescribed by the chartering and/or regulatory body so that reported information is reliable and comparable to other credit unions;
- the employees receive adequate training so that errors do not compromise the integrity of the information; and
- the protection of data is adequate so that it can not be destroyed by natural elements or manipulated by employees or other individuals.

Chartering Body Procedures – Once the chartering body receives a complete charter application package, an acknowledgement of receipt should be sent to the founding members. The chartering body should have the right to request additional information or documents that are deemed necessary to make a decision on chartering the proposed credit union.

An employee of the chartering body will review the application package and verify its accuracy and reasonableness. The employee will inquire into the financial management experience and the suitability and commitment of the proposed officials and employees, and will make an assessment of economic advisability through a detailed review of the business plan. The business plan should be assessed for:
- realistic projections;
- attainable goals;
- adequate service;
- sufficient start-up capital; and
- sufficient time commitments by the proposed officials and employees.

Any concerns that the chartering body may have after the review process should be discussed with the prospective credit union officials. All concerns should be resolved prior to granting the charter; these resolution efforts may delay the processing and granting of the charter.

Approval of a charter should be based on the qualitative evaluation and assessment of the:
- probability of financial and operational success;
- reputation and background information of the founders and the elected and appointed officials;
- professional qualifications of the general manager and other key employees;
- evaluation of the business plan;
- adequacy of start-up capital; and

- suitability of the proposed credit union location, premises, and equipment.

Under normal circumstances, assuming that the chartering body receives all of the necessary documentation completed as prescribed, the charter should be granted in no more than 60 calendar days from the receipt of the documentation. When a proposed credit union is approved for operations and receives a charter, operations should begin within one year from the date the charter was issued.

All chartering documentation should be maintained in a file specific to the chartered credit union. At a minimum, the file should contain the following:

- the approved application for chartering;
- the approved bylaws;
- the names, addresses, account numbers, and ownership share balances of the founding members;
- the business plan;
- decision of the chartering body to license the credit union; and
- the charter or license that grants the credit union the right to operate.

The chartering body should also have the right to deny charters. Charters are usually denied for the following reasons:

- non-submission of all the documents needed for chartering;
- non-compliance of submitted documentation with requirements set forth in law and applicable rules and regulations;
- inadequacy of start-up capital;
- economic non-viability of the business plan; and
- individuals proposed as officials and/or operational management are found to be under criminal investigation, have been convicted of a crime, are liable for, or associated with, losses at other financial institutions, or are generally unsuitable to carry out the duties and responsibilities of their proposed position.

If the chartering application is denied, the chartering body should, within one month, send a written notice of denial to the applicant and give the reason(s) for denial. If the founding members of the proposed credit union can address and correct all the reasons that caused the denial, they should be able to re-apply for a license at any time. If the founding members feel that they are being treated unfairly by the chartering body they should have the right to appeal the decision to a court.

Pre-Licensing On-Site Contact - Prior to granting a license, an employee of the chartering body should perform an on-site visit to meet with the founders and any other individuals having an interest in the proposed credit union to assess the viability and to establish rapport with the founders. The chartering body employee should discuss the role of the chartering body, its expectations regarding the operations of the credit union, and determine that everything is in place to commence credit union operations. All of the observations noted should be placed in writing and made a part of the credit union's permanent file. This information should be used for any follow-up visits.

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Registration of Existing Credit Unions with a Regulatory Authority

December 30, 2002

In many countries, credit unions were originally chartered and registered under general cooperative laws as were cooperatives of all types. Over time credit unions have expanded the instruments they use for attracting funds and have become true savings and loan organizations, offering their clients similar savings choices to those found in more formal financial institutions. Because of these changes and enhancements to member service, credit unions should be licensed by an agency or body that is dedicated solely to financial institutions and the credit unions should be regulated and supervised in a similar fashion as other formal financial institutions are.

Changes at the Supervisory Authority Level – Where credit unions are to be formally regulated, the responsibility is normally given to the existing banking regulatory agency assuming:

- it has displayed reasonable competency in supervising banking institutions;
- the examiners chosen to provide credit union supervision will be adequately trained in credit union operations and supervision techniques; and
- credit unions would receive the supervisory attention needed even though they are smaller in asset size and therefore pose less systemic risk than banks.

Keeping banking and credit union supervision together in one institution facilitates a consistent regulatory approach to and treatment of different types of supervised financial institutions. It may at the same time be efficient and in the best interest of the credit unions to create a specialized credit union department within the overall regulatory agency. Credit unions have a unique ownership and governance structure and other special characteristics that set them apart from other financial institutions.

Changes to Existing Legislation or Regulation – In order to designate a regulatory authority as the regulator and supervisor of certain qualifying credit unions, the existing law or regulation usually will have to be changed. In making changes to the existing regulatory framework, or drafting new legislation and regulation, the following issues should be considered:

- Clear designation of those institutions that will be regulated;
- Establishment of the requirements to be met in order to receive a license to operate as an open credit union;
- The strengthening of credit unions both financially and operationally; and
- Establishment of whom will regulate the institutions and how they will be regulated.

In order to achieve the aforementioned, the new legislation or regulations should:

- Most importantly, establish a capital adequacy requirement that should be met prior to applying for a license from the regulatory authority and outline how this capital requirement is to be met. The capital requirement is best expressed as a percentage of assets. The regulation might establish only one capital requirement or establish scaled institutional capital requirements based on the risk associated with the products and services offered by the credit union. The amount of required institutional capital should be sufficient to ensure that the credit union has the resources it needs to operate in an efficient manner given the services it offers, its expected volume of business, the associated operating and infrastructure costs, and working capital needs.

- Designate ownership shares as non-leverageable equity, not institutional capital, and establish limits on withdrawal.
- Require that all credit unions, prior to applying for licensing, have fully funded their allowances for investment, loan, and other asset losses for all potential losses.
- Establish minimum liquidity standards to diminish the possibility of the credit union not being able to meet member savings withdrawal requests.
- Limit the investment that can be made in fixed or non-earning assets.
- Require that standardized accounting be used to provide for transparent reporting.
- Require an external audit be performed, prior to applying for a license, and stipulate that the credit union should receive an unqualified or "clean" opinion to be considered for licensing.
- Establish minimum education and professional requirements for all officials and the general manager.
- Establish strict conflict of interest and insider dealing regulations that state what constitutes a conflict of interest and limits activities and dealing of officials and management to those that are beyond reproach or question.
- Allow credit unions to merge in order to meet the qualifications for licensing as an open credit union.
- Allow the regulatory authority:
  - to draft model bylaws that will assist credit unions in adapting their bylaws quickly and with the least margin of error; or
  - to require changes to existing bylaws, policies and procedures within credit unions registering for an open credit union license.
- Grant the regulatory authority the necessary powers to effectively supervise, regulate, and compel institutions to comply with any sanctions or administrative actions issued.

If, after changes in the regulatory framework are completed, there is more than one body regulating credit unions, emphasis should be placed on ensuring that the different supervising and/or chartering bodies work in harmony as much as possible when drafting and enforcing regulations and monitoring management and credit union operations.

Required Documentation for Chartering – Required documentation for a licensing application will vary from country to country, however, the following written documentation should be requested:

- Completed application for licensing as provided by the regulatory body that usually includes the following information:
  - the name and location of the credit union;
  - the field of membership;
  - the total amount of institutional capital;
  - the total amount of ownership shares;

  - the names, positions, and number of officials that make up the board, credit and supervisory committees; and
  - the products and services offered, including a breakdown of the loan portfolio as to collateral type and loan purpose that should also include the total loan amount and number of loans for each collateral type and loan purpose.
- Proposed bylaws that contain any required changes or adaptations as prescribed by the regulator;
- Resumes or educational and employment information for the members of the board, credit and supervisory committees, and the general manager;
- Organizational chart detailing the positions within the credit union and the individuals that fill the positions;
- Credit, collections, capital accumulation, investment, and personnel policies; and
- A 2-3 year business plan.

Meeting Requirements of the New Regulatory Framework – Non-regulated institutions can not be expected to comply immediately with all aspects of the law, bylaws, and rules and regulations. Because the supervisory authority generally has much more stringent requirements than the original cooperative chartering agency, the open credit unions should be given adequate time to comply with the new requirements and standards to allow for changes in operations, financial structure, procedures, policies and accounting. This process of bringing credit unions into line with the regulatory framework so they can engage in financial intermediation has four stages.

➢ **Stage One** – Information and instructions should be given to the credit unions to assist the officials, members, and daily management in deciding whether to operate as an open or closed credit union. The information should include the necessary documentation to be submitted, the qualifications that must be met in order to be registered as an open credit union, and the time frame in which the institutions have to comply. Credit unions should be required to declare in writing, to the appropriate authorities, if they intend to function as an open or closed institution

➢ **Stage Two** – Involves the receipt and evaluation of the information provided by those credit unions applying to be registered as open credit unions. Upon evaluating all of the requests, the regulator should prioritize the eligible institutions that have met all the requirements by asset size, membership size, degree of financial intermediation with a broader-based community oriented group, and overall institutional risk.

➢ **Stage Three** - Upon prioritizing the credit unions as previously mentioned, the regulator should perform an on-site examination to evaluate the safety, soundness, and institutional preparedness for the licensing change. The objectives of this examination are similar to that of an annual examination:
  - evaluate the credit union's financial soundness;
  - appraise the quality of management;
  - develop plans with officials to correct problems; and
  - determine the degree of risk to the credit union system as a whole and to the insurance fund, if applicable.

- **Stage Four** – If the credit union meets all of the requirements for licensing under the regulatory authority then the license should be granted and the credit union subject to regulation just as any other formal financial institution.

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Supervision of Problem Credit Unions

December 31, 2002

One of the most important job functions of a regulatory examiner is the supervision of problem credit unions. Examiners must provide a credit union the attention it needs to fully resolve problems before they:

- threaten the credit union's safety and soundness;
- cause a financial loss to the members; or
- adversely effect member confidence in the credit union and the system as a whole.

Off-site Problem Identification – The objective of off-site supervision is to quickly identify negative trends and emerging problems and to resolve the issues before they become so serious that they could negatively affect the credit union's financial condition. Problems are best identified through a trend analysis of the credit union's balance sheet, income statement, and delinquency report figures. From these figures a ratio analysis should also be performed, using ratios that best determine a credit union's financial condition. An examiner should perform a trend analysis of both the actual results and the ratios no less than semi-annually. More frequent analysis is indicated if any serious problems have been identified, the credit union is newly chartered, or if the credit union offers higher risk products such as business and agricultural loans. In addition to a trend analysis for a particular credit union, all credit unions should be part of a peer group so that credit union results and ratios may be compared for a similar group of credit unions. Peer groups are usually based on credit union asset sizes.

The examiner that is responsible for performing the on-site supervision can perform off-site supervision or the supervision duties can be divided between on and off-site supervision departments.

On-site Problem Identification – If the regulatory agency has a sufficient budget and an adequate number of employees, there is no better way to identify and resolve a problem, whether it is emerging or evident for some time, than with an on-site contact. The examiner can:

- request and review any necessary reports to determine the extent and severity of the problem;
- interview and observe employees to determine the source of the problem;
- determine if the employees and officials are adequately trained and capable of fulfilling their job duties;
- discuss and develop agreeable solutions with daily management and the officials;
- determine on a first hand basis if fraud or a misappropriation of funds is involved; and
- observe the working relations between the employees and the quality of the overall work environment.

Supervisory Tools to Be Used for Problem Resolution – All of the most commonly used supervisory tools that may be used by an examiner are explained in-depth in the summary entitled "Administrative Actions". These supervisory tools encompass those actions that the regulatory authority can take or enforce against a problematic credit union in order to reverse negative trends or operational results, remove officials, or take over management of a credit union. Often problems can be resolved and the necessary changes affected through a well-written Document of Resolution (DOR) that is a part of every full-scope examination. If the DOR, along with on and off-site supervision provided by the assigned examiner, can not resolve the problems then the following are other tools that may be used, listed in their order of severity:

- Letter of Understanding and Agreement;
- Cease and Desist Order;
- Monetary Penalties;
- Establishment of Special Reserves;
- Removal of Officials;
- Prohibitions;
- Conservatorship;
- Merger;
- Liquidation; and
- Revocation of Deposit Insurance, License, or Charter.

Additional supervisory tools may exist if credit unions are part of a deposit insurance scheme or a stabilization fund. Generally deposit insurance or the stabilization fund is administered by the regulatory authority charged with credit union supervision. In general there are two categories of assistance that may be offered to selected credit unions:

- **Non-Financial Assistance** – The credit union's undivided earnings and other reserves first absorb losses, followed by regular reserves or revocable reserves in excess of regulatory reserve requirements. In most non-financial assistance cases, a representative of the regulatory authority (the examiner and their supervisor) will issue an LUA containing a repayment schedule to replenish regular reserves for approved reserve changes or reserve transfer reductions.
- **Financial Assistance** – If a credit union that is covered by deposit insurance or the stabilization fund has inadequate available reserves and a deficit in undivided earnings, the administrator of the deposit insurance or stabilization fund may consider granting financial assistance to continue operations, in lieu of liquidation or merger. Financial assistance may be temporary or permanent in nature. Generally temporary assistance is limited to 6 months and permanent assistance does not exceed 24 months.

The previously mentioned supervisory tools can be used to resolve any credit union problem. Examples of prevalent problems are discussed below along with suggestions for their resolutions.

1. Problem – Increasing ratio of loans delinquent more than 30 days as compared to total loans.

Identify Source of Problem – Several factors or changes can cause an increase in delinquent loans. The examiner during off or on-site supervision should determine what is the source of the increase. The source of this problem can usually be identified by:

- reviewing a sample of delinquent loans and current loans noting changes in loan underwriting and borrower creditworthiness;
- comparing the underwriting of loans granted during a period when delinquency was not an issue to the existing delinquent loans;
- reviewing the efforts of the collections department; and
- interviewing the general manager, heads of lending and collections, lending and collection staff, credit committee officials, or any other officials who may have good insight.

An increase in delinquency is often caused by:

- a decrease in loan underwriting standards in order to increase loans outstanding;
- inadequate or non-existent written loan and collection policies and procedures;
- excessive turnover in the loan department, therefore, individuals with limited experience are reviewing and approving loans;
- a credit committee with very little experience in granting loans;
- changes in the collection department staff or techniques used; or
- employment problems such as layoffs, strikes, or business closures with the credit union sponsor or in the credit union's operational area.

Supervision Techniques Used to Solve the Problem – Increasing loan delinquency can impact the financial health of a credit union quickly if left unresolved. Because borrowers are not making their loan payments:

- interest on loans will decrease,
- collection expenses will most likely increase because there are more delinquent loans,
- net income will decrease due to a reduction in gross income and an increase in expenses, and
- capital contributions will be negatively affected due to the decrease in net income.

Examiners must work with credit union management to quickly identify the source of the increase in delinquency and draft action steps to be taken in a DOR. This document is part of a full-scope examination, but can be used at any time to identify problems, establish action steps or resolutions to problems, and monitor progress made towards the resolutions of the problem or the lack thereof. The DOR could be used to outline the steps that need to be taken to improve loan underwriting or collection procedures or to assist credit union management in resolving loan delinquency due to local economic problems.

When drafting action steps to reduce delinquency, the examiner will want the assistance of the credit union's general manager, heads of collection and lending, and the credit committee, if applicable. Upon completing these agreed upon action steps, the examiner should discuss the action plans with their supervisor and have the credit union officials approve the DOR.

To closely monitor the future trend of delinquent loans the examiner should receive a balance sheet, income statement, and delinquency report monthly. The examiner should carefully analyze the status of each delinquent loan on the delinquency report. If loans are removed from the report from month to month, the examiner should determine how these loans were removed to ensure that there was no manipulation of data to reduce loan delinquency.

If the action steps in the DOR do not resolve the problem and the credit union is solvent, the examiner should consider using a more severe administrative action. Depending on the reason(s) the DOR was ineffective, what the source of the delinquency problem is, and how threatening the delinquency problem is to the on-going concern of the credit union determines alternative courses of action. Alternatives include:

- A Letter of Understanding and Agreement (LUA) requesting that the officials have the general manager or any individuals responsible for the on-going delinquency problem terminated;
- A Cease and Desist Order which requires that the credit union cease and desist all of the actions that are causing loan delinquency to increase;
- Removal of Officials, if the credit committee or any of the board members are the source of the problem;
- Establishment of Special Reserves to cover the potential loan losses;
- Conservatorship; or
- Merger.

2. Problem – The allowances for asset losses (this includes loans, investments, and any other assets) accounts are not adequately funded for potential losses.

Identify Source of Problem – Inadequate allowances can be identified quickly:

- by an individual review of all potential losses with the purpose of determining the amount that needs to be in the allowance (usually performed with an on-site contact); or
- if the allowances are not sufficient to met the required formula amount as prescribed by the regulatory authority based on the age of the asset or loan delinquency (this can be identified during off or on-site supervision).

Examiners should quickly determine the reason(s) for the inadequate allowance accounts and address the problem with the general manager. If the allowance accounts are not adequately funded it could dramatically skew financial results and any trend analyses and peer comparisons performed. Inadequate allowances are usually due to:

- no employee responsible for determining how much should be in the accounts;
- an overly optimistic or inadequately trained individual determining the amount that should be in the allowance accounts; or
- daily management's unwillingness to show a net loss for the accounting period.

When the allowances are funded, it is done through an expense account. Any increase to this expense account will therefore increase overall expenses and negatively impact the net income account. This will directly effect the credit union's ability to increase the capital accounts.

Supervision Techniques Used to Solve the Problem - If the allowances are not adequately funded then assets, net income, and institutional capital will be overstated. In the worst case scenario, a credit union could appear to be solvent, when in reality it is insolvent because the credit union's unrecognized losses exceed it's institutional capital. The DOR should initially be used to address the inadequacies of the allowance accounts and require that the allowance accounts be adequately funded immediately. If for some reason due to local law this is not possible, then the credit union should be required to adequately fund the account over an established time period. Additionally the financial statements should be footnoted as to the amount that should be in the allowances and the effect on net income and capital if the allowance accounts were adequately funded.

When drafting the action steps to adequately fund the allowance accounts, the examiner should work with the credit union's general manager. Upon completing these agreed upon action steps, the examiner should discuss the action plans with their supervisor and have the credit union officials approve the DOR.

The examiner should follow up on a monthly basis to ensure that management and officials have complied with the DOR. If the action steps in the DOR do not resolve the problem and the credit union is solvent, the examiner should consider using a more severe administrative action, depending on the reason(s) the DOR was ineffective, why the allowance accounts are inadequate, and if the improper funding of the allowance accounts is threatening to the on-going concern of the credit union. Alternatives include:

- An LUA that requires the officials to adequately fund all allowances and specifically details the more severe actions that may be taken should the officials not comply with the LUA;
- Monetary Penalties;
- Removal of Officials, if officials are the cause or they will not take the necessary actions such as terminating the general manager if he/she is the source of non-compliance with the DOR or the LUA;
- Establishment of Special Reserves to cover the amount that is not provided for in the allowance accounts;
- Conservatorship;
- Merger; or
- Revocation of Deposit Insurance, License, or Charter.

3. Problem – The operating expenses rise dramatically and net income falls.

Identify Source of Problem – It is clearly the direct responsibility of daily management to control credit union expenses. Expenses may increase quickly if:

- adequate budgeting and an expense approval process are not in place;
- the credit union lacks an adequate review process of monthly expenses to ensure that the expenses are within the budget and properly approved;

- loan losses are increasing, and the provision for loan loss expense has to be increased to adequately fund the allowance for loan loss account;
- employee salaries and benefits are increased dramatically;
- expensive fixed assets are purchased thereby increasing the monthly depreciation taken;
- collection expenses increase in an attempt to reduce the amount of delinquent loans; or
- a new service is added such as checking accounts and there are no offsetting fees or the fees established are inadequate.

Examiners can easily identify increasing expenses through on and off-site supervision using trend analyses of financial results accompanied by income statement ratio analysis and peer group comparisons. An examiner may have to make an on-site visit to identify the exact expense items that have increased or they may contact credit union management to have them send all monthly expenses broken out by expense account number or income statement line item. The examiner, with this information, may be able to determine the source of the increase.

Increasing expenses can become a very serious problem if left unchecked. They will negatively impact both the credit union's net income and its ability to build institutional capital and, if left unresolved, they could directly effect the credit union's ability to survive in the future.

Supervision Tools Used to Solve the Problem - As with the other problems discussed above, the examiner should contact management to discuss the increasing expenses, determine what the cause(s) of the increase is and establish effective solutions to the problem(s). Once the problem(s) has been identified the action steps needed to resolve increasing expenses should be outlined in the DOR with the assistance of management. In addition to the action steps, the DOR should also clearly state the time frame for completion of each action step and who is responsible for the completion of each step. The proposed DOR should then be reviewed by the examiner's supervisor and approved by the board of directors.

The examiner should follow up on a monthly basis to ensure that management and officials have complied with the DOR; the amount of total operating expenses is decreasing as is the operating expenses to average assets ratio. If the action steps in the DOR do not resolve the problem and the credit union is solvent, the examiner should consider using a more severe administrative action, depending on the reason(s) the DOR was ineffective, why the expenses are increasing, and if the increasing expenses are threatening the credit union's financial future. Alternative actions include:

- An LUA that requests the officials to review, reduce, and eliminate all unnecessary expenses and specifically details the more severe actions that may be taken should the officials not comply with the LUA;
- A Cease and Desist Order that states the actions that the officials and management must cease and/or desist in order to reduce expenses;

- Removal of Officials, if officials are the cause or they will not take the necessary action such as terminating the general manager, if he/she is the source of non-compliance with the DOR or LUA;
- Conservatorship; or
- Merger.

4. Problem – Credit union liquidity is inadequate to meet loan demand, savings withdrawal requests, and the payment of operating expenses.

Identify Source of Problem – Illiquidity can easily be identified using on or off-site supervision through the monthly monitoring of the balances of:

- cash;
- investments with a maturity of less than 1 month;
- loans with a maturity of less than 1 month;
- savings accounts with no maturity;
- savings deposits with fixed maturities that will mature in the next month; and
- liquidity ratios such as liquid assets to total assets and liquid assets-short term payables as compared to member deposits.

An illiquid credit union can experience grave and irreversible damage if members are unable to access their funds when they want. Members will immediately lose confidence in the credit union as a sound financial institution, they will quickly tell others that they could not access their funds, and they could cause a "run" on deposits once members are allowed access to their deposited funds. Illiquidity can result from:

- an increase in loan maturity therefore slowing the rate at which the loan portfolio turns over;
- an increase in loan demand and approval;
- an increase in savings withdrawals;
- important holidays, festivals, and seasonality needs of members,
- a change in investment strategy to longer term investments; or
- large investment in fixed assets and/or non-earning assets.

Supervision Tools Used to Solve the Problem – The examiner will want to contact the general manager immediately to devise solutions to the liquidity problem. Initially the action steps to be taken to resolve the problem may be addressed in the DOR. The examiner will want to outline the action steps to be taken along with the applicable time frames and responsible individuals for completing each action step. The examiner will want to review the proposed action steps with their supervisor and present the DOR to the credit union's board of director for approval. To improve liquidity, management should consider:

- improving the day-to-day management of cash;
- controlling unpredictable outflows of cash;
- adhering to targets established for liquidity ratios; or
- establishing access to a line of credit or liquidity pool for short-term liquidity needs.

The examiner should follow up on a monthly basis to ensure that management and officials have complied with the DOR and that liquidity is improving. If the action steps in the DOR do not resolve the problem and the credit union is solvent, the examiner should consider using a more severe administrative action, depending on the reason(s) the DOR was ineffective, why the credit union continues to be illiquid, and if the illiquidity is threatening the credit union's financial future. Alternative actions include:

- An LUA that requires the officials to improve liquidity through specific outlined steps, within established time frames, and specifically details the more severe actions that may be taken should the officials not comply with the LUA;
- A Cease and Desist Order that states the actions officials and management must cease and/or desist immediately to improve liquidity;
- Removal of Officials, if officials are the cause or they will not take the necessary actions such as terminating the general manager, if he/she is the source of non-compliance with the DOR or the LUA;
- Conservatorship; or
- Merger.

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Accounting Norms and Principles

January 7, 2003

The purpose of an accounting system is to provide credit union management with complete and accurate financial information that can be used to operate the credit union safely and effectively. Accounting effectiveness is enhanced with the use of accepted accounting principles that address day-to-day credit union operations including:

- proper methods for handling member's transactions;
- accurate recording or transactions in the books and records;
- proper receipt and disbursement of funds; and
- preparation of financial statements in a manner that reflects the current financial position.

The accounting records also serve as the basis for reports to the members and interested third parties. Therefore, it is essential that the records be accurate, current, and reveal the true financial condition of the credit union.

Monetary Basis for Accounting – Credit union accounts should be stated in terms of the monetary amount or value as of the transaction. The recording of each transaction in terms of monetary units provides the best feasible indicator of its relative impact on the overall operations of the credit union.

Materiality – A statement, fact, or item is material if, after giving full consideration to the surrounding circumstances, it would likely influence or "make a difference" in the judgement and conduct of a reasonable person. Material facts relating to financial activity should be recognized in credit union accounting and the resulting financial statements. The accumulation of many small items, each of which in itself would be immaterial, would be material if the overall effect would tend to influence the judgement and conduct of a reasonable person.

Accounting and Dividend Periods – Credit union accounting periods may be monthly, quarterly, semi-annually, or annually. The credit union may select the period length and close its books accordingly, but all credit unions should be required to close their books no less than annually. Share dividends are usually paid at the end of an accounting period, however, provisions should be made for regulatory reserve requirements and adjustments made to allowances for asset losses prior to any payment of dividends on shares.

Double Entry Accounting System – All credit unions should use a double entry accounting system. In this system each transaction results in at least two entries: a debit (or entry on the left side of an account ledger) and a credit (or entry on the right side of an account ledger). If the transaction requires several debits and credits , the total of the debits and credits should be the same. In other words, for every debit entry there must be an equal offsetting credit entry and vice versa, if this is not the case the records will not balance.

The use of debits and credits can be very confusing to an individual with little accounting experience; to make accounting easier there are some basic rules that can always be followed:

- Asset accounts normally have debit balances, although at times such an account may have a credit balance.
- Liability accounts, including member savings and deposit accounts, normally have a credit balance, although at times the accounts may have a debit balance.
- Institutional capital and membership share accounts usually have credit balances, but like the liability accounts they may have a debit balance on occasion.
- Income accounts should have credit balances and, both operational and dividend expense accounts should have debit balances, although both income and expense accounts may have opposite balances from time to time.
- In other words, debits represent an increase of an asset, a reduction of a liability or capital account, or the payment of an expense. A credit represents a reduction of an asset, increase of a liability or capital account, or receipt of income.

Whether to debit or credit an account can be determined by the following guidelines:

- To increase an account that normally has a debit balance, it should be debited;
- To increase an account that normally has a credit balance, it should be credited;
- To decrease an account that normally has a debit balance, it should be credited; and
- To decrease an account that normally has a credit balance, it should be debited.

To ensure that the correct entry is made when preparing accounting entry, the accountant should answer the following questions:

- What are the account numbers and names that will be affected by this transaction?
- Do the accounts normally have a debit or credit balance?
- Is the account balance to be increased or decreased with the entry?
- How does the entry affect the financial statements?

Accounting for Transactions – The record of original entry or the Journal and Cash Record (JCR) is a diary of the transactions as they occur. Each day's cash receipts and disbursements are entered into the JCR in chronological order. Thus, a running history of each day's transactions is kept and may be summarized as needed.

At the end of a designated period, usually month-end, the total of all transactions for each account should be obtained by totaling the debit and credit columns of the JCR. The debit entries should equal the credit entries.

The record of final entry or the General Ledger as it is most commonly known serves as a means of summarizing the entries in a form that will enable the accountant to prepare reports on the results of operations as of month end and year to date. Entries in the general ledger consist of posting the debits and credits for each account in the JCR to the corresponding account in the general ledger and computing the net balance for each account. No entries should be made in the general ledger without first being made in the JCR.

When a general ledger account summarizes a number of transactions an additional record known as a subsidiary ledger should be used to provide detailed information about the general ledger account. Subsidiary ledgers are used to support general ledger accounts as they detail all of the entries made when more than one item is accounted for in the general ledger account. Subsidiary ledgers should be independent (bank statements, investment statements, etc.) from the general ledger. Subsidiary ledgers are used to verify that the general ledger balances are correct. If there is a difference between the general ledger balance and the subsidiary ledger then a reconciliation of the difference should be performed to identify the entries that make up the difference. The reconciliation should be retained with the subsidiary and general ledgers. A subsidiary ledger has many advantages including:

- isolation for a member, on a single ledger card, the transactions that effect their loans, savings, and share accounts;
- elimination from the general ledger of a great amount of detail relating to assets, liabilities, and capital accounts;
- easier location of errors by detailing individual entries that may be grouped or summarized in the general ledger account; and
- assistance to the accountant and the internal and external auditors in verifying the correctness of the general ledger balances and the financial statements.

For example – The general ledger account for depreciation of furniture, fixture, and equipment usually has one monthly entry summarizing all of the monthly depreciation amounts. Subsidiary ledgers are necessary for each piece of furniture or equipment. Each item accounted for was likely purchased on a different date and the purchase prices varied; therefore, the depreciation time frames and the amounts are different as is the outstanding balance of each depreciable item.

Financial Statements – Financial statements consist of two principal reports, the balance sheet and the income statement. The balance sheet summarizes the credit union's financial position as of a point in time. It is similar to a snapshot in that the balance sheet changes immediately after that point in time or the next business day. Normally the balance sheet is prepared as of the last day of each month.

The balance sheet lists the assets, liabilities, and capital accounts along with their outstanding balances as of month end. Assets are items of value that the credit union owns such as: loans, cash, investments, buildings, furniture, and equipment.

Liabilities represent amounts owed by the credit union to persons or legal entities. Typical examples of such items include: accounts payable, external credit payable, taxes, interest on member deposits, and accrued expenses. The liability side of the balance sheet also contains the member savings, ownership shares, and capital accounts.

The total of the asset accounts on the balance sheet should always equal the sum of the liability and capital accounts. If this is not the case, there is an error(s) as the credit union accounting records are not in balance.

The income statement reflects the gross amount of income earned and the total amount of expenses incurred during the period and allows users to determine if the credit union made a profit. If gross income is greater than the total of expenses and interest paid, the difference represents a net gain from operations during that particular period and is reflected as an increase in the undivided earnings account when the accounting records are closed. If the expenses and interest paid are greater than gross income, a loss is incurred and the undivided earnings account decreased as is institutional capital. The net gain or income after all expenses, interest on member deposits, and regulatory requirements have been met is available for payment on ownership shares.

At the end of the accounting period all income and expense accounts are closed and the balances are transferred to the net income account. The overall difference between gross income (credit balance) and total expenses and interest paid on member deposits (debit balances) also known as net income or loss is then closed and transferred to the undivided earnings account. Closing these accounts is necessary to reduce the income statement account balances to zero so these accounts can be used to collect revenue and expense transaction data for the following accounting period. Closing accounts at the end of an accounting period does not occur with balance sheet accounts. Balance sheet accounts collect transaction data throughout the life of the credit union, not just the accounting period.

Principles Effecting the Recording of Assets, Liabilities, Savings, Shares, and Institutional Capital as to Provide for Full Disclosure - Full and fair disclosure is defined as the level of disclosure a reasonable person would provide a credit union member to fairly inform them of the financial condition and the operational results of a credit union.

The financial statements described above should provide full and fair disclosure of all income, expense, assets, liabilities, savings, shares, and institutional capital accounts. Valuation or allowance accounts are usually necessary to present fairly the credit union's financial position.

The accounting principles relating to assets for a credit union using accrual-based accounting are as follows:

1. **Assets** *are considered* to be *something* of economic value that are used to satisfy the wants and needs of the members. Assets are normally recorded at their cost to the credit union. If an asset is no longer considered valuable such as, a borrower can not repay their loan or some equipment becomes obsolete, then the asset should be written off or removed from the balance sheet immediately.

2. **Loans Outstanding** should be recorded to reflect their unpaid balances as of the date of the financial statement.

3. **Accounts Receivable** represents amounts owed to the credit union by members, creditors, or employees. They are recorded to reflect their unpaid balances.

4. **Allowance for Loan Losses** represents all known and potential loan losses. This is a contra asset account, which means the account has a credit balance instead of a debit balance as asset accounts normally have. The effect of this contra asset account is to reduce the value of the loans outstanding by the amount of all potential loan losses. Monthly, management should determine that the allowance for loan loss account is adequate and meets any regulatory requirements. To avoid large adjustments to this account, the credit union should budget an amount (during the annual budgeting process) that will be expensed monthly through the provision for loan loss account (an expense account). This amount should be based on past losses, current delinquency, the economic situation, and regulatory requirements. If for some reason there is an unexpected large increase in the amount needed in the allowance for loan loss account, that amount should be expensed immediately, if it is not then the value of the loan portfolio will be overstated and the balance sheet not fully and fairly disclosed.

5. **Cash** (teller cash, vault cash, petty cash, credit union non-interest bearing checking accounts) is recorded as the amount of cash on hand at the credit union and in checking accounts as of the date of the financial statement.

6. **Investments** are recorded as the cost of the investment to the credit union. Under no circumstances are the values of investments written up to the current market value. If there is a significant decline in the value of the investment, then that decline should be recognized if the credit union will receive less at the investment maturity or the investment will be sold prior to maturity and result in a loss. If the investment is held to maturity, and the purchase value of the investment received, then a loss does not need to be accounted for. If the credit union is to recognize a loss it is done so with the **Allowance for Investment Loss account,** a contra asset account. The account has a credit balance. This account reduces the value of the investments by the potential loss. The offsetting or debit entry is to the provision for investment loss, an expense account.

7. **Fixed Assets** should be recorded in accordance with the following principles:
   - The purchase of fixed assets should be recorded at cost. The cost of acquisition is the net purchase price of the asset plus all incidental costs necessary to put the asset into use, such as freight, installation cost, etc. If property is exchanged for the acquired asset, then cost is recorded as the amount of cash paid plus the recorded amount of the asset surrendered. No gain, if any, should be recognized on the transaction; the entire indicated loss on the exchange, if any, should be recognized. If property is acquired through exchange without cost or a donation, the fair market value as of the date the asset is received should be used as the cost. *With donations, the offsetting credit entry is to donated equity.*
   - Each credit union's board of directors should establish a dollar value limit (for example $25USD or the equivalent in local currency) under which fixed assets will be recorded as a current expense instead of established as a fixed asset and depreciated.

8. **Depreciation** of credit union fixed assets is the charge allocated to an accounting period to distribute the cost of the fixed assets less salvage value (if any) over the estimated useful life of the asset. Depreciation is an equal amount that is expensed each month; it reduces the value of the asset as the asset is used. Depreciation is a contra account and therefore has a credit balance.
   - Fixed assets, whether purchased or donated, should be depreciated to a minimum amount or salvage value. They should not be removed from the general ledger or the credit union's inventory as long as they are in use. Assets that are depreciated to zero and no longer recorded in the accounting records can be easily removed from the premises since there is no longer any record.

9. **Prepaid Expenses** are costs of a material amount that effect subsequent accounting periods. These costs or expenses are amortized over the accounting periods to which they are applicable. For example, if a credit union has to pay association dues which cover one year's dues in the association during the 1st month of the year, then the accountant should establish a prepaid expense account and expense 1/12th of the expense each month throughout the year until the prepaid account has a zero balance. With this entry the credit union does not have a large expense during the 1st month of the year, the expense is evenly distributed throughout the time period for which the expense is attributable.

10. **Other assets** are all assets that do not fall in the above categories. They are to be recorded at cost.

11. An essential characteristic of a **liability** is that there is a present obligation and the settlement of the obligation will cause an outflow of credit union resources. **Liabilities** should be recorded at their actual amounts or, if the actual amounts are not known, they should be recorded based on reasonably accurate estimates.

12. **Accounts Payable** consist of all bills that have been received and are due for payment but as of the date of the financial statement remain unpaid. The invoice amount is the amount recorded in the books.

13. **External Credit Payable** represents all borrowed funds. The amount recorded is the outstanding amount payable.

14. **External Credit Interest Payable** is the amount of interest that is due on the external credit. The interest due as of the financial statements should be accrued for; the amount payable is all accrued interest since the last interest payment made.

15. Interest on member deposits that have a stated or contracted interest rate are to be accrued for in **Accrued Interest on Deposits**. Members usually sign a contract when making these deposits that states a certain amount of interest will be received for the deposit. Because of the contract, the member must always receive the interest amount

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described in agreement. The accrual is based on the stated rate in the agreement. Interest on deposits should be accrued no less than monthly.

16. **Accrued Expenses** allocate costs to the periods benefited. These expenses are estimable, based on past history, and should be accrued monthly. For example - A credit union has their annual meeting in September each year. To account for this type of expense an amount should be accrued monthly that is 1/12th of the amount anticipated to be spent (from October of the previous year to September of the current year). With this accounting the net income remains level throughout the year instead of a large expense in September when the meeting is held.

17. **Contingent Liabilities** are defined as an existing condition, situation, or set of circumstances that may or may not result in a loss for the credit union. The amount of the loss will be determined by future events. Examples of contingent liabilities include pending or threatened litigation, guarantees of the indebtedness of others, and agreements to repurchase assets that have been sold. The amount of a contingent liability should be accrued for if:
    - prior to the issuance of the financial statements it is probable that a loss will actually occur; and
    - a reasonable estimate of the resulting loss can be made.

18. **Member Deposits** are recognized in the accounting records at the actual amount deposited. Numerous types of deposit accounts are usually offered including: demand deposit accounts, term deposits of various maturities, special purpose savings accounts, retirement accounts, checking accounts, and hi-yield or money market accounts.

19. **Net Income** is the difference between all income, expense, and interest paid on external credit and member deposits for the current accounting period. Net income is considered a part of institutional capital.

20. **Capital** can be divided into two types, **institutional and equity capital.** **Institutional capital** is defined as the total of regulatory reserves, undivided earnings, special reserves (designated for a specific purpose), monetary donations, and net income. These capital accounts can be used for losses and no party or individual has any claim to these funds as they belong to the credit union. Ownership shares are **equity capital.** These shares are withdrawable upon membership termination and frequently can be used to secure loans. The credit union does not have sole claim to these shares, therefore it is not the rightful owner of the shares. Ownership shares may be used to absorb losses, if they are considered as the member's liability, but frequently are not available because they are securing member loans. Effectively these borrowers have withdrawn their shares in the form of a loan.

21. **Undivided Earnings** is a part of institutional capital; past net income and losses are accumulated in this account. At the close of each accounting period, the income and expense accounts should be closed to the Net Income/(Loss) account, after which the

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balance of the Net Income/(Loss) account should be transferred to Undivided Earnings. Other miscellaneous charges should be made to undivided earnings only for correction of an error of a material amount that represents adjustments affecting prior accounting periods. Material errors include: arithmetic mistakes, the misuse or deletion of information, mistakes in the application of accounting principles or procedures, and improper interpretations of the accounting aspects of major transactions. Correction of an error should result in the restatement of the prior year's financial statement to disclose the effect of the correction made.

22. **Capital Reserves** are the capital reserve accounts required to achieve capital adequacy. Credit unions should not be permitted to pay dividends on ownership shares prior to meeting all regulatory requirements. Regulatory reserves are a part of institutional capital.

23. **Donated Equity** is the account used to record a gift or donation of a tangible fixed asset of material value. The value of such an asset should be established by a credit to this account and the offsetting debit is to the appropriate asset account such as furniture and equipment. When fixed assets donated to a credit union are not considered material in value, the credit would be to non-operating income instead of donated equity and the debit either to an asset or expense account depending on the purpose of the donation. Only monetary donations are considered institutional capital.

24. **Asset Revaluation Accounts** are used to reevaluate fixed assets due to serious inflation. The appropriate fixed asset accounts are increased or debited, based on an appraisal, to recognize the effects of inflation and the reevaluation equity account is credited. Asset reevaluation accounts are not considered part of institutional capital as the account has no monetary significance, it is only an accounting adjustment.

25. **Ownership Shares** are classified as equity capital on the credit union's balance sheet. They are not considered to be a part of institutional capital. Ownership shares are accounted for at the actual amount of the deposit made by the member. Shares may be used to absorb operational credit union losses. Member liability is frequently limited to the amount invested in ownership shares. Each member must have the minimum amount in ownership shares to access all credit union services. Shares can be paid a dividend only after operating expenses, interest on deposits and regulatory capital requirements have been made. Dividends paid may be added to the share account balance or paid out to the member.

Principles Effecting the Recording of Income and Expenses as to Provide for Full and Fair Disclosure - All income, expenses, gains, and losses affecting an accounting period should be recorded in the appropriate income and expense accounts. Income and expenses from regular operations should be separated from extraordinary gains or losses occurring during the accounting period to enhance disclosure.

1. **Income** includes both revenues and gains. Revenue or income arises in the course of ordinary credit union activities and gains arise from non-operational or unusual occurrences. Income accounts normally have a credit balance. Income should be accrued for when earned but not yet received as of the date of the financial statement. The entries to recognize income are to accrued income on loans or investments (debit) and interest on loans or investments (credit). Fees and late charges should be recorded as income when received.

2. **Expenses** include losses as well as other expenses that arise in the course of ordinary credit union operations. Normal operating expenses include: employee salaries and benefits, association dues, rent, utilities, stationary and supplies, loan processing expenses, travel and entertainment expenses, repairs and maintenance, postage, publications, communications, advertising, professional and outside services, teller cash overages and shortages, interest on external credit and interest on member deposits. Expenses relate to current operations and should be paid and recorded promptly when due. If, however, at the end of the month there are invoices which are for expenses that have not been paid they should be recorded as current month expenses (debit) and to accounts payable (credit) until paid. Large expenses that are applicable to future periods should be recorded as prepaid or accrued expenses and amortized over the periods to which they are applicable, these include:
   - **Fixed Assets,** as discussed earlier, are depreciated monthly over the life of the asset through an expense account; and
   - **Prepaid and Accrued Expenses** are included in expenses monthly through the amortization of prepaid expenses and accruals for costly future expenditures such as the annual meeting, annual audit, property taxes, etc.

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Code of Conduct/Conflict of Interest

December 6, 2002

Credit union officials and employees have an obligation to the credit union that extends beyond assuring that their actions do not violate any statute or regulation. They are fiduciaries who owe it to the credit union to act in good faith in the performance of their duties.

In accepting a position as an official or employee of a credit union, an individual should recognize that the interests of the credit union and its members have priority over any personal interest that an individual may have. The position should not be used to gain personal profit or advantage.

Credit union law normally gives the board of directors responsibility for the general direction and control of the credit union. The board thus has the task of establishing policies and procedures for the conduct of the credit union's affairs. A code of conduct should be established to guide officials and employees in avoiding conflicts of interest. The focus of the policy is to protect the image and integrity of the credit union and to strictly prohibit actions from which officials or employees could derive personal gain while fulfilling their duties and responsibilities.

All officials and employees should have to review, sign, and date a code of conduct statement and review the code of conduct policy. This should be done initially when the employee is hired or the official appointed and it should be renewed annually either at the first meeting of the officials immediately preceding the annual general meeting or during the annual employee appraisal. The statement should request information that can be used to determine if the official or employee may have a conflict of interest that would disallow them from performing their job duties and responsibilities. Requiring the officials and employees to sign a code of conduct statement disallows those involved in a violation to use the excuse "I didn't know this was a problem".

The following discusses and outlines the information that should be included in a code of conduct policy and statement.

General Policy Statement – A code of conduct policy should make it very clear that if an employee or official partakes in any of the disclosed actions that it is grounds for termination. The policy should start with a brief statement outlining what is expected of officials and employees. Officials and employees of the credit union are expected to:

- Conduct the business of the credit union in full compliance with both the letter and spirit of the law and within guidelines established by this policy.
- Recognize that the confidentiality of information must be maintained.
- Recognize and avoid conflicts of interest.
- Protect credit union property, including information, products, services, and assets.
- Properly manage personal finances so they do not interfere with the duties and responsibilities of the official or employee.

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- Treat fairly and with respect all credit union employees, members, and others with whom they interact.

Purpose and Objectives – The purpose of the policy should be clearly defined. The code of conduct policy establishes clear standards of conduct for officials and employees. The policy provides guidance to those performing credit union business to ensure that such activities are performed in compliance with the letter and the spirit of the law.

Authorized Activity – Every policy should clearly state authorized activity and acceptable behavior. The acceptance of fees (including special discounts of any direct or indirect payment of money or property) and other items of value in return for service the credit union renders are generally prohibited. The following exceptions may be allowable:

- Payments of bona fide salary, wages, and fees or other compensation, when these payments are made in the usual course of business;
- Acceptance of gifts, gratuities, or favors based on obvious family or personal relationships (with parents, children, or spouse of credit union officials and employees) where circumstance are clear that the relationship rather than credit union business is the motivating factor;
- Acceptance of meals, refreshments, or entertainment of reasonable value (not to exceed 'X' amount per individual) in the course of a meeting or occasion, provided these expenses are otherwise reimbursable by the credit union as a justifiable business expense;
- Except where prohibited by law, the acceptance of loans from banks or other financial institutions, provided such transactions are made with customary terms and are used to finance legitimate and usual activities by credit union officials and employees;
- Acceptance of unsolicited promotional materials of nominal value (limited to 'X' amount per item and person);
- Acceptance of discounts or rebates on merchandise or services, provided they do not exceed those that are available to other credit union members or the general public;
- Acceptance of gifts of reasonable value (limited to 'X' amount per item and person) on the occasion of recognized events such as job promotions, retirement, etc.
- Acceptance of civic, charitable, educational, or religious awards in recognition of a service performed or an accomplishment; and
- Other activities not identified may be acceptable on a case-by-case basis with prior written approval from the board of directors.

Unauthorized Activities – In general employees and officials are prohibited from soliciting, offering, promising, or accepting anything of value in connection with any transaction or business conducted by the credit union if that individual expects to be rewarded for performing the transaction.

Specific activities will vary depending on the laws within the country; any specific unauthorized activities not addressed below should be included in the code of conduct policy. The following are always considered unacceptable business activities:

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- No director, officer, or employee will solicit or accept anything of value including, but not limited to, gifts, gratuities, fees, amenities, travel, or related expenses in connection with any transaction or business of the credit union.
- Officials and employees are prohibited from having expenses paid for trips or other extensive entertainment by members or suppliers.
- No official or employee may accept a personal fee for arranging a loan from the credit union or from any other person or lending institution.
- No official or employee may receive any monetary considerations in connection with the making of an investment for the credit union.
- No official, employee, or immediate family members may receive a loan that is made with preferential rates, terms, or conditions.
- No official may be related to any employee of the credit union or have a contractual relationship with the credit union.
- No official or employee may be delinquent on a credit obligation with the credit union.
- Officials, employees, or members of their immediate families are prohibited from accepting directly or indirectly any bequest from a member of the credit union. If the official or employee learns of such a bequest in a member's will, they must immediately report all the facts to the supervisory committee and board of directors. In any event, unless the bequest is from a close relative, the official is not permitted to accept it.
- Confidential information regarding any member obtained in the course of business *must not* be used for personal gain; nor should it be revealed to any person outside the credit union without the consent of the member or as otherwise permitted by law.

The code of conduct policy should be reviewed and revised as needed no less than annually. The review should be so noted in the board minutes. The supervisory committee is responsible for the follow-up on any suspicious activity. The committee will report to the board of directors, or to a special meeting of the membership if it concerns the board of directors, any findings that might compromise the integrity of the credit union or be in violation of the code of conduct.

Code of Conduct Statement – As discussed briefly in the introduction, each employee and official should be required to sign a code of conduct statement upon being hired or appointed to their position. Annually, during their appraisal or at the first meeting of the officials preceding the annual general meeting each official and employee should be required to read the code of conduct policy and date and sign a new code of conduct statement.

Below is an example of a code of conduct statement.

CODE OF CONDUCT STATEMENT

I have received a copy of the code of conduct statement and been given an opportunity to review the document and the code of conduct policy. After having read the aforementioned policy, I affirm that:

I do not presently hold a position as an official or employee in another depository institution except as follows:

Name and Address of Depository Institution	Official Capacity	Percentage of Ownership or Interest	Income or Fees Earned in Past 12 Months

I am not presently engaged in any other outside business activity, nor do I have any other outside employment, except as follows:

Business Activity or Employer	Capacity	Hours of Work	Compensation

I have not been a part of any of the activities listed as unauthorized in the policy or partaken in anything that might be considered unethical or a conflict of interest that would disallow me from fulfilling my job duties and responsibilities.

I affirm that the above information is correct.

Date____________________________
Signature__________________________
Staff or Official Position Held ______________________

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Board of Directors Duties and Responsibilities

December 4, 2002

The board of directors is elected by credit union membership during the annual general meeting (AGM) and reports to the general membership. The board members usually serve on a voluntary basis. The board consists of an odd number of directors; the number is normally not less than 5 or more than 9 directors. The board of directors is part of the overall management team that includes a supervisory or audit committee and a credit committee, if the function has not been delegated to professional loan officers. The board of directors has the ultimate decision making authority and responsibility for directing and controlling the affairs of the credit union and providing effective and efficient management of overall operations. The board approves policies that direct operational management and delegate the necessary authority to staff so they can fulfill their job responsibilities. A manager or CEO is in charge of daily operations. The board supervises the manager who reports directly to the board.

Board members have a fiduciary responsibility to their membership. That being said, board members should have a background in business or management. Each board member should be able to assess the financial condition and the operational quality of the credit union. The board should not be reliant on operational management to interpret financial data and other information received. The board must be independent and able to question management about issues they do not understand or are unclear.

Each board member should fully understand their duties and responsibilities. They should receive and review a written job description just as an employee would. The duties and responsibilities should be clearly stated in the job description given to all perspective board members so that expectations are perfectly clear. The following information should be included in the job description of a board member.

Board of Director Job Prerequisites – Each board member must be a member of the credit union and capable of the following so that they are an active and effective part of the board:

- Ability to read and interpret financial statements;
- Basic understanding of laws governing the credit union;
- Knowledge of risk measurement and effective management;
- Knowledge of and a commitment to credit union philosophy;
- Familiarity with asset liability management;
- Familiarity with lending and collections;
- Familiarity with marketing concepts;
- Ability to work as part of a team;
- Able to commit enough time to successfully complete all of the job duties and responsibilities; and
- Strong oral communications skills.

Specific Duties and Responsibilities – These duties and responsibilities should be reviewed not only by prospective board members, but no less than annually by all board members at the meeting immediately following the AGM and the review so noted in the board minutes.

The duties and responsibilities of the board include:

- Attend monthly board and committee meetings, the annual general meeting, any special membership meetings, and the annual planning seminar.
- Reconvene monthly meetings at a later date if a quorum of the board is not present.
- Provide input and participate in decisions of the board.
- Read and evaluate monthly financial reports and other board materials before the meeting.
- Ensure the credit union complies with all applicable legislation.
- Act on all membership applications, either directly or through the appointment of a membership officer.
- Approve credit union policy, financial statements, the annual budget, and the business plan.
- Work with management to develop short and long range planning based on objectives that meet member needs, reflect credit union philosophy, and assure sound operation.
- Perform an annual written appraisal of the manager based on goals established in the budget and business plan.
- Determine the minimum ownership share requirement and the maximum amount of shares that may be owned by one member provided that no member shall hold more than 10% of the total shares amount.
- Authorize the appropriate investment of credit union funds.
- Determine from time to time the services, loan interest rates and terms, deposit interest rates and terms, and types of deposits and loan accounts that the credit union shall offer its membership.
- Authority to declare a share dividend at the AGM only after all expenses and mandatory payments have been made and regulatory requirements met.
- Designate a safe depository for surplus funds and investment.
- Approve any external borrowings of the credit union.
- Employ, establish compensation and duties of the manager, and terminate the manager with due cause.
- Ensure the safe preservation of the credit union's books and records.
- Assess the adequacy of insurance of credit union assets.
- Authorize the manager or such other persons as may be agreed upon, to sign all official documents on behalf of the credit union.
- Authorize the writing off of uncollectible loans and their removal from the books.
- Approve loans to directors, committee members, and the manager by a simple majority vote when the loan exceeds the shares and savings of the director, committee member, or manager.
- Propose amendments to the credit union bylaws, subject to approval by the regulatory authority.
- Plan and reside over all annual and special meetings.

- Report to the AGM on the activities occurring since the last annual meeting, the annual budget, and proposed use of profits for the fiscal year.
- Determine the physical security needs of the credit union.
- Ensure that the monthly board minutes and any board committee minutes are in writing and prepared within 10 days of the respective meeting and verified by the secretary and the presiding officers of the meeting. Such minutes shall contain the names of members present, the date, time, and place of the meeting and a record of material discussions and all decisions made.
- Appoint specific committees and task forces as may be necessary to improve the administration of the credit union and its services.
- Ensure that the credit union's supervisory and credit committees are fulfilling their duties and responsibilities.
- Fill vacancies on the board, credit, and supervisory committees until the next AGM.
- Keep the business of the credit union and its members confidential.
- Disclose all conflicts of interest with any credit union business and refrain from voting on issues related to the conflict of interest.
- Remain current on all credit obligations with the credit union.
- Represent the credit union in the community.
- Promote the credit union and its services as appropriate in day to day interactions.

Upon reading their job duties and responsibilities, each potential board member should date and sign that they have read the document. Their signature implies that they will perform the duties and responsibilities to the best of their ability. The signed document should be retained in the perspective board member's personal file and should be available for review by regulatory authorities.

In addition to reviewing their duties and responsibilities each perspective board member, prior to the AGM and election, should provide their resume or CV to the nominating committee. This information should be retained in their personal file and made available to the membership prior to the election so that each voting member can cast an informed vote. The background information of most interest to the voting membership includes:

- Professional background;
- Education;
- Prior service on a board of directors; and
- Any special skills in the areas of finance, business, marketing/public relations, legal, technological, fund raising, etc.

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Credit Committee/Loan Officer
Duties and Responsibilities
December 5, 2002

The credit committee is elected by the members at the annual general meeting (AGM) or appointed by the board of directors. The method used to staff the committee normally is discussed in the credit union law. The credit committee usually serves on a voluntary basis and reports to the membership or the board of directors, depending if they were elected or appointed. The committee usually consists of not less than 3 or more than 5 members.

In some countries there exists a clause in the bylaws that allows the credit committee to delegate their powers to loan officers. Since loan officers are experienced professionals they are able to grant more complex loans and the credit union can provide additional loan products to the membership. In new or small credit unions with very limited loan products such as share secured, co-signed, and unsecured loans the credit committee is usually capable of evaluating the borrower's ability to repay the loan and making the loan decision. These loan types normally have short maturities, are for small amounts, and the paperwork needed to properly secure the loan is limited to the application and note.

As credit unions grow and expand the array of loan products offered, the use of professional loan officers instead of the credit committee is a good business decision. Vehicle, real estate, business, and agricultural loans are complicated. The documentation to properly secure the loan is extensive and labor intensive. The evaluation of the borrower's ability to repay is also much more complicated; it usually involves financial statement, tax return and cash flow analysis. These loans usually are for a much greater amount and a longer term so the risk posed to the credit union is far greater.

Loan Officer Duties and Responsibilities – Loan officers are employees of the credit union. They report to the loan department supervisor or the general manager. They should have extensive experience in underwriting the loan types offered by the credit union. If the credit committee is able to delegate their authority to a loan officer, the following are their job duties and responsibilities:

- Interview loan applicants, obtain all of the necessary documentation to make the loan decision, properly secure the collateral used to qualify for the loan, and approve the loan.
- Provide information to the membership concerning the different types of loans offered, the terms and interest rates, and the documentation needed to be considered for a loan.
- Make loan decisions in a timely fashion to meet member needs.
- Grant loans according to credit union policy and procedures and in compliance with local law(s).
- Provide financial counseling to members in the wise use of credit.
- Refer all borrower requests for loan extensions, refinances, or any changes to original loan terms to the credit union manager or as designated in policy .

- Make counter offers to borrowers that are creditworthy but can not qualify for the loan they requested.
- Assist management in drafting written procedures that clearly state how each step of the lending process is performed.
- Remain current on all personal credit obligations with the credit union.
- Maintain and keep current the loan officer minutes, include the following for approved loans: borrower account number, borrower name, amount of loan granted, interest rate, maturity, collateral used to secure the loan and any comments, for denied loans include the borrower name, amount of request, collateral offered to secure the loan, and the reason for denial.
- Maintain all loan documents in fireproof containers and ensure that all documents in the loan file are filed according to procedure.
- Participate in training, seminars, and workshops to improve loan underwriting skills and techniques.
- Make suggestions to the manager concerning changes to the lending policy and/or procedures.
- Evaluate the credit union's lending performance annually and compare it to past periods by reviewing a breakdown of the number and dollar amount of loans outstanding by purpose and collateral, total number and amount of loans approved and declined, the total number of borrowers, the ratio of borrowers to members, the average loan size, the delinquent loan to total loan ratio, the net charge off/average loan ratio and the amount of delinquent and charged off loans granted by each loan officer.

These duties and responsibilities should be clearly stated in writing. Prior to hiring a loan officer the credit union manager will want to interview the potential candidate(s) for the job and discuss all their duties and responsibilities with them in detail. Each candidate should date and sign the document outlining their duties and responsibilities. Their signature implies that they have reviewed the document and will perform their duties and responsibilities to the best of their ability. The signed document should be retained in their personal file and should be available for regulatory review. Annually, compliance with this document should be a part of the loan officer's appraisal process.

If the credit union has a credit committee, each credit committee member should fully understand their duties and responsibilities. They should receive and review a written job description just as an employee would. The duties and responsibilities should be clearly stated in the job description given to all perspective committee members so that expectations are perfectly clear. The following information should be included in the job description of a credit committee member.

Credit Committee Job Prerequisites - If the credit union is newly chartered and/or small and a credit committee is used, credit committee members should be:

- A member of the credit union;
- Experienced granting consumer type loans – such as unsecured, co-signed, and share secured loans;
- Capable of evaluating a borrower's financial condition and their ability to repay;

- Capable of evaluating the value of collateral;
- An established member of the community that the credit union serves;
- Familiar with the majority of the membership;
- Knowledgeable of laws governing the credit union and the granting of credit;
- Familiar with the credit union's lending and collection policies and procedures;
- Able to commit enough time to successfully complete all of the job duties and responsibilities; and
- Able to work as part of a team.

Credit Committee Duties and Responsibilities – These duties and responsibilities should be reviewed not only by prospective credit committee members, but no less than annually by the entire committee at the meeting immediately following the AGM and the review so noted in the committee minutes.

The duties and responsibilities of the committee include:

- Meet no less frequently than monthly and more frequently as required by the volume of business referred to the credit committee for decision or review.
- Review applications for loans and make decisions upon such applications within the authority delegated to the committee. All loan decisions must be based on the loan policies established by the board of directors and in compliance with applicable local law(s).
- Provide financial counseling to members in the wise use of credit.
- Act upon the request of a member with respect to amendment of the terms and conditions of a loan provided that such amendment falls within the loan policy.
- Give preference to the smaller loan applications if the need and credit factors are equal should adequate funds not be available to meet all loan demand.
- Review credit union loan and collection policies along with performance. Recommend changes to the policies to improve loan underwriting and collection efforts.
- Evaluate the credit union's lending performance annually and compare it to past periods by reviewing a breakdown of the number and dollar amount of loans outstanding by purpose and collateral, total number and amount of loans approved and declined, the total number of borrowers, the ratio of borrowers to members, the average loan size, the delinquent loan to total loan ratio, and the net charge off/average loan ratio.
- Prepare and present a report at the AGM summarizing the loan activity for the year.
- Remain current on all personal credit obligations with the credit union.
- Appoint loan officers to assume all or part of the loan granting function. Ensure that the loan officers carry out their duties according to all legal requirements, board policies, and credit committee guidelines.

Upon reading their job duties and responsibilities, each potential credit committee member should date and sign that they have read the document. Their signature implies that they will perform the duties and responsibilities to the best of their ability. The signed document should be retained in the perspective committee member's personal file and should be available for review by regulatory authorities.

In addition to reviewing their duties and responsibilities each perspective committee member, prior to the AGM and election, should provide their resume or CV to the nominating committee. This information should be retained in their personal file and made available to the membership prior to the election so that each voting member can cast an informed vote. The background information of most interest to the voting membership includes:

- Professional background;
- Education;
- Prior service on a credit or related committee; and
- Any special skills in the areas of loan underwriting, debt collections, finance, business, legal, etc.

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Credit Union Legislation

December 9, 2002

Credit unions have been important contributors to economic and social development for over 150 years in all regions of the world. Credit unions are now significant participants in the national financial markets of many industrialized, developing and transitional economies. In many jurisdictions, however, legislation has not kept pace with the development of credit unions. Legislative and regulatory deficiencies imperil the safety and soundness of credit unions and restrict their ability to meet their member's financial service needs. Credit unions lacking adequate legislation often find themselves limited in mobilizing savings and making loans to the lower- and middle-income groups they generally serve. Also, they are unable to participate fully in national financial markets, where their services could contribute to greater economic efficiency and expanded development opportunities for current and potential members.

To achieve their potential as full-service financial institutions meeting the saving, borrowing, and related needs of their member's credit unions need to strengthen their safety and soundness. To do this, they need to:
(1) operate under a specialized body of law;
(2) be subject to a specialized supervisory agency with appropriate skills and powers of examination, regulation, and enforcement; and
(3) specialize in financial intermediation.

Leadership of each national credit union system or the entity promoting credit union formation within a country needs to enter into a dialog with government representatives to select the best approach for modernizing the laws governing credit unions. This is usually a slow process, so patience and focus are of the utmost importance.

Creating enabling legislation and supervision is critical to establishing sound, sustainable financial cooperatives/credit unions. Credit unions in most developing countries are not registered or regulated under specific credit union legislation but under cooperative societies acts. An ultimate objective of the credit union movement in any jurisdiction should be the enactment of a specific enabling law for credit unions. While credit unions are cooperative organizations, their specialization in financial services makes them different in many significant respects from other cooperative societies. Thus the general cooperative societies acts which govern the business operations of agricultural, consumer, commercial, and industrial cooperatives are usually inadequate for credit unions, whose operations most closely resemble banking institutions. Microfinance institution legislation generally does not recognize the savings orientation of credit unions. Legislation intended for commercial banks is generally inappropriate for credit unions, whose purpose is to provide cooperative financial services to members who are its depositors, borrowers, and owners. Some of the key features that distinguish credit unions from other cooperatives, microfinance institutions, and commercial banks are:

- Democratic Control by Member-Owners,
- Member Savings Mobilization,

- Ownership Share Contributions,
- Credit Union Capital,
- Return on Savings,
- Diversified Lending Services,
- Character and Repayment Capacity Lending, and
- Access to Financial Sector Services.

Because of these differences, credit unions have been most successful where they operate under specific credit union legislation.

The Credit Union Law – In order to make credit unions legal financial institutions, a law must be passed by Parliament or the legislative body that makes law for the country. This law should be general in nature; so that it does not have to be changed frequently as the credit union system grows and matures. All amendments to the existing law will have to be approved subsequently by the legislative body. This is usually a long, time-consuming process that is best to be avoided if at all possible.

That being said, the law is usually organized in chapters, sections, or parts and articles are used to address each specific point within the chapter, section, or part. The essential structure and content of the core provisions of a unified credit union law should address the following areas:

- Part 1 – Preliminary – The law should begin with identifying general information such as: the name of the law or credit union act, its effective date, the purpose for which credit unions are formed, the legal designation of credit unions, its application to other existing acts or law, and all definitions needed to understand and correctly interpret the law.
- Part 2 – Organizing a Credit Union – This part should present the organizational procedures and criteria to be met by a group wanting to register or incorporate as a credit union and reasons for which the request could be denied by the regulatory authority. It is important to set forth the basic requirements to be met when applying for a charter and details concerning the responsibilities of the regulatory authority during the licensing process. Often the regulatory authority will draft a regulation that addresses this area and the procedures involved in much more detail.
- Part 3 – Powers of a Credit Union – A credit union should be authorized to exercise the basic powers of any corporate entity such as the power to hold and dispose of property, enter into contracts, take part in legal proceedings, and exercise incidental powers. It is important that the law grant these basic powers and it does not restrict the credit union in performing business transactions that would benefit the members and the credit union.
- Part 4 – Membership of a Credit Union - The specifics of credit union membership should be laid out and the chain of command developed within the credit union. This part should establish the requirements for membership in the credit union, limit member liability, and lay out the conditions for termination of membership. In addition, it should also designate that the members, through the annual general meeting, have ultimate control of the credit union where policies are established and direction given to those officials who are delegated to act on behalf of the members.

- Part 5 – Management and Administration – The authority and functions of, as well as constraints on, the board of directors, supervisory committee, credit committee, and the individuals appointed to administer the day-to-day operations of the credit union should be clearly addressed in the law. If term limits for officials are to be instituted they should be addressed in this section. It is important that the duties and responsibilities of each position are well thought out so that the law does not restrict the officials or operational management from effectively and efficiently fulfilling their job duties.
- Part 6 – Shares and Deposits – Credit union representatives drafting the law should ensure that the law allows credit unions to offer all types of share products to members and that members can deposit and withdraw their funds as they want. There are normally two types of financial interests for members – ownership shares and deposits. This section establishes these products as legal offerings, permits the payment of dividends and interest, and provides the conditions for deposits and withdrawals.
- Part 7 – Loans – The law should allow credit unions to grant all types of loans to meet member needs. This part should establish credit granting as a legal credit union activity. General limits on loan terms, conditions, interest rates, and loans to officials should be addressed within this section.
- Part 8 – Investment of Funds and Liquidity – Credit union investments are of secondary importance as compared to member loans. To avoid losses from investments, authorized investments should be limited to those without a risk of loss such as bank deposits or government securities. For this to be accomplished, this part of the law should give a credit union the power to invest for income the accumulated funds that are not on loan to members and allow the credit union to access lines of credit or loans to meet short-term liquidity needs. In addition, it should discuss who is responsible for making policy on investing and liquidity, what are the authorized investments, and what amount or percentage of assets needs to be retained in liquid accounts to meet liquidity demands. Frequently the regulatory authority, in addition to the law, addresses the specifics of investing and liquidity in a separate regulation.
- Part 9 – Capital, Reserves and Allowances – This part should define institutional capital, address minimum capital requirements, disallow the distribution of income in the form of ownership share dividends until the minimum capital requirement has been met, and establish a uniform approach for reserve establishment, allocations, and usage. The credit union's liability should be limited to the extent of it reserves, allowances, and ownership shares. It is very important that the minimum capital requirement is addressed in the law so that newly formed institutions have a sound foundation and will remain an on-going concern well into the future.
- Part 10 – Regulation and Supervision – The basic considerations required for regulating and supervising credit unions should be clearly addressed such as:
  - the general powers of the regulator,
  - the enforcement powers to compel compliance with legislation which should include:
    - merger,
    - involuntary liquidation,
    - conservatorship,

- removal of officials, and
- suspension of the credit union's charter.

Regulatory agencies need to have these powers so that problem and/or insolvent credit unions can be managed and closed, if needed, to protect the member deposits and the integrity of the credit union system. This part also should give the regulatory agency the authority to supervise all the credit unions formed under the law through the issuance of model bylaws, rules and regulations, and prudential standards.

- Part 11 – Voluntary Changes in Organizations – Procedures should be set forth to: merge one credit union with another, consolidate two or more credit unions, wind up the business affairs of a credit union entirely and convert a credit union from registration under another law to registration under the credit union law. It is important that credit unions can voluntarily make these changes because weaknesses or changes in a credit union's membership group, its own leadership or the regional economy in which it operates can sometimes force the credit union to restructure itself or to cease operations completely.
- Part 12 – Credit Union Associations – A credit union association is a secondary support system or "a credit union for member credit unions." It provides an array of programs, services, and systems to assist individual credit unions. It may also include a central finance facility to manage the liquid funds of member credit unions. This section should make these organizations legal, if they are going to be a part of the credit union system developed in the country, and address the authorized purposes and services of such central organizations.
- Part 13 – General Provisions – This part should detail miscellaneous requirements and exemptions related to record keeping, criminal offenses, tax status, the fiscal year, and other items not previously addressed.

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Model Credit Union Bylaws

December 9, 2002

Every credit union must submit proposed bylaws as part of the licensing process. The board of directors should adopt the proposed bylaws upon approval by the regulatory authority and receipt of the license or charter. Bylaws, at a minimum, define:

- the credit union's field of membership,
- the requirements for membership,
- the scope of the credit union's activities,
- the services a credit union can offer, and
- the duties and responsibilities of its officials and operational management..

All officials and management should be familiar with the bylaws to thoroughly understand their job duties, authorities, and responsibilities.

Every regulatory body charged with credit union supervision and regulation should draft model bylaws to facilitate the organization and supervision of credit unions. Model bylaws serve as a guide in drafting a credit union's individual bylaws. Model bylaws allow for some standardization in credit union operations. Credit unions can be permitted to deviate from the model bylaws, however, prior to doing so the proposed change or amendment should have to be submitted to the regulatory authority for approval.

Model bylaws should be divided into sections or chapters with articles that address each specific item within the section. The following are general areas that should be addressed when drafting model bylaws:

- Section 1 – Name, Address, and Legal Designation
  - The credit union's name, address, chartering date, license number, and legal designation should be identified along with its rights, obligations, and restrictions based on the legal designation.
- Section 2 – Credit Union Goals
  - The specific goals for which the credit union was founded should be declared..
- Section 3 – Capital, Shares, and Saving
  - Articles in this section should address: the minimum ownership share deposit, legal age requirement to join, the process for share and savings withdrawals, the right to impose fees for withdrawals, the definition of a dormant account, the process to be followed when handling dormant accounts, and the right to earn interest and dividends.
- Section 4 - Common Bond and Membership
  - The specific common bond should be defined and the membership rights described.
- Section 5 – Handling of Disputes and Member Expulsions
  - The process for handling disputes and expulsions should be described along with valid reasons for expelling a member.
- Section 6 – Membership Meetings
  - Articles in this section should address: when the annual general meeting may be held, the use of regional meetings when credit union membership is large and/or a

large portion of the membership lives far from the home office, each member has only one vote regardless of their volume of business, the definition of a quorum, general issues for discussion at the annual general meeting, the process for calling special meetings, and the information to be noted in meeting minutes.

- Section 7 – Elections
  - Articles in this section should address: when a nominations committee should be appointed, for what reason, by who, how many individuals should be on the committee, how elections are to be held at the annual general meeting, and how terms are to be staggered for officials so that all terms do not expire at once.
- Section 8 – Board
  - The board of directors should be defined as the executive body, which oversees credit union operations in accordance with the general plans and rules laid down at the annual general meeting. To accomplish this, articles in this section should address: their duties and responsibilities, number of members on the board of directors, the appointed positions within the board of directors, how the board is to fill vacancies of the board, how special meetings are to be called, and if the board members will be volunteers or compensated for their time. Prohibitions, disqualifications, and incompatibilities for the board and other governing bodies should also be defined.
- Section 9 – Credit Committee
  - The credit committee should be defined as the entity that acts upon and approves member loan requests. Articles in this section should: establish the number of committee members, specify their duties and responsibilities, identify whether they are volunteers or professional staff, and grant the committee the right to delegate its authority to professional loan officers when they do not have the expertise to grant more complex loans and meet member loan requests.
- Section 10 – Supervisory Committee
  - The supervision committee should be defined as the entity which acts as the internal supervisor of the operations and management of the credit union. To this end, articles in this section should: establish the number of committee members, specify their authorities, duties, and responsibilities, determine its liabilities in case of nonperformance or negligence, and allow the committee to delegate some or all of their job duties to professional internal and external auditors.
- Section 11 – Duties and Responsibilities of Operational Management
  - Along with the duties and responsibilities, this section should clearly state that the general manager reports directly to the board and is ultimately responsible for implementing all board policies, procedures, budgets and business plans.
- Section 12 – Investments of Funds, Cash, and Liquidity
  - This section should: allow the credit union to invest excess funds in interest earning investments, specify that the board establishes all written policies addressing the investment of excess funds, establish a time limit for how long excess funds may be kept on the credit union premises before depositing them into the depository institution, define the size of the change fund that may be used to meet member demands, and state the amount of funds that are to be kept in liquid demand deposit type accounts to meet liquidity needs.
- Section 13 – Annual Budget

- The process for the development and periodic review of the annual budget should be established.
- Section 14 – Payment of Credit Union Expenses and Dividends on Ownership Shares
  - Dividends on ownership shares should be permitted only after all expenses and regulatory capital requirements have been met.
- Section 15 – Reserves
  - This section should specify: how reserve and allowance accounts are to be established, what types of reserve accounts may be established, what accounts are considered to be institutional capital, and that funds in reserve accounts may only be distributed to members upon credit union liquidation and after payment of all outstanding obligations.
- Section 16 – Loans
  - The section should specify: the board is responsible for approving loan policies, the types of loans made, the loan application requirements, the maximum loan amounts, any individuals or groups that are restricted from accessing credit, that a borrower may pay a loan off prior to maturity, and the credit union can assess fees on loans granted and/or delinquent loans.
- Section 17 – Conflict of Interest
  - Every official and employee should be required to disclose any conflict of interest they may have with any business transaction performed with the credit union. Failure to reveal this information should result in removal from office or termination of employment.
- Section 18 – Merger and Liquidation
  - Articles in this section should allow the credit union to voluntarily merge with another credit union or liquidate if the membership and regulatory authority approve the action.
- Section 19 – Amendments and Changes to Bylaws
  - Articles in this section should allow the members to amend the bylaws at an annual general or special meeting. No amendment should be final without the approval of the regulatory authority.
- Section 20 – General Provisions or Miscellaneous Items

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Operational Management Duties and Responsibilities

December 4, 2002

The board of directors delegates to the general manager full responsibility over the daily credit union administration and operations. The general manager reports directly to the board. The manager is responsible for the supervision of credit union employees.

Credit union managers should have experience in managing financial institutions and employees and a financial or business background. Their duties and responsibilities should be clearly stated in writing. Prior to hiring a manager, the board members will want to interview the potential candidate(s) for the job and discuss all of their duties and responsibilities with them in detail. Each candidate should date and sign the document outlining their duties and responsibilities. Their signature implies that they have read the document and will perform the duties and responsibilities to the best of their ability. The signed document should be retained in their personal file and should be available for regulatory review. Annually, compliance with this document should be a part of the manager's appraisal process.

Duties and Responsibilities – This list assumes that the manager is not the only employee; the credit union has an accountant, loan officer, collector, and a cashier. The duties and responsibilities of the manager are:

- Direct and supervise all credit union daily operations.
- Plan, recommend, and implement programs and policies, direct personnel and provide general administrative direction.
- Appraise the general economic environment, anticipate changes in the economy as they may affect credit union operations, and develop and recommend changes so that the credit union remains competitive with the market.
- Prepare and propose to the board changes to credit union policy.
- Ensure that employees follow all of the established board policies.
- Assist in the drafting and implementation of written procedures for each operational area of the credit union.
- Assist the board in developing financial goals.
- Report to the board at the monthly meeting on the financial condition of the credit union and participate in the meeting without voting rights.
- Prepare an annual operating budget and cash flow budget with input from the board.
- Participate in the strategic planning session and develop a long-range business plan with board input.
- Coordinate the publicity and promotion of the credit union.
- Hire and terminate credit union personnel.
- Supervise and appraise in writing all staff members, no less than annually.
- Plan, organize, and staff the credit union to accomplish the objectives of the organization. Propose to the board new staff positions and revisions of the salary schedule.

- Encourage self-development among employees through job training, seminars, workshops, and provide cross training amongst the staff positions to improve member service and enhance internal controls.
- Represent the credit union in business transactions authorized by the board.
- Implement recommendations set forth in the audit reports and those issued by the regulatory body.
- Provide information to the regulatory authority in a timely fashion.
- Authorize budgeted expenditures and sign all documents disbursing credit union funds, if this responsibility has not been delegated to an employee.
- Establish accounting and administrative internal controls to ensure that the credit union's assets are protected from financial mismanagement and fraud.
- Ensure that all accounting records are in balance and up to date and that all financial reports are complete and accurate.
- Ensure that the accounting records are maintained using accrual basis accounting and comply with accepted accounting principles.
- Assist the board in establishing a pricing strategy for products and services.
- Assist the board in determining acceptable types of collateral that can be used to secure credit union loans.
- Make investments in the name of the credit union, if the board has delegated the authority.
- Ensure that there is adequate liquidity to meet loan demand, savings withdrawals, and operating expenses.
- Establish access to loans and lines of credit sufficient to meet short-term liquidity needs.
- Ensure that all legal obligations are met, such as the payment of all taxes, maintenance of sufficient liability insurance for all risks to which the credit union is subject, and compliance with all applicable laws and regulations.
- Remain current on all personal credit obligations with the credit union.

Participate in community affairs to enhance the presence of the credit union in the community.

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Problem Resolution by Credit Union Management

January 9, 2003

Attempting to resolve serious operational problems in addition to running the daily operations of a credit union can be a daunting task. However, many general managers and credit union officials are asked to do just that. Some of the individuals working on the solutions may have been a part of overall management when the problems occurred while others may have entered the credit union only to find that their job is twice as difficult as anticipated. Not only do they have to direct and control daily operations but they have to resolve serious problems that if left unaddressed, could threaten the very existence of the credit union and the livelihoods of all staff members.

Discussed below are some of the most common and potentially serious problems along with suggested solutions. A manager may only have to implement a couple of the solutions to make the necessary operational changes or he/she may have to implement numerous solutions to resolve several problem areas. The problems and suggestions discussed are not mutually exclusive; a suggested solution may provide positive results in several problem areas.

Problem – High, Rising, or Uncontrolled Loan Delinquency is one of the most common problems that can quickly destroy a credit union if management does not locate the cause and remedy the problem(s). A loan is considered delinquent when one payment has been missed. When calculating delinquency the entire outstanding loan balance should always be considered delinquent not just the delinquent payments.

Identifying the Cause of Rising Delinquency – Management must analyze the delinquent loans to determine the cause of the problem. Management might want to ask the following questions to determine the cause:

- When were the delinquent loans granted?
- Were a majority of the delinquent loans granted by the credit committee or one particular loan officer?
- Have there been any employee changes that would affect the quality of loan underwriting or collection efforts?
- Are the loan officers or credit committee adequately trained to grant quality loans?
- Do the delinquent borrowers have anything in common? Are they related? Do they live in the same area? Do they work together? Do they have similar occupations?
- Have the loan underwriting standards decreased as of late in order to increase loans outstanding?
- Do the loan officers or credit committee effectively analyze the borrower's ability to repay the loan granted?
- Are the loan and collection policies and procedures adequate?
- When do collection efforts begin once a loan becomes delinquent? Is this quick enough? Are collection efforts effective? Is the collection department adequately staffed and focused to meet the challenges of high or increasing delinquency?

- Has anyone manipulated the delinquency information in the past to hide delinquency? This can be done by changing the terms in the computer or on the manual loan ledger card or by improper use of loan extensions and refinances.
- Has there been a major event that is beyond the credit union's control such as a natural disaster, a strike, employee layoff, or business closure?

Problem Resolution – Delinquency can have a major impact on the financial condition of the credit union. Because delinquency is high or increasing and borrowers are not making their loan payments, interest on loans decreases, collection expenses increase, the provision for loan loss expense will increase if the loans are considered a potential loss or deemed uncollectible, and capital will decrease due to the negative impact on net income of falling income and rising expenses.

Depending on the cause of the delinquency, management should do a number of things to resolve the problem that will probably include several of the following:

1. Management and the officials should ensure that delinquency is correctly calculated and disclosed. Management should review the delinquency list no less than weekly when delinquency is considered problematic to determine:
   - if collection efforts are effective;
   - the causes for new loans being added to the list; and
   - to ensure that any loans that are removed from the list are done so without improper data manipulations.
2. Management should ensure that the delinquency report is useful. The report should include:
   - Member name;
   - Member account number;
   - Date the loan was made;
   - Original amount of loan;
   - Current delinquent loan balances grouped by age of delinquency (1-2 months, 2-3 months, 3-6 months, 6-9 months, 9-12 months, and greater than 12 months delinquent);
   - Date of last payment;
   - Amount of last payment;
   - If the loan has been extended or refinanced;
   - Member share and savings balances; and
   - Comments.

   This report should be analyzed with the following in mind:
   - The trend in the number and total amount of delinquent loans in each delinquency category;
   - The total number and amount of delinquent loans;
   - The original date the loans were granted;
   - Determining if a majority of the loans were granted by one individual;
   - Determining if the credit union has enough collection staff working in the office and field to handle the level of delinquency; and if lawyers and collection agencies are being used appropriately.

3.Employees working with delinquent loans should perform a review of each loan to determine their collectibility. Any loans that are greater than 12 months delinquent or deemed to be uncollectible, no matter how delinquent they are, should be removed from the accounting records by charging off the loan to the allowance for loan loss account. This will provide for more transparent financial statements and allow collection personnel to concentrate on delinquent loans that are collectible.

4.All charged off loans and loans that are need of legal attention should be given to lawyers or collection agencies for legal action against the delinquent borrower. Management should receive a monthly report from any third party collecting loans to ensure that collected funds are remitted to the credit union and that there is adequate progress on collecting delinquent loans.

5.Management should ensure that interest on loans is not accrued when a loan becomes two months delinquent. Interest should only be recognized upon receipt for all loans two months or more delinquent.

6.Management should determine that the allowance for loan loss account is adequate for all potential loan losses. If it is found to be inadequate it should be increased through the appropriate expense account.

7.Loan delinquency can be fictitiously lowered through extending the maturities of delinquent loans or rewriting the loans as new loans. The use of loan extension and refinances should be strictly limited. Loan extensions are an extension of the term and should be used only when the borrower has the ability to repay the loan but is faced with an unexpected emergency such as a death in the family, hospitalization, or a family crisis. Loan refinancing should be used only when the borrower no longer has the capacity to repay the loan under the original terms but still has the intent, desire, and ability to repay the loan under new terms.

8.If delinquency is high or increasing due to the actions of one specific loan officer, that individual should either be terminated, or removed from the loan officer position and placed in another position or, adequately trained, and only allowed in the future to grant loans under close supervision. If the delinquent loans were granted by a volunteer credit committee, their duties should be delegated, if allowed by law, to a more professional group such as a technical loan committee that is staffed with competent, paid individuals who have proven lending experience.

9.If loan underwriting appears to be the source of the problem, the credit policies and procedures should be revised. Credit should only be granted to those borrowers who have demonstrated their ability to repay. Loan policies should provide guidelines for: loan authorities, loan ceilings, concentration limits, credit information requirements, credit granting, security and collateral, establishing and maintaining interest rates, and the review of files to ascertain compliance with policy and procedures. The credit policy and procedures should be part of the training program for lending staff members.

10. Loan applications should be revised so that they collect the information necessary to determine the members ability to repay such as: number of dependents, sources of all income, employment and salary history, outstanding debts and monthly payments, and credit references.

11. If loan collection practices appear to be at fault, the policies and procedures should be revised. Collection practices should focus on immediate contact with delinquent

borrowers, personal contacts instead of phone calls and letter writing, documentation of all contacts made and promises to pay by the borrowers, and consistent follow-up until the delinquent loans are current. Collection policies should clearly state: when a loan is considered delinquent, when the first contact should be made, how contacts are to be documented, what should be done if the borrower misses a promised payment, when the co-signer should be contacted, when collateral should be repossessed, how repossessed collateral will be sold, and under what circumstances loan extensions, refinances, and work-out plans can be used. The collection policy and procedures should be part of the training for collection staff members.

12. Frequently in credit unions collection activity is an afterthought and the collection work is given to an employee who has some extra time. Management should ensure that collection staff has the experience and disposition or personality necessary to be effective.

Problem – Inadequate or Falling Net Income is another fairly common problem in credit unions. Net income problems need to be addressed quickly because many of the changes that can be made do not have immediate results, they take time to effect net income. Decreases in net income also negatively impact capital. Capital growth comes from net income, if net income is inadequate or decreasing then so is capital.

Identifying the Cause of Inadequate or Falling Net Income – Management must look closely at all operational areas. To assess operations and determine the cause of the inadequate or falling net income, the following questions should be answered:

- Are loan rates competitive with local competition for similar loan products?
- Do the credit union's loan rates cover the cost of funds, operating costs, provision for loan losses, and capital formation needs?
- Has loan delinquency increased or loan demand decreased, therefore reducing the interest collected on loans?
- Is the interest on loans calculated correctly?
- Do the loan interest rates adequately compensate the credit union for the risk present in different loan types and with individual borrowers?
- Are fees for loan origination adequate to cover the associated costs?
- Is excess cash invested in interest bearing accounts?
- Is interest on investments a consideration along with safety and liquidity when making investment decisions?
- Are fees and charges adequate to cover the costs of associated services? Are there fees assessed for abuse of credit union services or to change member behavior such as late loan payment fees or excessive withdrawal fees?
- Are operating expenses reviewed periodically in an attempt to reduce or eliminate unnecessary expenses?
- Are operating expenses within the amount approved in the annual budget?
- Are all operating expenses approved by management?
- Are there large expenditures that can be postponed?
- Have loan collection and provision for loan loss expenses increased due to an increase in loan delinquency?

- Has a new product or service been added that is very costly?
- Are savings interest and share dividend rates above the rates paid by local competitors?
- Do the savings interest and share dividend calculation methods correctly calculate interest and dividends?

Problem Resolution – Like increasing delinquency, falling net income is a serious problem if left unresolved. It can directly affect the credit union's ability to survive in the future. In order to improve net income, management will probably have to take several of the following actions:

1. In order to respond quickly to changes in the marketplace management should have the ability to change loan and savings interest rates and share dividends as needed. At the monthly board meeting the directors can approve any interest rate changes made.
2. Monthly a credit union representative should compare the loan rates offered by the credit union as compared with local competition. If rates are too high, the credit union will only attract those borrowers who can go no where else to get a loan and delinquency will likely increase. If the rates are too low loan income will not be adequate to cover operating expenses, the provision for loan losses, cost of funds, and capital formation needs.
3. In addition to determining that rates are competitive, management should also ensure that the interest rates charged are adequate to cover credit union costs and compensate the credit union for risk present in different loan types and with individual borrowers.
4. An analysis should be performed of the costs associated with granting a loan. Borrowers can be required to pay associated direct costs to improve loan income.
5. To improve loan demand and the resulting loan income, management should ensure that credit union loan products offered meet the needs of the membership. This can be done through a member survey or suggestion box.
6. A cash flow analysis should be performed to:
   - isolate the sources of income funds,
   - determine if excess funds are quickly placed in interest bearing accounts, and
   - explain changes in cash accounts.

   Management should determine that cash is used in the most effective manner and any excess funds are immediately placed in interest bearing accounts.
7. How members use credit union services should be carefully analyzed. Members who abuse credit union service should be assessed fees. For example – There should be fees for late loan payments, excessive withdrawals, or for account balances that fall below an established minimum. In addition, fees should be assessed for member services such as: bill paying, money orders, wire transfers, traveler's checks, or safety deposit boxes.
8. Management and/or the supervisory committee should periodically review operating expenses to determine that all expenses are necessary and if there are ways to decrease or eliminate some expenses. Additionally, management and the supervisory committee should determine that all expenses are properly approved,

are in deed expenses of the credit union, and are within the approved budget amount.

9. Each month a credit union representative should review the savings and share rates offered by local competition. Credit unions should pay average market rates to attract funds. If rates are too high, then money that is "rate sensitive" or looking for yield only will be attracted. When the credit union can no longer pay the higher rate, these funds will likely leave in search of higher rates quite possibly causing a liquidity shortage. If rates are too low, it will be difficult to attract and retain member deposits.
10. To reduce the cost of funds, interest on savings and dividends on shares could be calculated using the low or average account balance for the interest or dividend period. Interest should only be added to accounts at the end of an accounting period or at maturity for fixed term deposits.
11. To lower the cost of funds, management can also establish minimum balance requirements to earn interest for each account type.

Problem – Accounting Records are Out of Balance and/or Seriously in Arrears. On a monthly basis, the general manager should determine that all accounting records are up-to-date and in balance. This is accomplished by reviewing the accuracy of the financial statements and ensuring that each general ledger account balances with its supporting subsidiary ledger. If the records are not verified for accuracy monthly and/or a credit union does not have an adequately trained accountant, or the accountant leaves the employment of the credit union and is not quickly replaced by a qualified individual, or the accountant is on leave and not replaced by a knowledgeable individual, the accounting records can quickly become in arrears and/or out of balance.

Identifying the Cause of the Accounting Deficiencies – Management will want to waste no time in identifying the cause of any accounting problems as the longer one waits the more serious the problem becomes and the harder it is to correct without incurring a loss. Additionally, due to the lack of effective internal controls this is an ideal environment to commit fraud as the accounting entries are not being reviewed and verified. In identifying the causes, management might want to answer the following questions:

- What is the extent of the out-of-balance condition and/or for how long have the accounting records been in arrears?
- Is only one account out of balance or in arrears or are numerous accounts?
- Do the accounts that are out of balance or in arrears have high transaction volumes or will it be fairly easy to bring the records in to balance or up-to-date because the affected accounts have low transaction volumes?
- What is the cause(s) for the out of balance condition and/or the reason(s) for the accounts being in arrears?

Problem Resolution – Once the source of the problem has been correctly identified, management will need to quickly take some or all of the following steps.

1. If the accountant is incapable of balancing the accounts or keeping them up-to-date then this individual should be quickly replaced. They should not be allowed to take

any of their records with them, they will be needed to correct the accounting problems.

2. If the accounting problem is serious, management should consider hiring someone temporarily to bring the accounts in to balance and/or up to date while the accountant ensures that all current transactions are properly accounted for. If the accountant uses their time to resolve past problems, then the current information most likely will not be up-to-date and/or could continue in an out of balance condition, this only makes the problem more serious.
3. The individual that is responsible for bringing the accounts into balance and/or up-to-date should be required to balance all general ledger account balances with subsidiary ledgers, document all of their work in writing, identify any losses due to the lack of adequate accounting, and determine and make (with the assistance of the accountant) the entries needed to correct all of the accounting errors.
4. If the losses can not be resolved, then the losses should be approved by the board of directors and written off to current earnings.
5. To ensure that accounting problems do not occur in the future, management should determine that there are adequate written procedures in place that state at a minimum:
   - All general ledger account balances involving cash and member transactions should be supported by a subsidiary ledger from a source independent of the general ledger such as a bank statement, investment statement, or member savings and loan ledger cards. General ledger accounts that are based on accounting transactions such as fixed and prepaid assets and accrued expenses should be supported by a subsidiary ledger that is based on the cost of the item evidenced by an invoice and depreciated or amortized over the life of the item.
   - Individuals, other than those responsible for making accounting entries, should ensure that the general ledger account totals balance with the subsidiary ledgers monthly.
     - If reconciliations have to be performed then the reconciling items should be reviewed no less than monthly to determine that reconciling items are being researched and cleared in a timely fashion.
   - Accounts should be closed and financial statements finalized no later than the 15th of the following month.

Problem – Credit Union Dependency on External Credit is more common in the developing world due to access to subsidized credit. Credit unions become dependent on this source of credit in bulk however, this dependency seriously changes the characteristics of a credit union from a combination of savers and borrowers to a borrower dominated institution accustomed to low interest loans. With external credit borrowers often have little incentive to repay the loan and credit unions have limited incentive to collect delinquent loans because both parties often believe the funds come from wealthy individuals who live far away. When a credit union loses the subsidized credit source, illiquidity can become a serious problem, as does reeducating membership to repay loans because the loan funds now come from local member deposits instead of foreign credit sources.

Problem Resolution – Resolving this problem is a lengthy process for credit union management that normally involves numerous steps and a complete change in thinking, attitude, and operations. External credit is problematic because the interest rate on the credit is controlled by an outside source, the funds are frequently not available when anticipated or needed, and future funding is at the whim of individuals not involved with the credit union or community. In order to reduce this dependency, credit union management must change their focus from locating and accessing external credit to mobilizing member savings.

1. When accepting member deposits, the credit union has a fiduciary responsibility to protect those deposits from loss. Therefore, prior to promoting savings mobilization any responsible official or manager must first ensure that the credit union is safe and sound. Institutional capital should be adequate to absorb losses and protect member savings. Adequate credit, collections, investment, savings, and internal control policies and procedures should be in place and officials, daily management, and staff members properly trained.
2. Management should survey the membership to determine the savings potential of the community, individual members, and what types of savings products are needed and desired. Based on the survey information a marketing campaign should be initiated that focuses on changing the image of the credit union to one of a safe and sound institution with local savings mobilization as a primary objective.
   - The marketing campaign should focus on aggressive recruitment of members with strong savings potential.
3. Members must be assured that their savings are secure, that access to their funds is convenient, and that they can withdraw their funds when they want.
   - To enhance security, the credit union may want to hire a security guard, install an electronic security system, a vault, locking teller drawers, and bars, or other devices to deter entry through doors and windows. The member's privacy should also be considered. Each member should be able to complete transactions with adequate privacy and all credit union business should be held in strict confidence.
   - Convenient service usually entails having office hours before and after work hours and on the weekend. To extend hours, credit unions also use drop boxes, night depositories, mobile collectors or cashiers, or ATMs.
   - Based on the member survey, management should develop savings products attractive to membership. Generally, the most popular savings product is the regular savings or passbook account that allows members to withdraw their funds as needed. If members are going to make a large withdrawal, they can be required to give prior notice so that liquidity is not adversely effected.
4. Many credit unions have required members to make deposits into non or low- interest bearing ownership share accounts to access credit, this should no longer be required. Members should be encouraged to open savings and deposit accounts at the credit union. Ownership share accounts should pay a fair rate of return, if all capital requirements have been met.
5. In order to attract deposits the interest rates paid on deposits and the terms must be competitive with local competition. To initially attract savings deposits the credit union may offer, for a limited time period, higher interest on certain savings types

or for account balances over a certain amount, or institute a raffle for useful household items. As stated previously, except for promotional periods or if the credit union has a specific use for higher cost funds, the interest paid on deposits should be equal to the average rate paid by the competition so the credit union does not attract "rate sensitive" money that is deposited for the sole reason of earning high interest.

6. The management of liquidity should take on added importance. When external credit is the source for loan funds and there are no loanable funds available, a waiting list is formed and the borrowers wait if no other alternatives exist for obtaining a loan. When member savings are mobilized, credit union management must ensure that there are sufficient funds available to meet, first and foremost, the member savings withdrawals and secondly, loan demand. If a member is told that their funds are withdrawable only to arrive at the credit union and be unable to access funds because of a liquidity shortage, the credit union will quickly lose the confidence of these members and others who learn of the illiquid situation. This could easily cause a run on deposits when members are finally given access, causing a more serious liquidity shortage.

Problem – Share Multiple Lending is Used instead of making lending decisions based on the member's credit history, their ability to repay the loan, the risk associated with the loan purpose, and the value, condition, and resalability of the collateral offered to secure the loan. Share multiple lending effectively restricts the size of the loans available. Only member's who can place a large amount in shares can access larger loans, however, members with a large savings potential frequently do not need loans. Therefore, regardless of a member's income and repayment capacity, the member is not able to acquire a large loan. This practice results in credit unions often being unable to meet member needs for loans to finance housing and commerce. In order to change from the archaic share multiple lending method to a more dynamic lending method management should consider the following:

1. Credit policies and procedures should be revised. Credit should only be granted to those borrowers who have demonstrated their ability to repay. Loan policies should provide guidelines for: loan authorities, loan ceilings, concentration limits, credit information requirements, credit granting, security and collateral, establishing and maintaining interest rates, and the review of files to ascertain compliance with policy and procedures. The credit policy and procedures should be part of the training program for lending staff members.
2. Loan applications should be revised so that they collect the information necessary to determine the members ability to repay such as: number of dependents, sources of all income, employment and salary history, outstanding debts and monthly payments, and credit references.
3. If a volunteer credit committee is currently being used, their duties should be delegated, if allowed by law, to a more professional group such as a technical loan committee that is staffed with competent, paid individuals who have proven experience granting loans based on a borrower's ability to repay. This method requires much more analysis and knowledge than does lending based on a multiple of the share balance.

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4. A credit granting system should be established that has several different tiers of loan approval. Large, longer-term, and risky loans should be approved by all of the technical loan committee. The general manager, credit manager, and credit officers may have different levels of authority for loan approval based on their experience. All credit decisions should be subject to random review by the supervisory or credit committees and the board of directors.
5. The credit union should be adequately compensated for the risk involved in making loans. To this end, loan interest rates and terms should vary according to the risk posed by the loan type, loan purpose, and the individual borrower.
6. The credit union should develop loan products based on member needs and desires. Small, low risk loans should be offered first such as unsecured, co-signer, and share secured loans. As the technical credit committee and individuals granting loans gains experience more difficult, risky loans can be granted such as vehicle, real estate, agricultural, and business loans.
7. Borrowers should be expected to build-up a credit history with the credit union. To establish a credit history borrowers should start with simple, small loans. Members will gain access to larger loans based on their repayment history of the smaller loans and their ability to repay larger amounts. As loan size and risk posed by the loans grows, members should be required to provide collateral to secure the loan and be subject to a more in-depth analysis of their repayment capacity.

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Supervisory Committee Duties and Responsibilities

December 5, 2002

The members at the annual general meeting (AGM) elect the supervisory committee. The supervisory committee members usually serve on a voluntary basis and report to the membership. The committee normally consists of an odd number, not less than 3 or more than 5 members. The supervisory committee's principal objectives are to perform, or select a qualified individual to perform the annual audit, member account verification, and periodic internal audits of operational areas throughout the year.

Because of the technical nature of the supervisory committee it is imperative that the elected committee members have "hands on" experience in accounting and auditing. Very few committees are capable of performing the auditing procedures nor do volunteers usually have enough spare time to adequately perform the necessary audit steps. This being said, it is in the best interest of all credit unions and their members to have a disinterested third party conduct the annual audit at the very least. If the annual audit is performed by a qualified, outside auditor, then the supervisory committee can perform the account verification and internal audits throughout the year. If sufficient funding is not an issue, then the supervisory committee should hire an individual to perform the member account verification and the internal auditing function. This individual should report directly to the committee.

However, many newly chartered or small credit unions can not afford an external auditor, so their only option is to have the supervisory committee perform all auditing functions. The supervisory committee should only be allowed to perform the audit if operations are simple. That is, the credit union offers only the most basic services. Examples of basic services and simple operations are:

- short-term consumer loans – unsecured, share secured, co-signed,
- ownership share accounts,
- term deposits,
- no cash on site,
- investments made at a local financial institution in demand deposit accounts only, and
- limited or no investment in fixed assets.

If the credit union is going to use the supervisory committee to perform the auditing functions, each member should fully understand their duties and responsibilities. They should receive and review a written job description just as an employee would. The duties and responsibilities should be clearly stated in the job description given to all perspective committee members so that expectations are perfectly clear. The following information should be included in the job description of a supervisory committee member.

Supervisory Committee Job Prerequisites – Supervisory committee members should be:

- Experienced in accounting, finance, and/or auditing;

- Experienced in performing external and internal auditing;
- Capable of reading and interpreting financial statements;
- Able to understand and comply with all laws governing the credit union;
- Knowledgeable of all credit union policy and procedures;
- Capable of investigating and resolving any membership complaints or comments made by staff or any other individuals with regards to mismanagement and/or fraud;
- Able to commit enough time to successfully complete all of the job duties and responsibilities; and
- Able to work as part of a team.

Supervisory Committee Duties and Responsibilities – This duties and responsibilities should be reviewed not only by prospective supervisory committee members, but no less than annually by the entire committee at the meeting immediately following the AGM and the review so noted in the committee minutes.

The duties and responsibilities of the committee include:

- Perform or select an external auditor to perform the annual audit of the financial records and books of the credit union.
- Perform or contract with a qualified individual to perform internal audits monthly of:
  - different operational areas to evaluate the books and records for accuracy,
  - the assets for security, and
  - the procedures for the proper handling and use of funds, and make accounting and procedural recommendations regarding internal controls.

  Internal audits should, at a minimum, include the following: physical cash and negotiable item counts, review of investments, bank account reconcilement, random sample and review of outstanding loans and loans granted in the past 6 months, review of loans on the delinquent loan list, compliance with policies and procedures, determination that general ledger accounts balance with their subsidiary ledgers, verification of opened and closed accounts, review of employee savings, shares, and loan accounts, and a review of internal control reports.
- Present all internal audit findings and the annual audit report to the board at their regular monthly meetings. All information should be presented in writing and retained with the board minutes.
- Perform or select an external auditor to perform a 100% verification of the member deposit, share, and loan accounts with the records. A record should be maintained of this verification and the results reported to the board and AGM.
- Follow-up on all recommendations made during the external audits, periodic internal audits, and regulatory exams and ensure they have been implemented.
- Ensure that the credit union complies with the law, regulations, bylaws, AGM resolutions, and established policies.
- Present the annual audit report and the findings at the AGM.
- Remain current on all personal credit obligations with the credit union.
- Receive and investigate any complaint or appeal by members concerning the operations of the credit union.

Upon reading their job duties and responsibilities, each potential supervisory committee member should date and sign that they have read the document. Their signature implies that they will perform the duties and responsibilities to the best of their ability. The signed document should be retained in the perspective committee member's personal file and should be available for review by regulatory authorities.

In addition to reviewing their duties and responsibilities each perspective committee member, prior to the AGM and election, should provide their resume or CV to the nominating committee. This information should be retained in their personal file and made available to the membership prior to the election so that each voting member can cast an informed vote. The background information of most interest to the voting membership includes:

- Professional background;
- Education;
- Prior service on audit or supervisory committees; and
- Any special skills in the areas of finance, accounting, auditing, business, etc.

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