SUPERVISORY AND REGULATORY GUIDELINES
Management of Liquidity Risk
Issued: 22 December 2015

GUIDELINES FOR THE MANAGEMENT OF LIQUIDITY RISK FOR CREDIT UNIONS

1. INTRODUCTION

1.1 The Central Bank of The Bahamas ("the Central Bank") is responsible for the registration, regulation and supervision of all credit unions operating in and from within The Bahamas, pursuant to the Bahamas Co-Operative Credit Unions Act, 2015 ("the Credit Unions Act") and the Central Bank of The Bahamas (Amendment) Act, 2015 ("the CBA"). Additionally, the Central Bank has the duty, in collaboration with financial institutions, to promote and maintain high standards of conduct and management in the provision of credit union services.

1.2 The Central Bank recognizes that credit unions are not-for-profit organizations, and in this respect are different from other deposit-taking financial institutions. The Central Bank is aware that credit unions work as a co-operative, valuing volunteerism, co-operation and member participation. Therefore, the Central Bank is committed to ensuring the unique characteristics of credit unions are maintained, while still fulfilling its obligations to protect the interests of credit union members.

1.3 All registrants are expected to adhere to the Central Bank's registration and prudential requirements, ongoing supervisory programmes and regulatory reporting requirements, and are subject to periodic on-site examinations. Credit Unions are expected to conduct their affairs in conformity with all other Bahamian legal requirements.

2. PURPOSE

2.1 These Guidelines specifically address the minimum liquidity requirements for credit unions. Liquidity is a credit union's capacity to fund increases in assets or meet collateral obligations at a reasonable cost as they fall due, without incurring unacceptable losses. Liquidity must also be sufficient to satisfy demand for cash withdrawals, financing commitments for approved loans, and routine operating cash outflows. Therefore, maintaining an adequate level of liquidity depends on the credit union's ability to meet expected and unexpected cash flows.

2.2 The Central Bank endorses the principles and best practices of the World Council of Credit Unions (WOCCU). Credit Unions are encouraged to refer to these principles and best practices on the WOCCU's website at http://www.woccu.org.

3. APPLICABILITY

1

3.1 These Guidelines apply to all financial co-operative credit unions which are registered under the Credit Unions Act or deemed, by virtue of section 126(1) to be registered under this Act.

4. DEFINITION

4.1 Liquidity risk is the risk that a credit union's financial condition or overall safety and soundness are adversely affected by an inability to meet its contractual obligations. A credit union's obligations and the funding sources used to meet them depend significantly on its business mix, balance sheet structure and the cash flow profiles.

5. MANAGEMENT OF LIQUIDITY RISK

Board and Senior Management Responsibilities

5.1 Ultimate responsibility for the liquidity risk assumed by a credit union and the manner in which this risk is managed rest with the credit union's Board of Directors ("the Board"). Senior management should ensure that the standards set forth in these Guidelines are appropriately addressed.

5.2 Senior management is also responsible for ensuring that board approved strategies, policies and procedures for the day-to-day and long term liquidity management of the operations are appropriately executed within the lines of authority and responsibility designated for managing and controlling liquidity risk.

6. LIQUIDITY RISK MANAGEMENT FRAMEWORK

6.1 Liquidity risk management should be fully integrated into each credit union's risk management processes. Therefore, each institution should have a comprehensive process for identifying, measuring, monitoring and controlling liquidity risk. Critical elements of a sound liquidity risk management framework include:

6.1.1 Effective corporate governance consisting of oversight by the Board and active involvement by senior management in the control of liquidity risk;

6.1.2 Appropriate strategies, policies, procedures and limits used to manage and mitigate liquidity risk;

6.1.3 A process for measuring and monitoring operational liquidity levels;

6.1.4 Conditions for liquidity funding and lines of credit, (inclusive of the aggregate maximum amount of any such lines of credit);

6.1.5 A process for monitoring large deposits, the withdrawal of which could impact the level of operational activity;

6.1.6 Internal controls and internal audit processes sufficient to determine the adequacy of the liquidity risk management process; and

6.1.7 Appropriate contingency funding plans that sufficiently address potential adverse liquidity events to which the institution may be exposed and emergency cash flow requirements.

6.2 The Central Bank will review these critical elements in its assessment of each credit union's liquidity risk management framework, during the course of its on-site examination.

7. LIQUIDITY RISK MEASURMENT AND MONITORING

7.1 Credit unions should comply with the minimum liquidity requirements prescribed under Regulation 15 of the Bahamas Co-Operative Credit Unions Regulations, 2015 (the Regulations).

7.2 Credit unions should also comply with their statutory reserve requirements prescribed in Regulation 14 of the Regulations, 2015.

7.2.1 Where a credit union cannot meet its statutory reserves allocation requirements as set out under Regulations 14, it may apply to the Central Bank in writing for an exemption from this requirement.

7.3 In addition to meeting the Apex Body's reserve requirements, each credit union shall have no less than 10% of its members' savings deposits in liquid assets or demand deposit type accounts to provide sufficient liquidity for share and savings withdrawals, external borrowing repayments, loan demand and operating expenses. Credit unions must also maintain operational liquidity of 15% - 20%, in easily accessible instruments and accounts in compliance with the requirements under PEARLS and the WOCCU Safety and Soundness Principles.

Liquidity Ratio

7.4 This ratio shall be reported to the Central Bank as prescribed. The liquidity ratio calculation is as follows:

Liquid Assets (those with no maturity or a maturity of less than 30 lays) **minus Liabilities** (due in 30 days or less)

Total Deposits

Liquidity ratio range 15% - 20%
Net Loans / Total Asset Ratio range 70% - 80%

7.5 A credit union should strive to maintain a loan to asset ratio sufficient to meet members' loan demand and still meet other liquidity needs. A high loan to asset ratio (e.g., in excess of percent) may stress liquidity, especially if the credit union has limited other funding sources, existing funding depends on volatile sources (e.g., non-member shares), or the credit union has minimal short-term investments.

8. ASSET LIABILITY MANAGEMENT (ALM) POLICY

8.1 The credit union's Board of Directors shall be responsible for formulating, reviewing and adjusting the liquidity/ALM policy. The policy shall address:

8.1.1 Who is responsible for liquidity management and ALM;

8.1.2 Who may access or establish a line of credit for liquidity purposes;

8.1.3 How will liquidity be monitored: for example, what liquidity management systems will be used, what time frames will be used in cash flow analysis, their level of detail and the intervals for updating ratio and cash flow analysis;

8.1.4 Minimums and maximums for total cash assets and for the amount to be kept on-site at the credit union;

8.1.5 Minimums and maximums for other liquidity related ratios;

8.1.6 What process or method will be used to monitor ALM; and

8.1.7 How often the ALM position will be analyzed and discussed.

8.2 The board shall annually review and revise the policy as needed.

9. CONTROL AND AUDIT

9.1 Credit unions should have appropriate internal controls addressing relevant elements of the risk management process, including adherence to policies and procedures, the adequacy of risk identification, measurement, reporting and compliance with applicable rules and regulations.

9.2 Senior management should ensure periodic reviews and assessment of various components of the credit union's liquidity risk management processes. A qualified, licensed independent party, i.e. internal and external auditors, should perform such reviews and assessments.

9.3 All weaknesses or problems identified in the review should be brought to the attention of senior management for prompt corrective action. The reviews and assessment should cover the following areas:

9.3.1 Adequacy of risk identification, measurement, reporting and compliance with supervisory guidance (including statutory liquidity ratios/limits) and industry sound practices;

9.3.2 Suitability of the underlying assumptions for conducting cash flow analyses;

9.3.3 Integrity and usefulness of management information system reports; and

9.3.4 Adherence to established liquidity policies and procedures.

10. MANAGEMENT INFORMATION SYSTEM

10.1 Credit unions should have a reliable management information system ("MIS") consistent with the size and nature of their operations. This will measure, monitor and control liquidity risk under normal and stressed conditions. MIS should be able to capture all sources of liquidity risk, including contingent risks and the related triggers and those arising from new activities. The system should have the ability to deliver more granular and time sensitive information during periods of stress.

10.2 The MIS should particularly be able to:-

10.2.1 Calculate and project various liquidity related limits and ratios, including statutory requirements, and for internal risk management purposes;

10.2.2 Set out clearly the assumptions and limitations underlying cash flow management reports;

10.2.3 Generate timely reports on risk measures and liquidity trends for management;

10.2.4 Check compliance with established liquidity policies and limits, and generate exception reports.

11. REPORTING REQUIREMENTS

11.1 The Central Bank will monitor the liquidity position of the credit union on an ongoing basis to satisfy itself that the liquidity risk is being appropriately managed, taking into account the nature, scale and complexity of the credit union's operations. As part of this process, the credit union is expected to:

11.1.1 Provide the Central Bank with a copy of its liquidity risk management strategy; and

11.1.2 Report on its liquidity position via the Maturity Schedule of the Excel Reporting System (ERS) on a monthly basis, for large credit unions.

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