World Council

June 21, 2019

Delivered Via Email: fsb@fsb.org

Randal K. Quarles
Chair
Financial Stability Board
Bank for International
Settlements CH-4002
Basel,
Switzerland

Re: *Evaluation of Too-Big-To-Fail Reforms ("TBTF Evaluation")*

Dear Chair Quarles:

World Council of Credit Unions (World Council) appreciates the opportunity to comment on the Financial Stability Board's (FSB) *Evaluation of Too-Big-To-Fail Reforms ("TBTF Evaluation").*[1] Credit unions are cooperative depository institutions and World Council is the leading trade association and development organization for the international credit union movement. Worldwide, there are over 68,000 credit unions in 109 countries with USD 1.8 trillion in total assets serving 235 million physical person members.[2]

There is no doubt the financial crisis exposed numerous weaknesses in the financial markets. To that end we applaud many of the reforms that have been implemented that have resulted in a strengthened and more resilient financial system.

While we acknowledge the importance of many of the reforms —particularly for Systemically Important Financial Institutions (SIFIs) and complex international banks— the complexity, usefulness, and corresponding regulatory burden and costs for smaller non-systemically important credit unions often becomes questionable, particularly those that are only involved in deposit taking and simple retail consumer lending.

[1] Financial Stability Board, *Evaluation of Too-Big-To-Fail Reforms ("TBTF Evaluation)* (May. 2019), *available at* https://www.fsb.org/2019/05/fsb-launches-evaluation-of-too-big-to-fail-reforms-and-invites-feedback-from-stakeholders/.
[2] World Council of Credit Unions, *2016 Statistical Report* (2017), *available at* http://www.woccu.org/publications/statreport.

World Council of Credit Unions, Inc.
99 M Street SE, Ste 300, Washington, DC 20003 • +1-202-638-0205 • +1-202-638-3410
www.woccu.org

While the reforms applicable for Global-Systemically Important Banks (G-SIBs) and Domestic-Systemically Important Banks (D-SIBs) are likely appropriate, our concern comes in the lack of clarity in the implementation for those that are neither D-SIBs or G-SIBs.

Credit Unions and other community-based cooperative depository institutions are not systemically important on a global or domestic level. Their operations are far less complex than those of G-SIBs, D-SIBs or internationally active banks and thus we question whether the supervisory usefulness of the reforms for these types of community-based institutions justifies the attendant compliance burdens.

What we observe occurring, absent the specific clarity in the reform standards, is that national authorities tend to apply these standards without regards for proportional tailoring to the risk or complexity of a credit union or other community-based mutual depository institution. This is particularly true in jurisdictions that contain institutions that are of large size compared to other local credit unions or where the credit union or other mutual is of large size relative to the capitalization of the local deposit insurance fund or other savings guarantee scheme.

Thus, our comments herein are focused on the broader effect of the reforms and the effects on credit unions and other community-based mutual depository institutions.

I. De-Risking/AML/CFT

In the recent Progress Report on FSB's Action Plan to Assess and Address the Decline in Correspondent Banking[3], FSB notes that the decline in the number of correspondent banking relationships remains a source of concern for the international community, as the number of active correspondent banks declined by 3.4% in 2018, bringing the cumulative decline since 2011 to 19.3%, with concentration increasing with fewer correspondent banks handling payments. This remains a concern for many of our credit unions who are often challenged to establish relationships to provide effective banking solutions, often to underserved populations. It is a particular concern to credit unions located in the Caribbean.

May of the issues arise out of the application of anti-money laundering/countering the financing of terrorism (AML/CFT) regulations and in particular the lack of proportional application of these provisions, but also from the corresponding burden associated with many of the pos-crisis reforms. We urge the continued efforts of the FSB in this area to address this critical area.

[3] Financial Stability Board, *Progress Report, Action Plan to Assess and Address the Decline in Correspondent Banking* (May 2019) *available at* https://www.fsb.org/wp-content/uploads/P290519-1.pdf.

World Council of Credit Unions, Inc.
99 M Street SE, Ste 300, Washington, DC 20003 • +1-202-638-0205 • +1-202-638-3410
www.woccu.org

II. Basel III

The finalization of Basel III is in an important milestone in the reforms. We applaud the inclusion of a proportional regulatory approach to market risk reserves that will help limit compliance burdens on credit unions and other community-based depository institutions. We further strongly supported the decision to significantly reduce the amount of additional reserves community-based institutions will be required to hold against interest rate swaps and caps under the simplified approach.

While these important items are included in the final standards, we continue to be concerned about the practice of "gold-plating" where jurisdictions adopt standards exceeding the standards. We urge FSB to continue reinforcement of the principle of proportionality included in the standards providing that effective implementation of the Basel framework does not require its application to all institutions in a particular jurisdiction. Further, enforcement of the principal that implementation of the standard is not a one size fits all approach and that consideration of the size and complexity of its activities and its international presence is key to tailoring the standard[4].

Specifically, WOCCU continues to urge for clearer guidance on the factors appropriate for national level regulators to consider when developing proportionate approaches. A set of high-level principles or weighing-factors would be useful on when less complex approaches are appropriate such as:

- Whether the institution has cross-border operations;
- The complexity of the institution's assets and liabilities;
- The asset-size of the institution;
- The extent of the institution's leverage;
- The institution's interconnectedness with the financial system;
- The degree to which the institution reports to multiple prudential supervisors;
- The extent and nature of the institution's off-balance-sheet exposures; and
- The mix of business activities of the institution, such as whether it engages in community banking, commercial banking and/or investment banking.

[4] *See, e.g.*, Basel Committee on Banking Supervision, *Core Principles for Effective Banking Supervision*, at ¶4 (Sep. 2012) ("[T]he Committee has sought to achieve the right balance in raising the bar for sound supervision while retaining the Core Principles as a flexible, globally applicable standard. By reinforcing the proportionality concept, the revised Core Principles and their assessment criteria accommodate a diverse range of banking systems. The proportionate approach also allows assessments of compliance with the Core Principles that are commensurate with the risk profile and systemic importance of a broad spectrum of banks (from large internationally active banks to small, non-complex deposit-taking institutions)"), *available at* https://www.bis.org/publ/bcbs230.pdf.

World Council of Credit Unions, Inc.
99 M Street SE, Ste 300, Washington, DC 20003 • +1-202-638-0205 • +1-202-638-3410
www.woccu.org

Without such increased proportionality, the disproportionate regulatory burdens associated with Basel III will continue to exacerbate the "Too-Big-To-Fail" problem by increasing the market power of the largest deposit-taking institutions while increasing consolidation among community-based deposit taking institutions.

III. Stress Testing

Similarly, with stress testing, we have observed the application of over-burdensome requirements by national level-supervisory authorities. We acknowledge and agree that stress testing is an important regulatory and management tool —particularly for SIFIs and complex international banks— but again, the usefulness, and corresponding regulatory burden and costs for smaller non-systemically important credit unions becomes questionable.

We urge FSB to continue to reinforce the concept that authorities should consider their corresponding costs and the likely benefit that they will obtain from a supervisory perspective before implementing any requirements on their regulated entities, in order further to reinforce proportional application of stress testing to regulated institutions based on their size, complexity, and cross-border operations (or lack thereof).

IV. Over-The-Counter Derivatives

World Council urges the FSB to continue to seek to create incentives to centrally clear interest rate swaps for all firms, including the smallest and least active, to help better ensure that credit unions and other community-based depository institution can continue to hedge interest rate risk using interest rate derivatives at fair rates. We urge the FSB to continue seeking the design of such incentives or to mandate fair and affordable access to centrally cleared interest rate derivatives for all users and to reduce the standardized approach for measuring counterparty credit risk exposures (SA-CCR) capital requirements to help better ensure continued access to interest rate derivatives for smaller uses

V. TLAC

We urge the FSB to maintain the final version of the standard related to the Total Loss Absorbing Capacity (TLAC) standard such that it only applies to Global-Systemically Important Banks (G-SIBs) and institutions subject to Basel III that invest more than 5% of their common equity in convertible bonds or other TLAC instruments issued by G-SIBs Credit unions and other mutuals subject to Basel III will therefore only be impacted by this new Basel standard if they invest an amount more than 5% of their "common equity Tier 1" capital (i.e. retained earnings and most types of perpetual capital shares) in convertible bonds or other TLAC

World Council of Credit Unions, Inc.
99 M Street SE, Ste 300, Washington, DC 20003 • +1-202-638-0205 • +1-202-638-3410
www.woccu.org

instruments issued by a G-SIB. We believe this is appropriate given the size and complexity of credit unions and other mutuals.

World Council appreciates the opportunity to comment on the FSB's *Evaluation of Too-Big-To-Fail Reforms*. If you have questions about our comments, please feel free to contact me at aprice@woccu.org or +1-202-843-0704.

Sincerely,

Andrew T. Price
Vice President of Advocacy
World Council of Credit Unions

World Council of Credit Unions, Inc.
99 M Street SE, Ste 300, Washington, DC 20003 • +1-202-638-0205 • +1-202-638-3410
www.woccu.org