World Council

Feb 9, 2018

Sent via email
Mr. Gerben Everts
Chair
The Monitoring Group
c/o International Organization
of Securities Commissions
(IOSCO)
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Re: Monitoring Group Consultation: *Strengthening the Governance and Oversight of the International Audit-Related Standard-Setting Boards in the Public Interest*

Dear Chair Everts:

World Council of Credit Unions (World Council) appreciates the opportunity to comment on the Monitoring Group's Consultation: *Strengthening the Governance and Oversight of the International Audit-Related Standard-Setting Boards in the Public Interest*.[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 60,000 credit unions in 109 countries with USD 1.8 trillion in total assets serving 223 million physical person members.[2]

Question 1: *Do you agree with the key areas of concern identified with the current standard setting model? Are there additional concerns that the Monitoring Group should consider?*

World Council supports increasing the independence of accounting and auditing standard setting and also supports staffing standard-setting boards with professionals who have relevant industry experience with respect to institutions subject to these standards, such as community banking industry experience and experience with cooperatives.

World Council does not, however, support increasing the frequency of issuing

[1] The Monitoring Group, Consultation: *Strengthening the Governance and Oversight of the International Audit-Related Standard-Setting Boards in the Public Interest* (Nov. 2017), *available at* https://www.iosco.org/library/pubdocs/pdf/IOSCOPD586.pdf.
[2] World Council of Credit Unions, *2015 Statistical Report* (2016), available at https://www.woccu.org/documents/2015_Statistical_Report_WOCCU.

international standards.

Regarding timeliness of issuing international standards, World Council believes that the public interest is best served by the well-considered development of standards that are relevant and practical for all forms of corporate organization, including cooperative depository institutions. Absent exigent circumstances—such as in the case of a new standard causing unintended consequences—World Council believes that the pace of standard promulgation cannot likely be increased significantly without decreasing the relevance of the standard for a significant portion of users of the standard (because of decreased stakeholder input), which would likely lead to new standards creating unintended consequences more frequently.

Rapidly changing standards also create unnecessary business uncertainty and regulatory compliance burdens on industry. This is because institutions subject to changing rules must bear the costs of updating their systems to comply with the new standards. These institutions can also face difficulties with respect to long-term planning when applicable standards are in flux.

World Council supports increasing the independence of standard setting and also supports staffing standard-setting boards with professionals who have relevant industry experience. World Council does not, however, support increasing the frequency of issuing international standards.

Question 2: *Do you agree with the overarching and supporting principles as articulated? Are there additional principles which the Monitoring Group should consider and why?*

World Council supports the overarching and supporting principles that the Monitoring Group has articulated in this consultation regarding developing standards in the public interest with independence, credibility, cost effectiveness, relevance, transparency, and accountability. We urge the Monitoring Group to finalize these principles as proposed.

Cost-effective and relevant standards are especially important with respect to limiting unnecessary regulatory burdens on community-based financial cooperatives.

Regarding cost-effectiveness, World Council believes that standard setting bodies performing quantitative cost-benefit analyses are essential to determining whether a proposed standard meets the Group's proposed statement that "expected benefits of proposed standards or changes to standards should justify the cost of any required changes." We urge the Monitoring Group to urge international standard setting bodies to include quantitative cost-benefit analyses using reasonable assumptions as part of their consultative processes.

Regarding relevance, cooperatives and other mutually organized legal entities perform important roles promoting the public interest—such as credit unions and other mutuals promoting financial inclusion and financial stability—but have corporate legal structures that materially differ from joint-stock companies. In addition, the relevance of a standard's application to cooperatives is based on the standard faithfully representing the institution's true economic value. Input from financial cooperatives regarding proposed standards should be considered seriously by policymakers to help ensure the standard's relevance both in terms of faithful representation of the institution's financial position as well as to help promote the public interest of maintaining confidence in the financial system.

World Council supports the overarching and supporting principles that the Monitoring Group has articulated in this consultation regarding developing standards in the public interest with independence, credibility, cost effectiveness, relevance, transparency, and accountability. We urge the Monitoring Group to finalize these principles as proposed.

Question 3: *Do you have other suggestions for inclusion in a framework for assessing whether a standard has been developed to represent the public interest? If so what are they?*

We urge the Monitoring Group to urge international standard setting bodies to help limit unnecessary regulatory burdens on community-based cooperative depository institutions by:

(a) Using quantitative cost-benefit analyses as part of their consultative processes; and

(b) Ensuring the relevance of their standards to all types of business enterprises, including cooperative depository institutions, by seriously considering input from a wide range of public stakeholders in the standard development process.

Question 8: *Do you agree that the focus of the board should be more strategic in nature? And do you agree that the members of the board should be remunerated?*

Yes, World Council supports a more strategic focus of the board that includes "multi-stakeholder (non-professional)" board members, especially board members experienced with community-based banking institutions and cooperatives. We believe that multi-stakeholder board members will help the board develop standards that better serve the public interest through being more cost-effective and relevant to all types of business enterprises.

World Council also supports remunerating members of the board in order to attract and retain the best qualified individuals to help develop international standards.

Question 9*: Do you agree that the board should adopt standards on the basis of a majority?*

No, World Council does not agree that the board should adopt standards on a majority basis. We believe that building consensus on the board for a final standard is in the public interest and essential for achieving international standards that are relevant and practical for a wide diversity of business enterprises including cooperative depository institutions and other mutually organized legal entities.

Credit unions and other mutual depository institutions, as well as other types of mutuals such as mutual insurance companies, form an important part of the financial systems of many jurisdictions around the world and are often subject to audits pursuant to international auditing standards. Community-based cooperative financial institutions promote the public interest by promoting financial stability and financial inclusion. Regarding financial stability, community-based financial cooperatives contribute importantly to a more resilient financial system because their assets are spread over many independent balance sheets (reducing concentration risk and contagion risk in the financial system) and because community-based institutions operate using a less-risky business model than large commercial banks.

Credit unions and mutual banks typically use traditional community banking models and operate for the purpose of promoting thrift and providing their members, who are also the owners of the cooperative, with financial services at fair rates. Credit unions and mutual banks also are typically much smaller than internationally active banks and—because of their smaller asset size, independent balance sheets and conservative business model—represent less risk to the financial system and to savings guarantee schemes than do systemically important institutions.

Changes in accounting, auditing and other international standards designed to address weaknesses at joint-stock companies can have unintended regulatory effects on credit unions and mutual banks. Careful deliberation and consultation with industry by international standard setting bodies regarding international standards for cooperative depository institutions, however, has typically resulted in relevant, practical and effective international standards that promote financial stability while being compatible with cooperatives' and other mutuals' corporate structures.

For example, regarding whether shares issued by financial cooperatives can qualify as regulatory "common equity Tier 1" (CET 1) capital under Basel III, the Basel Committee on Banking Supervision's willingness to consider carefully the views of credit unions and cooperative banks resulted in a practical framework for cooperative shares to qualify as CET1 capital if the shares have sufficient permanence and the ability to absorb losses on a going-concern basis.[3] Cooperative depository

[3] *See* Basel Committee on Banking Supervision, *Guidance on the application of the Core Principles for Effective Banking Supervision to the regulation and supervision of institutions relevant to financial inclusion*, at 22 n. 55 (Sep. 2016), *available at* https://www.bis.org/bcbs/publ/d383.htm ("Member shares

institutions' subsequent consultations with national-level supervisors have resulted in regulatory approval for cooperative depository institutions to issue CET1 capital shares in jurisdictions including the European Union, Australia and Canada.[4]

These CET1 cooperative shares are equivalent to joint-stock company common equity shares and can absorb losses on a going-concern basis, providing increased protection to the institution's depositors and to any applicable deposit insurer or other savings guarantee scheme. The enhancements to institutional and systemic financial stability provided by these regulatory capital CET1 shares, however, would have been difficult to achieve without policymakers considering carefully how best to design international standards that were relevant, effective and compatible with the cooperative depository institution model.

Similarly, producer cooperatives and service cooperatives, such as electrical cooperatives and agricultural cooperatives, also represent significant business sectors in many jurisdictions and often are audited pursuant to international auditing standards as well.

Like credit unions and mutual banks, these producer and service cooperatives can present unique or complex accounting questions that are best resolved through a thorough consideration of the cooperatives' corporate structure, business model, and corporate purpose (such as existing to serve its members rather than to maximize

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issued by mutual and cooperative banks could be treated as common equity for regulatory purposes provided that they meet the permanence and loss absorption criteria, as per BCBS (2011). This issue is under discussion in conjunction with the evolution of international capital standards. National regulators are encouraged to use their discretion to adjust their capital definitions and other elements of regulatory capital requirements to align with emerging guidance and sound practices."); Basel Committee on Banking Supervision, *Basel III: A global regulatory framework for more resilient banks and banking systems*, at 14 n.12 (June 2011), *available at* https://www.bis.org/publ/bcbs189.htm ("The [Common Equity Tier 1 capital] criteria also apply to non-joint stock companies, such as mutuals, cooperatives or savings institutions, taking into account their specific constitution and legal structure. The application of the criteria should preserve the quality of the instruments by requiring that they are deemed fully equivalent to common shares in terms of their capital quality as regards loss absorption and do not possess features which could cause the condition of the bank to be weakened as a going concern during periods of market stress. Supervisors will exchange information on how they apply the criteria to non-joint stock companies in order to ensure consistent implementation.").

[4] *See* Australian Prudential Regulation Authority (APRA), *Prudential Standard APS 111: Measurement of Capital*, at 58-63 (Nov. 2017), *available at* *https://www.legislation.gov.au/Details/F2017L01591/Html/Text#_Toc499554591*; Office of the Superintendent of Financial Institutions (OSFI) of Canada, *Capital Adequacy Requirement (CAR) Guideline*, §§ 2.1.1.1(5), 2.1.2, 2.2 (Dec. 2016), *available at* http://www.osfi-bsif.gc.ca/Eng/fi-if/rg-ro/gdn-ort/gl-ld/Pages/CAR17_chpt2.aspx; *Commission Delegated Regulation (EU) No 241/2014 of 7 January 2014 supplementing Regulation (EU) No 575/2013 of the European Parliament and of the Council with regard to regulatory technical standards for Own Funds requirements for institutions*, 2014 O.J. (L74) 8, *available at* http://eur-lex.europa.eu/legal-content/EN/ALL/?uri=CELEX%3A32014R0241; *see also Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012*, Arts. 26-29, 2013 O.J. (L176) 1, 37-40, *available at* http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex:32013R0575.

profits) to ensure the standard's relevance vis-à-vis representing the cooperative enterprise's true economic value.

World Council believes that building consensus on the board for a final standard is in the public interest and essential for achieving international auditing standards that are relevant and practical for a wide diversity of business enterprises including cooperative depository institutions and other mutually organized legal entities.

Question 10: *Do you agree with changing the composition of the board to no fewer than twelve (or a larger number of) members; allowing both full time (one quarter?) and part-time (three quarters?) members? Or do you propose an alternative model? Are there other stakeholder groups that should also be included in the board membership, and are there any other factors that the Monitoring Group should take account of to ensure that the board has appropriate diversity and is representative of stakeholders?*

World Council supports increasing the representation of stakeholders with community-banking and cooperative depository institution experience in the board's membership. Credit unions and other community-based cooperative depository institutions are impacted significantly by international auditing standards as well as especially by accounting standards concerning the definition of equity and the recognition of expected credit losses. Increasing the representation of professionals with community banking and cooperative industry experience is in the public interest because it will increase international standards' relevance for cooperative depository institutions and other types of cooperatives, as well as help prevent standards from creating unintended consequences such as excessive compliance burdens.

For example, accounting standards concerning the definition of equity and the recognition of credit losses, and auditing compliance with those rules, can have macroeconomic impacts on national economies by affecting the availability of credit to local consumers and businesses. This is especially true with respect to credit availability to consumers and small and medium-sized enterprises (SMEs) in most jurisdictions, as well as for businesses of all sizes located in smaller jurisdictions. Smaller jurisdictions do not typically have deep and liquid securities markets and therefore rely primarily on funding from banking institutions to provide capital in their economies.

In addition to audit compliance burdens, community-based banking institutions, including financial cooperatives, currently face high regulatory compliance costs in general. Internationally active banks are better able to absorb these regulatory compliance costs because of their larger economies of scale. The steady increase of regulatory compliance costs for banking institutions around the world has contributed significantly to a long-term merger trend among community-based depository institutions—to achieve larger economies of scale that can better absorb applicable regulatory burdens—in many jurisdictions around the world.[5]

Including stakeholders with community-banking and cooperative depository institution experience on the board would help maintain a proportional and relevant standard setting approach that serves the public interest by promoting financial stability and transparency without creating unintended consequences or imposing unnecessary regulatory burdens on community-based depository institutions.

Question 12: *Do you agree to retain the concept of a CAG with the current role and focus, or should its remit and membership be changed, and if so, how?*

World Council agrees with the general concept of retaining a Consultative Advisory Group (CAG), however, World Council believes that a larger CAG with a broader multi-stakeholder composition would better serve the public interest by helping to develop standards that are more relevant and practical for a wide diversity of business enterprises, including cooperative depository institutions.

One potential model for a larger, more diverse CAG would be the Financial Action Task Force's Private Sector Consultative Forum. Private Sector Consultative Forum members are invited by the Financial Action Task Force to provide comments regarding proposed international standards at an in-person consultative meeting that is usually held at least once per year. These consultative meetings operate under the Chatham House Rule. The Private Sector Consultative Forum's membership includes a wide representation of private-sector stakeholder organizations affected by anti-money laundering/countering the financing of terrorism compliance rules.

World Council agrees with the general concept of retaining a CAG, however, World Council believes that a larger CAG with a broader multi-stakeholder composition similar to the Financial Action Task Force's Private Sector Consultative Forum would better serve the public interest.

Question 13: *Do you agree that task forces used to undertake detailed development work should adhere to the public interest framework?*

Yes, World Council agrees that task forces used to undertake the development of detailed standards should adhere to the public interest framework. We believe that any standard setting work that affects members of the public, including cooperative depository institutions, should adhere to the Monitoring Group's public interest framework.

Task forces typically work on more detailed standards to address technical issues

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[5] In the USA, for example, there were 16,277 credit unions in December 1987. Thirty years later, largely as a result of voluntary mergers, there were 5,767 credit unions in the USA in December 2017. *See* Credit Union National Association of the USA, *Monthly Credit Union Estimates*, at 4 (Dec. 2017), *available at* https://www.cuna.org/About-Credit-Unions/Credit-Union-Data---Statistics/.

that were not resolved as part of an overarching standard. One example is International Financial Reporting Interpretations Committee Interpretation 2 (IFRIC Interpretation 2) *Members' Shares in Co-operative Enterprises and Similar Instruments*,[6] which addresses under what circumstances cooperative shares qualify as equity on an accounting basis.

We believe that the work undertaken by task forces, as well as any other standard setting process affecting cooperative depository institutions and other members of the public, should adhere to the Monitoring Group's public interest framework.

Question 15: *Do you agree with the role and responsibilities of the PIOB as set out in this consultation? Should the PIOB be able to veto the adoption of a standard, or challenge the technical judgements made by the board in developing or revising standards? Are there further responsibilities that should be assigned to the PIOB to ensure that standards are set in the public interest?*

Yes, World Council agrees with the proposed role and responsibilities of the Public Interest Oversight Board (PIOB) as set out in this consultation, and also urges the Monitoring Group to increase the representation of non-practitioner stakeholders on the PIOB.

We believe that public accountability and transparency are essential to ensuring that the standard-setting process properly adheres to the Monitoring Group's public interest framework. In addition, we believe that such accountability and transparency are most likely to be achieved if the PIOB has the authority to veto the adoption of a standard or challenge technical judgments. Without such authority, it may be difficult for the PIOB to discharge its responsibility of ensuring that international standards are set in the public interest because other participants in the standard-setting process could choose to ignore the PIOB's concerns.

World Council agrees with the proposed role and responsibilities of the PIOB as set out in this consultation, including giving the PIOB authority to veto standards or challenge technical judgments, and also urges the Monitoring Group to increase the representation of non-practitioner stakeholders on the PIOB.

Question 17: *Do you have suggestions regarding the composition of the PIOB to ensure that it is representative of non-practitioner stakeholders, and what skills and attributes should members of the PIOB be required to have?*

World Council supports including non-practitioner stakeholders with community-banking and cooperative depository institution experience on the PIOB. In addition to representatives from cooperative depository institution trade associations, World Council believes that current or former prudential supervisors of community-based

[6] International Financial Reporting Interpretations Committee, IFRIC Interpretation 2: *Members' Shares in Co-operative Enterprises and Similar Instruments* (updated Feb. 2008).

cooperative depository institutions would provide valuable perspectives concerning community-based depository-institution safety and soundness regulation. In many cases, the rulebooks applicable to community-based cooperative depository institutions and community banks are inextricably intertwined with accounting and auditing standards.

Including cooperative depository institution trade association representatives as well as current or former community-based cooperative depository institution prudential regulators on the PIOB would also help maintain a proportional and relevant standard setting approach that serves the public interest without creating unintended consequences or imposing unnecessary regulatory burdens.

Question 20: *Do you agree that the Monitoring Group should retain its current oversight role for the whole standard-setting and oversight process including monitoring the implementation and effectiveness of reforms, appointing PIOB members and monitoring its work, promoting high-quality standards and supporting public accountability?*

Yes, World Council agrees that the Monitoring Group should retain its current oversight role. We believe that the Monitoring Group continuing to perform its current oversight role is fully consistent with the principles that the Group has articulated in this consultation regarding developing standards in the public interest with independence, credibility, cost effectiveness, relevance, transparency, and accountability.

Accountability, in particular, can be ensured only through external monitoring and evaluation, such as the external monitoring and evaluation of the whole standard-setting and oversight process currently performed by the Monitoring Group. World Council agrees that the Monitoring Group should retain its current oversight role.

World Council appreciates the opportunity to comment on the Monitoring Group's Consultation: *Strengthening the Governance and Oversight of the International Audit-Related Standard-Setting Boards in the Public Interest*. If you have questions about our comments, please feel free to contact me at medwards@woccu.org or +1- 202-508-6755.

Sincerely,

Michael S. Edwards
VP and General Counsel
World Council of Credit Unions