Technical Note: Stabilisation

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Introduction

Definition

The word 'stabilisation', in the context of financial institutions, covers a number of concepts and actions that aim to protect vulnerable but viable financial institutions from liquidation, transformation or collapse. It also refers to the general intention to maintain public confidence in the financial system. In the context of financial cooperatives it typically refers to a central fund built up from fees and / or contributions collected by their apex body. One example is The Irish League of Credit Unions which developed its own form of 'stabilisation scheme' in the 1980s to 'protect the saving of credit union members' and 'to increase public confidence in the Movement'. Similar initiatives were launched in Jamaica, the USA, and Canada, as well as many other national movements. Even in the newer movements such as that of Uzbekistan the concept has been adopted. The spur for such a move, and the structure used, may differ from jurisdiction to jurisdiction. However, the motivation is the same, the need to protect the movement's reputation, by protecting viable but distressed financial cooperatives and their members.

Ideally every apex body, recognising that public confidence can be enhanced by creating a stabilisation scheme, should do so. This remains so even where there are independent regulatory controls and guarantee schemes instigated at the behest of the state or other international bodies.

Stabilisation support is more than just financial support; it should also encompass technical support to implement an agreed set of actions to address the problem that caused the financial distress. A stabilisation scheme needs to have a fund which is large enough to enable the apex organisation to offer support to a proportion of member cooperatives (as crises can affect several at the same time). It should be noted that a relatively small fund (in comparison to the overall assets of the movement) can sustain several financial cooperatives, for example in situations where the fund is directed at propping up the institutional capital ratio by a small amount.

Its meaning can vary from country to country and from institution to institution based upon the objectives of the defining body or of the environment in which it operates. For the purposes of financial cooperatives, stabilisation schemes and practices encompass:

- Building a fund to provide the resources to assist and restore viable financial cooperatives that are threatened with liquidation, transformation or collapse. (This threat can arise from either internal or external sources or failures).
- An agreement by the scheme's members to abide by an underlying set of prudential norms that apply to all its subscribing financial cooperatives.
- The apex body must provide (or avail of) active monitoring to ensure that the members are adhering to good financial and governance practices on an ongoing basis.
- The cooperatives themselves and the apex monitoring systems, should identify as early as possible when a cooperative is in distress and commence assistance.
- Lastly, expert assistance should be put in place to provide advice and, where necessary, help to rebuild financial cooperatives in distress.

Manifestations of financial distress in credit unions can include substantial accumulated losses, extreme cash shortages, devaluation of assets (e.g. loans). Liquidity shortages and negative growth are also potential signs of distress, both can happen when there is a run on savings.

One of the key ratios for defining the financial health of a financial cooperative is the Capital Reserve Ratio. Most forms of financial distress will have a negative effect on this ratio. Typically it is recommended that this be around 10% of assets although the national standard may be less in certain circumstances. [1]

The financial cooperative can also be weak in governance and management terms which can result in serious financial distress. In such circumstances a stabilisation scheme should focus intensely on improving governance and management as well as financial viability.

Stabilisation support should only be given to cooperatives which have the potential to address their difficulties in a reasonable period of time if they are provided with some support. The support should be defined and should be time bound. If the situation of the financial cooperative is beyond redress then other actions such as liquidation or a merger should apply.

This note will discuss the principles of stabilisation, the methods of intervention and the funding mechanisms that the apex organisation can use to offer stabilisation services. Note, the approach set out below is one of a myriad of approaches, and while many of the principles apply broadly, the mechanics of a stabilisation scheme vary from context to context. Examples of different approaches are set out in Annex 1.

Relevance

Stabilisation is one of the most essential services the apex organisation can offer its member cooperatives. It complements and reinforces the monitoring function of the apex organisation. It also strengthens the ability of the apex organisation to advocate for the cooperatives since the apex can vouch for their financial stability more strongly when backed by a well-funded stabilisation scheme and a robust monitoring system.

Stabilisation should not be confused with Deposit Guarantee Schemes (DGS). DGS is a commitment of the state (or sometimes the apex body) to reimburse savers if their financial institution fails. State schemes generally apply to banks and Non-Banking Financial Institutions and have a limit on the total amount covered for each saver[2]. Financial cooperatives may be directly levied by government to fund this DGS. The sole purpose of the DGS is to reimburse depositors in the event of the failure of the institution. The DGS has no mechanism to aid the financial institution to improve its financial situation in advance of liquidation. DGS is activated when the institution is being liquidated, whereas stabilisation is activated at an earlier stage, with the aim of preventing liquidation and resolving problems.

While a number of parties, such as a central bank, may have an interest in the integrity of its overall financial system (including financial cooperatives), it is the movement itself that has the most vital interest of all. Consequently it is important that it operates a stabilisation scheme which is tailored to its own specific requirements. This will enable the movement to act in its member's interests even when the state's agenda and that of the apex are not in harmony.

Establishing and Running a Stabilisation Scheme

Financial cooperatives, in common with all other financial providers, face a range of threats. Some arise from internal factors, common reasons being loan impairment and failure in the area of good governance. External factors can present threats to a financial cooperative's welfare as real pressures

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[1] In some cases the ratio may be capital against loans, or a system of risk weighted assets may be used.
[2] Under European Union (Deposit Guarantee Schemes) Regulations 2015 (S.I. No. 516 of 2015), all deposit taking institutions within the EU must be covered by a state DGS

can be caused by an economic recession or natural disaster. For example, where members are affected by redundancies their ability to repay their loans may be impaired, or a collapse in the value of investments in the context of a more general economic decline. Either can seriously affect the balance sheet.

Another example of externally induced pressures is where credit is easily obtained from other sources at better terms and conditions. In such instances the loan books may shrink affecting the income available to pay for outgoings.

The stabilisation scheme should only be one part of the apex's suite of tools, albeit a vital one, for assisting member cooperatives. The scheme's operational management should be separate from that of the apex and operating solely in pursuit of its declared aims and objectives, although under the apex's overarching ownership. The following are key principles of a stabilisation scheme:

1. Stabilisation can provide technical and financial assistance to financial cooperatives in difficulty.
2. Stabilisation depends on a strategic and monitored "work-out" plan of action to re-stabilise the cooperatives to be a viable operation or to become fit for merger.
3. Stabilisation is time limited.
4. The stabilisation assets must be held separately from the apex's own funds.
5. Stabilisation depends on enforceable financial and operational standards.
6. Stabilisation demands robust monitoring, supervision and examination of cooperatives by the regulatory or administrative authority.
7. Stabilisation requires the power to intervene when cooperatives fail to meet required financial and operational performance targets and to take measures (e.g. informing the regulator) when not playing by the rules. Some schemes may implement a policy of charging non-compliant members a higher rate of contribution. This can be controversial, on the one hand, it can be a useful deterrent against under performance and non-compliance but on the other hand it is charging ailing CU a higher cost just when they are already suffering some form of distress (perhaps due to external factors).
8. Stabilisation is complementary to deposit insurance.

The scheme should have the capacity to provide business advice and assistance when required by member cooperatives. Underpinning the management of a stabilisation scheme is its linkage with a monitoring and regulatory system, with the power to impose sanctions where necessary and as a last resort. The power to intervene and consult the members of the affected cooperative when it fails to meet its required financial or governance standards should be embedded in the scheme's rules.

Stabilisation should be regarded as a multifaceted process which develops good standards, monitors their observance and provides the resources necessary to re-establish distressed cooperatives by the most appropriate method where feasible. It should act in harmony with any insurance/guarantee funds set up for savings protection whether by the state or other medium. The basis for such collaboration should be agreed from the outset.

There are many issues that must be addressed upon deciding to create a scheme. Among these are:

1. The appropriate legal structure to be used to host the scheme. This will be determined by the legal requirements of the relevant jurisdiction as well as the aims of the apex.
2. The management and governance structures of the scheme should be decided upon by the founding group and be amenable to later agreed change.
3. The manner of creating the funds to be accumulated and the arms-length hosting and control of the scheme's fund itself.

4. Establishing the rules and methodologies for evaluating membership applications
5. Establishing the rules and methodologies for disbursing financial aid when requested.
6. The facilitation of arrangements, where needed, for the management and monitoring of disbursed monies.
7. The policy relating to members who retire from the scheme. It is best that those rights should be established at the set up date (e.g. they typically are not entitled to be reimbursed the funds they have paid into the scheme).
8. The rights and duties of members upon dismissal from the scheme. These should be determined at the outset.
9. Specific provisions for the winding up of the schemes fund itself should that eventuality arise. The disposition of residual funds upon the scheme's liquidation should be planned for at the outset to avoid any potential conflict.
10. The resources needed to monitor and advise member financial cooperatives should be in place and the monitoring unit's relationship with the scheme and its fund should be clear. This for example, may be paid for by the apex (which is paid for by the financial cooperatives).
11. The nature and limits of sanctions that can be imposed on non-cooperating members.
12. The internal availability of, or the process for, hiring external qualified personnel, to evaluate the viability of a rescue plan for distressed financial cooperatives should be addressed.
13. How to highlight to the public the member financial cooperatives' commitment to high standards and their creation of the extra layer of protection that they have adopted by belonging to the stabilisation scheme.
14. The relationship if any with a state led scheme where one is in place. The apex operation should, of course, endeavour to work in harmony with the state body as far as possible.

It is necessary to work out in advance the mechanisms to get the maximum amount of the stabilisation money back from the financial cooperative when it restores stability. It is important to set up a proper structure for recouping the funds. Mechanisms include moral obligation on the cooperative to repay, having the financial cooperative transfer written off loans for ownership by the stabilisation scheme (with an incentive built in for the financial cooperative to aid in recouping written off loans),[3] developing incentives for the financial cooperative to pay back sooner rather than later and using future equity in the financial cooperative building as a cross guarantee mechanism. Any contractual arrangements need to be set out in a legally binding manner.

Conditions and Structure of Stabilisation Scheme

Conditions attached to membership will be decided by the apex as sanctioned by its members. Ideally, members should agree to participate fully in all aspects of the scheme. These should include:

- That the applicant financial cooperative is a member of the managing apex and in general good standing with it at all times.
- That it is solvent and has no embedded financial or governance problems at the time of joining the scheme.
- That it is willing to be subject to a monitoring regime as defined by the scheme.

[3] In situations of loan impairment a stabilisation fund can assist the cooperative by providing formal guarantees on non-performing loans. To do this, a list of loans as collateral for the guarantee amount is drawn up in conjunction with the co-operative. In general these loans are fully provided for but not yet written-off. If and when these loans are written-off, the stabilisation fund pays the amount of the loan to the cooperative. The guaranteed section of the portfolio is proactively managed under the supervision of the apex organisation. The guarantee is time-limited. This guarantee allows the cooperative to comply with statutory requirements. The cooperative works to recover the loans listed; when sums are recovered then the guarantee for those sums is not needed anymore.

- That it contributes to the scheme's fund in accordance with the standard rate in place at all times.
- That any initial and ongoing payments made become the permanent property of the scheme's fund without any right of recourse save as provided in the rules of the scheme/fund itself.
- That it agrees to subscribe to all the rules or regulations of the scheme while in membership.

Establishing a meaningful stabilisation scheme involves the creation of a holistic structure involving:

1. **Setting performance standards** for member financial cooperatives which they should observe as a condition of membership. These can be based on the World Council of Credit Unions' devised PEARLS ratios, the CAMEL ratios or lending quality standards for example. Note, the numerical measurements and ratios tell you about what has already happened and while they indicate and possibly infer trends, they tend to catch the problem after it has materialised. The performance standards will be at least as rigorous as the state regulation in place and may often be stricter.
2. **A monitoring system** to continuously evaluate the members' achievement in maintaining the agreed financial standards. This system should, ideally, comprise of both a desk audit system based on regular returns from the membership and a periodic 'field inspection operation' and evaluation of trends. Breach reporting, whereby cooperatives are obliged to inform the scheme when breaches occur, is also highly recommended.
3. **A team of suitably experienced experts to carry out the field operation** by means of regular visits to the financial cooperatives to test their management performance and controls. . In the past onsite visits were necessary but nowadays, experts can also conduct much of this assessment remotely if they access management systems and records online. Internal audit can also play a vital role. This team should also be capable of responding to signals of weakness in a cooperative's performance. It should also be capable of advising the boards of the financial cooperatives on managing any weaknesses that are discovered
4. **The creation of the scheme's fund which can** (i) provide the personnel to assess serious issues threatening a financial cooperative, and (ii) provide the necessary financial resources to revive it where it is judged to be capable of sustained recovery and where the cooperative itself commits to adjusting to meet its challenges.
5. **A clear sound management structure for the scheme's fund itself** with clear aims and a mandate to act where necessary in the movement's interest. Fund finances must be separate from all other funds of the apex, legally ring-fenced, properly housed and applied solely for the purpose of assisting viable member financial cooperatives that are in distress.
6. **Its mandate should** include the power to impose agreed standards, and where necessary to impose penalties, to monitor members' performance and to intervene where deemed necessary.

Relationship to the Monitoring Department

The apex organisation's Monitoring Department should be an inherent part of the overall stabilisation framework. Its function is to develop a detailed and complex programme to oversee the performance of the member financial cooperatives. Major elements of the monitoring system[4] involve field review and advisory services, a desk audit function and data collection and analysis (e.g. PEARLS). The Monitoring Department needs to work intensively with distressed financial cooperatives on due diligence so that stabilisation support can work constructively and effectively. This involves:

1. Reviewing both audited and management accounts
2. Analysing recent reviews carried out at the financial cooperative

[4] See Technical Note on Monitoring

3. Analysing forecasts and projections to assess viability
4. Reviewing the strategic plan
5. Reviewing all correspondence and/or meetings with the Regulator where relevant
6. Reviewing discussions with other financial cooperatives regarding possible merger (to be promoted as appropriate).

The stabilisation scheme can then provide financial support under clear rules and conditions. The following table shows the trajectory of a guarantee against set off against impaired loans from the loan book.

Timeframe	**Cooperative A**	**Amount of guarantee in situ for the affected fin. cooperative**	**Funds transfer from Apex to Cooperative**	**Outstanding from the cooperative due to the apex (moral obligation to repay)**
January 2014	Impaired loans of €1 million are approved for a guarantee of 2 years' time limit	€1 million		
December 2014	The cooperatives collect €0.1 million of the impaired loans, this amount is deducted from the guarantee	€0.9 million		
February 2015	The cooperative writes off €0.3 million of impaired loans drawing down this amount from the guarantee fund	€0.6 million	€0.3 million	€0.3 million
December 2015	The cooperative collect €0.2 million of the impaired loans, this amount is deducted from the guarantee	€0.4 million		€0.3 million
December 2015	The time limit of the guarantee expires and the guarantee terminates **OR**	€0		€0.3 million
Up to December 2016	***The apex organisation and cooperative agree a new guarantee and new time frame***	***€0.4 million rolled over to December 2016***		€0.3 million

Figure 1 Example of Stabilisation Scheme Guarantee

As can be seen, the guarantee is credited to the affected financial cooperative, effectively the money is on 'stand-by' for the credit union, in a ring-fenced account designated for the affected financial cooperative, not necessarily drawn down by the financial cooperative, but utilised primarily for the purpose of temporarily augmenting the institutional capital on the balance sheet (it can be put in a special bank account set up in the name of the distressed financial cooperative with procedures and conditions attached to drawdowns). In the above example, the financial cooperative does draw down €0.3 million from the guarantee fund for loan write-offs in February 2015. This is then deducted from the guarantee amount. Additionally, the financial cooperative manages to collect €0.3 million of the loans in two periods; in December 2014 (€0.1 million) and December 2015 (€0.2 million). The total amount written off by the financial cooperative is €0.3 million and the total amount collected is €0.3 million. At this point the amount needed in the form of a guarantee is €0.4 million, and the physical money owed (morally though not legally) to the apex is €0.3 million. Depending on the circumstances of the financial cooperative, the guarantee may need to be extended for an additional period or it could be terminated.

The advantage of the guarantee method over direct transfer of funds to a cooperative is that often the apex stabilisation scheme's fund does not have to pay over all of the amounts initially agreed, as the cooperative collects some of the non-performing loans. If all funds are paid over at the beginning it is more difficult to find a mechanism for the cooperative to repay funds to the scheme later.

Another approach is that the apex organisation takes over the bad loans of a cooperative directly, but this method of support has not been as successful. It is generally better for the financial cooperative itself to retain the responsibility for following up on defaulted loans (even if they are technically owned by the apex), and some financial incentive is put in place for them to pursue these loans.

When a Guarantee is Not Enough

When financial cooperatives have suffered major losses on their assets and premises valuations, or suffered major losses on investments, the stabilisation scheme's fund assists mainly with direct funding to restore a compliant balance sheet position. The apex organisation and the financial cooperative make an agreement whereby if it sells the asset, the cooperative will return surplus funds to the apex organisation. This is different from the above example in that a guarantee mechanism is not sufficient and actual money needs be transferred from the stabilisation fund directly to the affected financial cooperative for their use.

Normally, all stabilisation financial supports to a cooperative are undertaken in consultation with the Regulator in advance.

Conservatorship[5]

Conservatorship is a virtual take-over of the cooperative in the interests of the membership, in which the apex organisation replaces the board with an administrative board; and the manager and staff can also be replaced if required and if judged as not sufficiently competent to stabilise the cooperative. Once in conservatorship, the cooperative must establish a net worth restoration plan with operational and financial goals, as well as performance benchmarks with target dates. Cooperatives in conservatorship are only returned to the members after apex approval and after a further examination, carried out within 12 months of take-over. Financial cooperatives that cannot be re-established as viable by themselves after conservatorship are merged with another financial cooperative or liquidated.

Mergers

Many distressed cooperatives overcome their challenges, restore stability and continue to operate autonomously. However, for some the best option, or indeed the only option available to them to continue to ensure a service to their members, is to merge with another cooperative. Typically distressed cooperatives merge with neighbouring cooperatives which are not distressed. The government and the regulator may have a policy or an unofficial approach whereby they encourage cooperatives very strongly to merge. In this case, even compliant and well performing cooperatives can meet with encouragement or even pressure to merge to meet the future challenges and especially to provide expanded services to members. For the regulator mergers also bring efficiencies and lower the cost of regulating and supervising the sector.

[5] This is used in the USA, where the National Credit Unions Administration (NCUA) is usually appointed as the conservator by the regulatory authority. For an example of a public notice of a conservatorship see: http://www.melrosecu.org/assets/1/7/melrose_NCUA_Press_Release_-_Feberuay_10,_2017__Melrose_conservatorship.pdf

Apex Stabilisation Scheme Relationship with Regulatory Authorities

The relationship between the regulator and the stabilisation scheme is important. Financially distressed cooperatives are often in breach of key regulatory ratios such as the capital reserve minimum (usually around 10%) and the liquidity requirement (typically around 20%). In such situations all parties, including the regulator, are keen to see that the cooperative address underlying issues, return to good performance and attain stipulated standards as soon as possible.

The regulator may take a mild or 'hands off' approach to the stabilisation scheme. In that case it allows the scheme to implement its financial and technical support plan with minimal action from its side, but it would expect to be kept fully informed on progress and expects the support plan to achieve its objectives within the agreed timelines.

It may take a more active, 'hands on' approach, in which it allows the scheme to support the cooperative, but also takes direct actions itself with the aim of correcting the situation. Possible measures include:

- *Lending restrictions, e.g. no loans over a certain limit. These restrictions apply to all members, so even excellent borrowers are adversely affected.*
- *Limit on the payment of dividends or interest on savings, even if there is a surplus available.*
- *Increased liquidity requirements, which affects the capacity of the financial cooperative to earn income on its funds.*
- *Restrictions on the holding of General Meetings. Meetings can be deferred until the regulator is satisfied with the accounts produced by the cooperative and that the Board can present a sustainable business plan to the membership.*
- *Withholding of approval for a merger.*

The intended aim of such measures is to help the cooperative address its problems and prevent it from repeating actions that contributed to its distress. Sometimes, however, the measures can inhibit normal trading and business development. This can confuse and upset the membership and cause uncertainty in an already delicate situation. Often distressed cooperatives express frustration that they cannot trade their way out of their difficulties due to restrictions and thus the restrictions are counterproductive (e.g. a lending restriction is imposed but the conditions under which it will be lifted are not made clear).

It is paramount that the apex stabilisation scheme and the regulator be in harmony if both are directly engaging with a distressed cooperative. The apex organisation usually prefers that it alone engages directly with its member cooperative, develops feasible support plans that the regulator endorses and subsequently reports on progress to the regulator. Nevertheless there are occasions where the direct engagement of the regulator is welcomed, in particular when the apex organisation finds that the cooperative is resistant to reform, despite being supported by the stabilisation scheme.

Funding a Stabilisation Scheme

A stabilisation scheme needs a fund with which to support distressed cooperatives. The apex organisation should start to build this fund as early as possible. It can be built by:

- Annual contributions of member cooperatives
- Apportioning some of the apex organisation surplus to the fund

- Grants from external partners and / or a long term soft loan (these may be particularly relevant in disaster affected environments).

As with all collective funds there are a number of core considerations that should apply to its management. The following are some of the issues that will loom large at the establishment stage.

Firstly, the monies should not be made available for deployment until it is large enough to cope with the occurrence of a significant number of simultaneous calls on its resources. This will require a decision at what level the fund becomes active (for example, when it reaches a target of 0.4% of assets of financial cooperatives that are paying into it). All matters relating to this issue should be debated and decided at the outset.

Secondly, the basis for building up the fund, including the manner of levying the financial cooperatives involved, should be decided upon. This should include a formula for calculating the contributions which is related to the growth in the amounts at risk year on year.[6] It is very important that a limit of contributions is set, otherwise larger financial cooperatives will be reluctant to join the scheme. Any interest or income generated on the funds in the scheme should be re-invested in the scheme's fund. When the fund is large enough, it may be that contributions can be reduced.

Thirdly, while recognising the need for liquidity the scheme's fund should, as far as possible, endeavour to earn a return on its assets in order to forestall its premature depletion in real value.

Fourthly, its mandate should keep the conservation of its assets at its core. This will demand cautious investment strategies using such instruments as blue chip shares and state bonds. A careful spread of assets in a diverse number of investments is advisable. The idea of placing the entire fund into one financial instrument is not advisable from a risk point of view. Ideally experienced advisors should be given a clear mandate to invest the money on management's behalf. Clear instructions on the purpose and goals of the scheme's fund should be given to the appointed fund managers.

Fifthly, the selection method and characteristics of the scheme's fund's own directors or trustees should be the subject of careful discussion and decision before the structure is finalised. It is important that they should be capable of managing the experts chosen to invest the portfolio and of clearly describing the purpose and aims of the scheme's fund to them.

Sixthly, a good management and collection system should be in place.

Finally, the trustees or directors of the scheme's fund should ideally be a mixture of member financial cooperative volunteers and apex nominees. The ideal structure and governance requirements will evolve with the growth and development of the fund.

In good times, when there is little demand from cooperatives for stabilisation, and when there is high demand for investment in technology and business development, it is tempting to use this fund for other purposes, but this should be prohibited by the statute of the apex organisation. In some cases the Stabilisation Scheme may be structured as a subsidiary company of the apex organisation.

For a stabilisation scheme's fund to be considered fit for purpose it is recommended to have between 1% and 5% of total savings of the subscribing financial cooperatives. This means annual contributions

[6] In Ireland, financial cooperatives make a contribution of 40 cents per €1,000 of their total assets (i.e. if a financial cooperative has €1,000,000 in assets, it will cost them €4,000 in annual contributions to the stabilisation scheme). The amount of the payment in Ireland is capped for larger financial cooperatives.

to the fund are set as a percentage of the savings, or the assets of a cooperative. In times of low growth the stabilisation fund can grow rapidly relative to total assets. However, the opposite also applies as

		Total Assets of member cooperatives, thousand					Cumulative Stabilisation Fund, thousand			Stabilisation Fund to Total Assets ratio, %		
		2015	2025	2035			2015	2025	2035	2015	2025	2035
Annual growth rate, % (compound)	1%	1,000	1,105	1,220	Annual contribution, % of Total Assets	0.2%	2	23	46	0.2%	2.1%	3.8%
	5%	1,000	1,629	2,653			2	28	71	0.2%	1.7%	2.7%
	10%	1,000	2,594	6,727			2	37	128	0.2%	1.4%	1.9%

Figure 2 Size of Stabilisation Fund under Different Growth Scenarios

With low asset (compound) growth of just 1% annually for 20 years, an annual contribution of 0.2% of assets builds a fund of 3.8% of total assets of the cooperatives. However, with asset growth of 5% and 10% the growth of the fund falls to 2.7% and 1.9% of the total assets respectively.

The apex organisation needs to review the levels of the scheme's fund on a regular basis and adjust the funding contribution rates to maintain the fund it at the optimum level as a proportion of assets of the cooperatives. The level of the scheme's fund is of course affected by the use of the fund to support cooperatives. When demand for the stabilisation funds is high, then contributions may have to be increased to ensure its continuation.

The Stabilisation Scheme should consider the size of individual cooperatives. If some cooperatives are huge (e.g. over 10% of the assets of the entire movement) then it *may* be unrealistic to think that the Stabilisation scheme, which has a fund much less than the size of the cooperative, can support it if it is in extreme distress. It is vital that a cooperative diagnose any problems early and seek support while it is still within the means of the scheme to help.

How Important Is It that An Apex Should Create and Maintain Its Own Stabilisation Scheme and Fund?

Two main scenarios must be considered here. The first relates to the situation where no state led scheme exists. In this case it is extremely important that the apex initiates the process as soon as it can. In these circumstances a stabilisation scheme provides the collective equivalent of permanent equity in a bank or microfinance company. Such a provision is a vital component in underwriting the safety and soundness of financial cooperatives. Its' need is ignored at the movement's peril.

Secondly, a trend is developing where national banking and regulatory authorities are taking a growing and more intrusive role in financial cooperative management and control. There is an increasing number of state led stabilisation schemes (the financial cooperatives pay into their central bank who establish and administer this scheme). This is leading to increases in the regulatory costs and other burdens for the cooperatives. The regulators can place limits on the amounts that may be lent, when they deem it appropriate. They have defined the profiles of the people that may be deemed appropriate ('fit and proper') to be members of boards. In Ireland they have even announced restrictions on the maximum amounts that can be saved by individual members. These demands are leading to pressures to create larger units at the cost of direct community identity. This is also resulting in a dilution of the closeness of the 'common bond' concept.

New Zealand is an example of this phenomenon. In 1985 it had 312 financial cooperatives. By 2010 these had been reduced to less than thirty. Its membership in terms of people is quite low totalling just over 200,000 people out of a population of just under five million. In Canada this approach has been developed as well. The process may be justified in some regards, particularly in the light of modern market expectations and developing technological change. However, it poses a serious threat to some of the cooperative's primary principles. For instance the all-important principle of democratic control becomes less meaningful as does member ownership. The strong common bond or community is diluted dramatically. The further the membership is distanced from the running of the cooperative the more one of its unique strengths is weakened.

This is one reason why national movements must preserve and promote their stabilisation scheme and fund. The formation of such funds is the epitome of the cooperative principle of 'cooperation among cooperatives'. From a practical point of view, it also endows the movement with the power to protect its own financial cooperatives where relevant.

In addition, as the evolution from small to large financial cooperatives is probably inevitable, it is important that the apex bodies, rather than abandoning the concept, should strive to ensure that their schemes' funds grow at a similar pace to maintain their effectiveness in the changing environment.

Conclusions

Stabilisation is crucial for a distressed cooperative in steering its path to recovery, either on its own or through restructuring by merger. While assisted by professional management the responsibility for the safety and soundness of the financial cooperative is with the Board. A stabilisation scheme plays a critical role in:

- Directly assisting personnel and most importantly the Board of the financial cooperative,
- Networking the cooperative with other cooperatives if merger is an option,
- Supporting the cooperative in its interaction with the regulator,
- Maintaining public confidence in the cooperative and in the national movement.

Collaboration among financial cooperatives is essential and access to stabilisation is one of the most important benefits of membership of an apex organisation. Accordingly, it comes at a cost in terms of annual dues. A stabilisation scheme offers a safety net for financial cooperatives and is a crucial element in maintaining public confidence in the movement.

Annex 1. Selected Examples of National Credit Union Stabilisation Schemes

The approaches to financial cooperative / credit union stabilisation schemes vary from jurisdiction to jurisdiction. Most schemes were created to meet the identified needs of the financial cooperatives in their own countries. Supplementary to a stabilisation scheme, many state authorities saw fit to control the movement from a regulatory point of view. The levels of intervention by the regulatory authority differ and the approaches also differ even in terminology. Some of the schemes given the title of 'stabilisation' are in fact limited deposit guarantee funds to be invoked in cases where a financial cooperative is being closed down. Others are a combination of financial cooperative preservation initiatives and deposit guarantees.

Central banks are becoming increasingly involved in regulating financial cooperatives and in forming deposit guarantee schemes. These procedures and protections are often funded by the financial cooperatives themselves as the central bank levies charges to cover related costs.

Regardless of the measures put in place by a government and central bank, it is important that the special ethos of the movement is protected and the societies do not lose their unique offering to their community well-being. The Bank of Jamaica appears to have approached the issue on this basis and the outcomes of its deliberations with the league over the past years could, if realised, provide some pointers for future initiatives.

A sample of recent developments is given in the examples that follow (note the terms 'financial cooperative' and 'credit union' are used inter-changeably).

1. THE NATIONAL CONFEDFERATION OF COOPERATIVES (NATCO) IN THE PHILIPPINES

NATCO describes its stabilisation scheme as 'a form of solidarity fund as cooperatives contributing to it, in effect, are coming together to help one another.' It was established because 'the integrity of the cooperative is important and thus it must be guarded against any unfortunate incident. The failure of one cooperative can lead to a major loss of confidence in the entire sector.'

Further information can be accessed on its website at http://www.natcco.coop/index.php/product-services/financial-services/stabilization-fund (cut and paste link into browser).

2. THE LITHUANIAN CENTRAL CREDIT UNION

According to the supervision service of the Bank of Lithuania in 2016 the liquidity support reserve of the Lithuanian Central Credit Union amounted to €5 million year on year. The central had united 61 credit unions at that date. The stabilisation fund only stood at just below €1 million at the same time.

See http://www.lb.lt/ for further references.

3. NATIONAL CREDIT UNION ADMINISTRATION (U.S.A.)

The NCUA is an independent federal agency set up by the U.S. congress to regulate, charter and supervise federal credit unions.

It manages a national share insurance fund which insures the deposits of more than a hundred million account holders in federal credit unions in the United State of America as well as in most state chartered credit unions. This is through the medium of the National Credit Union Share Insurance fund (NCUSIF) which is capitalised by credit unions themselves. The fund covered savings/shares up to a maximum of $250,000. The fund has had a chequered record as the financial crises created pressure on credit unions as well as other financial institutions including banks.

In January 2009 it created what it called the 'Temporary National Credit Union Stabilisation Fund' to free the NCUSIF from its obligations, and recapitalised it. The 'stabilisation' fund could borrow from the Treasury for the sole purpose of dealing with the actual or threatened conservatorship or liquidation of a corporate credit union. This was in response to a crisis in the movement and it was funded by the insured credit unions.

This, in common with other insurance type funds, was mainly a reactive scheme.

4. TRINIDAD AND TOBAGO STABILISATION FUND

The Cooperative Credit Union League of Trinidad and Tobago 'was instrumental in the establishment of the Trinidad and Tobago Stabilisation Fund and the Central finance Facility'.[7]

The League operates a limited guarantee on member shares of up to $125,000 and deposits of up to $50,000. Its Deposit insurance Fund aims to provide credit unions with credit lines when they encounter short term liquidity problems. It monitors the financial performance of its members.

The central bank prepared proposals for own 'limited' protection fund for credit union shares and deposits in 2014 which involves credit union people in its management. It proposed the same coverage levels as those already in existence under the League's scheme. This too is a type of savings guarantee fund which will be paid for by the credit unions themselves.

Proposals underway in 2014 by the state were put forward to establish a state deposit guarantee fund (although the present system is more generous than the proposal for state deposit guarantee).

See www.ccultt.org for information sources.

5. JAMAICAN STABILISATION SCHEME

The Jamaican Co-operative Credit Union League has had its own stabilisation fund in operation since 1963. It stood at more than $2 billion in 2012. When a credit union gets into trouble the league 'tries to nurse them back to health and return them back to their members'[8] or apply another solution to enable its members to continue to receive the services that they were used to.

In common with current trends across the globe, the Bank of Jamaica, is about to introduce its own regulatory regime for the country's credit unions. The changes recognise the unique characteristics of credit unions and have been negotiated and debated with the league over many years.

6. THE BAHAMAS

In 2015, the Bahamas introduced legislation for the regulation of its credit unions (the 'Bahamas Co-operative Credit Union Act'). This included a number of interesting provisions including certain exemptions for small credit unions (those with assets of less than one million dollars).

[7] See The Cooperative Credit Union of Trinidad and Tobago webpage http://ccultt.org/site/our-league
[8] Rodgers, P. (2012) New Regulation Near for Credit Unions, Jamaica Observer. Available at: http://www.jamaicaobserver.com/business/New-regulation-near-for-credit-unions_10883346 [Accessed on 11/1/2017]

The creation of a stabilisation fund is specifically provided for in section 65 of the Act. This provides, inter alia, that 'Every co-operative credit union shall contribute annually to a stabilisation fund, in such amount as may be determined by the Apex body.'

The Act also provides that 'every co-operative credit union shall ensure that the proceeds of the statutory reserves, liquidity deposit and stabilisation funds are deposited with and administered by the Apex body in such a manner as may be prescribed by the regulations and the bye-laws.'

It also provides that where there is no apex that the Central Bank, which is the regulator, shall appoint such a person as they choose to fulfil the function 'after consultation with such co-operative credit unions.'

The importance of having such a fund is therefore clearly recognised in legislation. More interestingly, giving the power to manage the fund to the credit unions' apex is significant in the context of supporting self-help principles and worthy of ongoing observation.

7. CANADA'S ATLANTIC SEABOARD SCHEMES: NEWFOUNDLAND AND LABRADOR

The province of Newfoundland and Labrador in Canada operates a stabilisation scheme for credit unions. It has established a credit union deposit guarantee corporation which exists to compensate depositors of liquidated credit unions up to a predetermined limit.

More importantly the corporation, which has regulatory powers as well as the task of insuring member deposits, has duty to stabilise distressed credit unions where possible and to restore them to their members.

The fund is financed by the credit unions themselves. Its role is primarily preventative and it works to monitor and improve credit union performance.

This form of comprehensive stabilisation operation covers a number of Atlantic seaboard provinces in Canada such as New Brunswick, Nova Scotia etc. The corporations are empowered by their relevant legislatures to carry out the functions necessary to fulfil their comprehensive mandates.

See www.atlanticcreditunions.ca or www.cudgcnl.com and other web addresses under 'deposit insurance' on the main website for further information.

8. POLAND

Poland has separate stabilisation and guarantee schemes. The National Association of Cooperative Savings and Credit Unions (NASCU) in Poland operates its own stabilisation fund. This is funded by the credit unions themselves. 'It is used to support and stabilise the operation of credit unions in distress by means of loans and guarantees.'

The charter of NASCU dictates that the fund is to be used to stabilise the functioning of credit unions and of NASCU, in particular to subsidise recovery plans.

A separate guarantee fund is in place.

In 2013, alterations to the financial reporting standards used as well as auditing practices were ordered along with changes in other practices.