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The policies in this chapter are sufficient for most situations that may arise. The policies may not cover each and every situation and must be customized to meet each credit union's unique requirements.

The shaded text that appears in this chapter is customizable by your credit union. When customizing this chapter, use your software's Find/Replace function to insert your credit union's name wherever "the credit union" (or a variation of this phrase) appears.

Text in boxes, such as this one, is background information, and can be deleted when you customize this file.

Note: Material from By-Law No. 5 has been incorporated into this policy. Customizing it will provide your credit union with Central's policy recommendations. It is strongly suggested that credit union managers and boards consult the workbooks prepared by DICO for additional guidance that will help them comply with the By-Law.

The credit union believes that liquidity risk management is a necessary part of prudent financial administration, and is committed to engaging in proper liquidity risk management practices to comply with regulatory requirements and to guarantee the orderly funding of member needs and obligations. The credit union will ensure responsible liquidity risk management at all times to provide a cushion for unforseen liquidity needs.

Policy Objectives

To establish an overall framework of liquidity risk management which ensures that the credit union faces limited exposure to all material risks.

To implement a policy that addresses limits on the sources, quality and amount of liquid assets to meet normal operational, contingency funding for significant deposit withdrawals, and regulatory requirements.

Operational liquidity is defined as the liquidity required to meet anticipated day to day cash commitments including member withdrawals.

Responsibility

The Chief Financial Officer is responsible for managing liquidity risk in accordance with this policy and the annual business plan.

Policy Guidelines

a) The credit union will fully adhere to:

- all regulatory requirements prescribed in:
  - the Act [sections 84 to 89]
  - the Regulations [sections 16 to 21 of Regulation 76/95]
- DICO's standards of Sound Business and Financial Practices
- all other regulatory liquidity requirements

- the credit union's annual business plan, with respect to liquidity risk management.

b) The credit union will provide a framework for operating liquidity risk management under ordinary or reasonably expected business conditions.

c) The credit union will ensure funds are available to meet all cash outflow commitments as they fall due.

d) A minimum operating liquidity requirement will be established to maintain an adequate cushion beyond the minimum statutory requirement in order to meet cash needs, even during periods of market volatility.

e) A maximum operating liquidity target will be established, as retaining too much liquidity has a negative effect on earnings.

f) A target range for operating liquidity, stated as a percentage of deposits and borrowings, will be established.

g) The credit union will adhere to the principles of quality and diversity in its liquidity funding practices. Assets purchased with liquid funds will have a contractual maturity of less than one year, although term extension on a portion of the portfolio with a longer horizon is allowed. The average term of the overall liquidity portfolio will be geared to the needs of overall structural risk management requirements.

h) The credit union will endeavour to ensure that its deposit liabilities are not unduly concentrated with respect to:

- an individual person and connected persons
- the type of deposit instrument
- the term to maturity
- the market source of funds, if applicable
- currency of deposit, if applicable.

i) Large deposits from single depositors or connected persons will be invested in liquid securities when liquidity levels are low. These liquid securities will be in addition to other required operating liquidity.

j) Any deposits being held by an individual or their connected persons that will have a significant impact on required operational liquidity if withdrawn require 60 days' notice for withdrawal. Management will define "large deposits" for these purposes and advise the board.

k) The credit union's liquidity risk will be managed in a prudent manner and in full accordance with the requirements of this policy. If variances from policy arise, then management will put timely measures in place to correct the variance. Such actions will be reported to the board of directors.

l) Adequate measuring, monitoring and reporting on risk position and exposure management will be maintained. The credit union's liquidity needs will be reviewed weekly. This review shall encompass a detailed forecast of imminent liquidity requirements and a broad projection of cash needs for the next three-month period. Summary measurements of liquidity risk shall be prepared for board review at each board meeting.

m) The credit union may draw on its operating line of credit for short periods of time (under 100 days) to maintain liquidity at the minimum statutory level. The credit union need not borrow to meet its target liquidity cushion. Borrowings, however, whether revolving or term, are not to be used to meet lending requirements over the longer term (over 100 days) unless approved by the board of directors as part of a business plan. In the longer term, management will seek alternative strategies to alleviate liquidity problems and to meet the operating target for liquidity.

n) The responsible officer will invest the credit union's regulatory and operating liquidity with an objective of optimizing yields in securities providing a high level of security and liquidity. As an operating guide, the credit union shall seek to achieve an average return at least equivalent to the Credit Union Central of Ontario Discount Deposit yields. Management will devise methods and standards designed to meet the requirements of this paragraph.

o) The credit union will employ competent and qualified persons with appropriate experience to manage liquidity risk. Controls will be in place to ensure adequate segregation of responsibilities and duties to maintain adherence to liquidity risk management policies and procedures.

Liquidity Guidelines

a) Credit union management will establish a prudent target range for operational liquidity of between 12 and 18 per cent of deposits and borrowings. This target range meets the regulatory minimum for gross liquid assets to total 8 per cent of deposits and borrowings, in accordance with the Regulations [sections 16 to 21 of Regulation 76/95].

b) Assets which may be purchased as part of the liquidity portfolio are as follows:

- Deposits in a league
- Deposits in a Schedule I bank
- Treasury bills issued by Canadian governments
- Bonds and debentures unconditionally guaranteed by Canadian governments
- Canadian dollar deposits with, or acceptances issued by, Schedule I banks with a DBRS rating of R-1 low or better.

c) To limit extension risk, no more than 50 per cent of the operating liquidity portfolio may be invested for terms greater than 182 days, and no more than 25 per cent of the portfolio may be invested for more than one year. This limit is to apply at the time of purchase. Maturity of securities purchased or held is defined as the remaining term to maturity.

d) Prudent limits will be placed on unhedged liquid assets denominated in a foreign currency. The limits established below are in relation to the size of the overall liquidity portfolio and are to apply at the time of purchase:

Foreign Currency	Percentage of Liquidity Portfolio
United States dollar	5% of portfolio, maximum
Other currencies	No unhedged investment permitted

Annual Business Plan

Information dealing with liquidity and liquidity risk management will be included with the annual business plan that is presented to the board of directors for approval. This information will include:

- projected volume of operational liquidity
- seasonal liquidity increments
- liquidity borrowings
- average yield on liquid assets.

This information can be combined with the monthly projections developed for structural risk management planning.

The annual business plan will include an explanation of actions and strategies designed to meet budget expectations. It is management's responsibility to ensure that the details within the annual business plan are effectively communicated within the credit union.

The projections in the annual business plan will be on a monthly basis. Management will effectively communicate approved plans to all appropriate persons within the credit union.

When a material unfavourable variance from the annual business plan arises, it is incumbent on management to put in place timely and prudent corrective action designed to improve the problem, and to report this action to the board of directors.

Reporting

The Chief Financial Officer will report to the board, no less frequently than monthly, on the following:

- Compliance with this policy and regulatory requirements
- Regulatory, operational and excess liquidity, expressed in dollar volumes and as a percentage of deposits and borrowings, as well as variances to budget, and yields earned
- Concentration of large deposits of single and/or connected depositors and brokeraged deposits as a percentage of total deposits
- If there are borrowings for liquidity purposes, the level of such borrowings and the liquidity total less borrowings in relation to the statutory minimum.

Where regulatory liquidity is not maintained for five business days or more, the director and DICO must be notified immediately of the circumstances for non-compliance and of corrective steps taken, and the credit union must not make a loan or investment until it again complies with those sections, in accordance with the Regulations [section 20 of Regulation 76/95].

Where a credit union does not comply with the liquidity risk management requirement under the Regulations [section 21 of Regulation 76/95], it must, within 10 days, submit a plan to the director for the repayment of its borrowings to the extent necessary for the credit union to re-attain the required liquidity level, in accordance with the Regulations [subsection 21(4) of Regulation 76/95].

Liquidity Borrowings

The credit union's liquidity borrowings will not exceed 25 per cent, as stipulated in Section 183 of the Act.

Compliance

Annually, the Audit Committee will ensure compliance with this policy. The Audit Committee is responsible for developing and conducting an annual review of liquidity risk management procedures relative to the requirements established in this policy. The Audit Committee will report its findings and recommend any necessary corrective action to the board of directors. The Audit Committee may engage the services of additional volunteers or experts to assist in their review.

The external auditor will conduct whatever tests are necessary regarding this policy, in order to meet generally accepted auditing standards, and will report any shortfalls to the audit committee.

The board of directors (in conjunction with the audit committee, as mandated by the Regulations [paragraph 26.17 of Regulation 76/95]) will review written correspondence from the Ministry, DICO or a designated stabilization authority regarding liquidity risk management matters, and will investigate and respond as appropriate.

Policy Approval and Review

This policy, and any subsequent recommended changes to this policy, must be approved by the Board of Directors.

This policy shall be reviewed annually for ongoing appropriateness by the board (or by a delegated subcommittee of the board).