

## OFFICE OF THE REGISTRAR OF CREDIT UNION

### Practice Guidance Note. 4

#### On Credit Risk Management of Credit Unions

##### Applicability

1. The Practice Guidance Note 4 (hereinafter PGN4) is applicable to all credit unions which are registered and regulated by the Registrar of Credit Union under the Credit Union Act 1986 [Cap 165] (the Act hereafter), the CBSI Act 2012 (CBSI Act hereafter) and the Credit Union Standard By-Laws 1987 (by-laws hereafter).

##### Background

2. Credit Unions are customer/member owned financial cooperatives, based on the principles of common bond, volunteerism and member participation. Credit unions are democratically controlled by its members – both customer and shareholders, and whose primary purpose is to maximize the economic benefit of its members by providing savings, credit and other financial services or rewards at competitive and fair rates.<sup>1</sup>
3. The Registrar of Credit Unions is responsible for the registration and regulation of all credit unions operating in the Solomon Islands, pursuant to the Act, and the CBSI Act. The aforementioned Acts seek to promote stability within the credit union industry, thereby, maintaining confidence in the relationship between members, management and board of directors.
4. The Registrar's Office is mandated to ensure that sound credit risk management and prudent lending practices are observed by all registered credit unions while still fulfilling their obligations to protect the savings of and provide equitable loans to credit union members.
5. Regulatory examinations conducted by the Registrar's office reveal that most credit union continued operation under inadequate credit risk management. This may potentially lead to imprudent lending practices and unsound credit operating processes which can result in credit union's failure. Hence, an adequate Credit Risk Management is crucial for sustainability of credit union movement, and enhance accountability and to safeguard members' interests at all times.

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<sup>1</sup> World Council of Credit Unions [WOCCU] – “Technical Guide: Credit Union Regulation and Supervision”, 2008 & “Why Credit Unions”, 2023 [[https://www.woccu.org/about/credit\\_unions](https://www.woccu.org/about/credit_unions)].

6. The PGN4 emphasizes that all credit unions must implement internal credit risk management framework and ensure the adherence to sound lending conduct practices.
7. This PGN4 is not intended to be exhaustive, but provides the minimum standards that must be observed.
8. The Registrar expects credit unions to take appropriate steps to become compliant with this PGN4.

### **Purpose**

9. The minimum requirements in this PGN4 are based on the technical guide for credit union Regulation and Supervision principles and international best practices established by the World Council of Credit Unions (“WOCCU”), and Basel Committee, in conjunction with the Act, and the CBSI Act; to ensure that credit unions effectively establish and maintain sound credit risk management framework.
10. The PGN4 promotes effective management of credit risk as an important element of a comprehensive risk management framework that is foundational to the safety and soundness of a credit union and is crucial to its long-term viability.
11. The PGN4 purposely prescribes measures that credit unions must adopt to manage risks related to lending process and practices and ensure the adequacy of the management of credit risks.
12. The PGN4 is also aimed at promoting accountability and transparency in credit unions business operations and greater member confidence.

### **Definitions**

13. **“arm’s length”** means any transaction between a Credit Union and an officer or associated persons must be done independently without collusion or one party influencing/pressuring the other party; there must be act of fairness between a Credit Union and an officer or associated persons in business dealing.
14. **“associated/related parties”** means individuals who are closely connected to a director, committee member, officer of a Credit Union either directly by consanguinity or through marriage or similar forms of partnership like family members, or either socially or professionally as business partners, company, trust or other entity and has a controlling interest.

15. **“board of directors”** means the body elected by the members of Credit Union to manage the affairs of the Credit Union, as defined in section 2 of the Act.
16. **“by-laws”** means the standard by-laws and the registered supplementary by-laws, as defined in section 2 of the Act.
17. **“conflict of interest”** means a situation where an officer of the Credit Union stands to gainfully benefit from actions or decisions made in their official capacity.
18. **“credit committee”** means the committee elected by the members of Credit Union under the By-Laws to consider and approve loans, as defined in section 2 of the Act.
19. **“credit risk”** means the risk that a Credit Union as a lender may suffer a financial loss as a result of the potential that a borrower fails to meet his/her repayment obligations according to the terms and conditions of the agreement between the lender and borrower.
20. **“credit risk management”** means the process of controlling the impact of credit or loan risk related events on the Credit Union. This management involves identification, understanding, and quantification of the probability and degree of potential loss and the consequent taking of appropriate measures to minimize the risk of loss.
21. **“credit union”** means a co-operative, non-profit organisation registered under Section 8 of the Act having as its objectives the principles set out in Section 15 of the Act, as defined in section 2 of the Act.
22. **“doubtful loan”** means a loan which is impaired, the repayment of which is in doubt.
23. **“loan/credit”** means any advance of funds which are made to a borrower on agreed terms and conditions, basis on obligation to repay the amount borrowed together with interest thereon. Loans should be extended on a secured basis.
24. **“loans officer”** means a person appointed and empowered under the Act or the By-Laws to grant loans of amount not exceeding the amount prescribed by the Credit Union Regulations, in accordance with any directions given to him/her by the credit committee.
25. **“members”** means persons who join a registered credit union in accordance with its by-laws, as defined in section 2 of the Act.

26. **“officer”** means the chairman, secretary, manager, a member of the board of directors, the supervisory committee, the credit committee and includes any other person empowered under this Act or the by-laws to give directions relating to the business of a credit union, as defined in section 2 of the Act.
27. **“problem loan”** means loans which the ultimate collectability of principal and interest is compromised and there is no longer reasonable assurance that the Credit Union will collect all amounts due, according to the contractual terms of the agreement. These would include loans that are past due 90 days and above.
28. **“provision for loan losses”** means a balance sheet valuation account established through charges to provisions expense in the profit-and-loss statement and against which bad loans, or portions thereof, are written-off.
29. **“Registrar”** means the Registrar of Credit Unions appointed pursuant to Section 3 of the Act, as defined in section 2 of the Act.
30. **“risk mitigation”** means the process of reducing risk exposure and minimizing the effects of threats faced by a Credit Union, by developing preventive and reactive action plans to reducing the likelihood of credit risk or any adverse effects from risk.
31. **“security/collateral”** means any form of appropriate asset that is pledged by the borrower as a guarantee for a loan repayment, if the loan is not repaid, the Credit Union may sell or claim the asset to get its fund back.
32. **“supervisory committee”** means the respective committees elected by the member of credit unions, to provide independent review on the books of credit unions, as defined in section 2 of the Act.

### **Compliance**

33. Credit unions should consult with the Office of the Registrar if they believe they cannot meet this PGN4.

### **Credit Risk Policy/Lending Policy**

34. A credit union is required to establish and implement a written credit risk policy or a prudent lending policy that is appropriate to its size, business operations, risks and complexity. At a minimum, the credit risk policy must include:
  - a. Role, responsibility and level of accountability of the board, credit committee and loans officer in accordance to the Act and by-laws;

- b. Delegated commitment authority or delegated approval authority for credit committee and board;
  - c. Acceptable type of borrowers as prescribed in the Act and by-laws;
  - d. Types of loan and sector the credit union is allowed to fund and support;
  - e. Acceptable limits and repayment terms for each authorized type of loan;
  - f. Acceptable types of security;
  - g. Lending values for each type of security;
  - h. Loan evaluation and documentation;
  - i. Loan approval processes;
  - j. Loan approval limits;
  - k. Monitoring, evaluation and reporting of outstanding loans, including impaired loans;
  - l. Details on how problem loans should be managed and who is responsible for managing this function;
  - m. Clear definitions of loan rescheduling, refinancing, and consolidation which adhere to the Act and by-laws;
  - n. Write-offs/Provisions procedures;
  - o. Record keeping procedures;
  - p. Details on internal controls to mitigate credit risk; and
  - q. Independent review process.
35. A credit union must clearly detail its credit risk tolerance, including how much and what types of associated credit risk it is prepared to accept in compatible with the credit union's overall strategic objective.
36. It is also essential that a credit union's credit risk policy is effectively communicated within the credit union and that the relevant credit union officers are aware of the established approach to credit risk management.

### **Board of Directors Role in Credit Risk Management**

37. The board of director is ultimately responsible in overseeing the credit risk management function of a credit union. The responsibilities of the board shall include but are not limited to the following:
- a. To approve and adopt a sound documented credit risk policy that establishes strategic direction in guiding the lending activities of the credit union;
  - b. To review the credit risk policy periodically every two (2) years to ensure its adequacy and relevance given the changing operating circumstances, economic cycle, activities and risk that may face by credit unions;
  - c. To determine the maximum individual loans which may be made with or without security, in accordance to section 57 of the Act;

- d. To determine interest rates on loans and deposits, as prescribed under section 57 of the Act;
- e. To review the large or complex lending transactions which are outside delegated credit/lending approval of credit committee, management or loans officer;
- f. To ensure that adequate controls, credit committee and management reporting and independent review by supervisory committee are in place to monitor that the credit risks being accepted are in accordance to internal policies;
- g. To ensure compliance to the credit risk policy;
- h. To review lending trend analysis of the credit union to identify and understand emerging credit risks and make appropriate recommendations to mitigate potential risks.

#### **Credit Committees Roles/Responsibilities**

- 38. Each credit union's board of directors shall ensure a credit committee is formed with specific roles and responsibilities in accordance with Section 31, 44, 53, 58 and 59 of the Act and by-laws 21.
- 39. The credit Committee shall perform such roles and duties as are prescribed in the Act, Regulations and the by-laws. The duties of the credit committee shall include but are not limited to the following:
  - a. To perform general supervision of all loans to members and subject to the provisions of the Act;
  - b. To assess and make decisions on application of loans;
  - c. To determine the amount of, and the rate of interest on each loan from time to time;
  - d. To not consider any loan unless a majority of the committee is present and no loan shall be approved except by the unanimous decision of the members present;
  - e. May appoint a loan officer and delegate its functions to the officer;
  - f. To require security to be given on all loans in excess of an amount to be fixed by the Registrar;
  - g. To determine the security and guarantors required for each loan and the conditions of repayment;
  - h. To maintain books and records for the necessary and prudent recording of its lending functions; and
  - i. To ensure to comply with its statutory obligations.

### **Interest Rate**

40. The determination and setting of the interest rate shall be instituted in accordance to section 57, 58, 60 and 62 of the Act.
41. The process to determine the interest rate should be detailed in the credit risk policy document.

### **Credit Assessment**

42. Establishing well-defined credit assessment criteria is essential to approving credit in a safe and sound manner, supported by clear roles and responsibilities within a credit union. Credit assessment is when all credit application is collected to enable an assessment of the borrower's risk profile. At a minimum, the credit assessment criteria for a credit union should set out the followings:
  - a. Who is eligible for loan and for how much;
  - b. The maximum lending value for each type of loans;
  - c. What are the authorized types of loan products available;
  - d. What terms and conditions the loans should be granted.
43. Credit application forms should be sufficiently detailed to permit gathering of all information needed for the credit assessment to ensure that lending activities is done prudently and complies with the credit union's credit risk policy.
44. Each credit union should create a comprehensive pre-qualification criteria checklist to ensure all required information on the application form is collected and completed accurately.
45. A key element of credit processing and appraisal is assessing the borrower' ability to repay. It is important that a credit union assess whether it is likely that a member would be able to meet loan repayments without substantial hardship. A credit union should establish and implement credit appraisal criteria that would assist in the evaluation of the borrower's creditworthiness. At a minimum, the credit analysis for a credit union should be administered by adopting the "5 Cs": Character, Capacity, Condition, Capital and Collateral; detailed as follows:
  - a. Character: credit unions should assess the borrowers and guarantors' level of integrity, honesty and commitment;
  - b. Capacity: credit unions should assess the cash flow and level of repayment capacity of the borrower including assessing repayment history as an indicator of borrower's reliability to repay loans on timely basis;
  - c. Conditions: credit unions should assess the condition of the industry market, economy, employment, interest rate, repayment term and the amount and purpose of the loan proceeds (money);

- d. Capital: credit unions should assess the borrower's personal investment into the project/business or personal assets;
  - e. Collateral: credit unions should assess the value and availability of the business's or personal assets of the borrowers or guarantors as a secondary source of repayment.
46. A credit union should require security and guarantees to provide secondary protection to the credit union if the borrower defaults, but ultimately the primary consideration should be the borrower's debt-servicing capacity.
47. A credit union should adopt loan assessment and appraisal criteria, loan application form and pre-qualification criteria checklist and the 5 Cs loan analysis that is proportionate to the credit union's size, nature, risks and operations.

### **Loan Approval**

48. All loans should be approved in the manner prescribed under section 44, 58 and 59 of the Act and section 3 of the credit union Regulations, and by-laws 30.
49. Each credit union should document loan approval procedures for the granting of loans in proportionate to its size and nature of business operations. At a minimum, the procedure should identify the documentation required and risk acceptance criteria for applicants to meet in order to approve new loans and/or change the terms of existing loans.
50. The loan approval procedures should identify the relevant approval authorities and accountabilities in accordance with the credit risk policy; and ensure a separation of duties between officers with approval authority.

### **Delegated Credit Authority**

51. Delegated levels of authority to approve loans and their associated approval limits should be specified in the credit risk policy as prescribed under sections 58 and 59 of the Act and section 3 of the credit union Regulation.
52. The level of authority should be clearly delegated by the board and should be appropriate for the types of loan and amount assigned to the credit committee or loans officer as prescribed by the Act and the credit union Regulation. In essence, the board can delegate authority, however, it cannot delegate responsibility or accountability in relation to these lending functions.

53. As the credit risk policy is subject to review, the delegated credit authorities should be subject to timely reviews, to ensure they remain appropriate to current international best practice and market conditions.

### **Loan Security**

54. A credit union's approved types of security and circumstances on which the security should be required, must be clearly set out in the credit risk policy.
55. A credit union should require security for loans that is adequate and enforceable relative to borrower's current circumstances to maintain sound business practices in accordance to section 58 and 59 of the Act and by-laws 30. The level of security required with reference to a loan application should reflect the size and risk profile of the proposed loan.
56. The credit risk policy of a credit union must address the maximum individual loan values for each type of loan which should be made with security as prescribed in by-laws 19.
57. The credit risk policy of a credit union must include approved loan to value ratio for each type of approved security.
58. A credit union must take a risk-based approach using various tools and processes to undertake on-going monitoring of the security.

### **Contractual Requirements**

59. All loan contracts shall be in writing in plain English and borrowers must be provided with a copy of the contract free of charge. Any additional copies requested by the borrower may be charged by the credit union, which the borrower must be informed prior to purchase.
60. For loan contracts specifically, borrowers should be provided with information of a loan repayment schedule that outlines the principal amount, interest payments, and total cost of borrowing over the term of the loan prior to the completion of the contract.

### **Risk Concentration and Loan Limits**

61. Credit risk concentration may arise from high volumes of loans to individual and related parties with similar characteristics including but not limited to specific geographical locations, economic or industry sectors. Credit risk concentration is a

concern to the Registrar's Office because if these loans cannot be recovered, the financial condition of the credit union could be adversely affected.

62. Each credit union should establish internal controls and systems authorized by the board of directors, to measure, monitor and control credit risk concentration and large loan<sup>2</sup> accounts.
63. For prudent practice, credit unions should limit the credit risk concentration on loan portfolio in one or a few related loans. WOCCU recommends the maximum amount of related aggregate loans be the lesser of 10% of the credit union's total assets or 25% of its institutional capital<sup>3</sup>.
64. The by-laws of each credit union must provide limits on the amounts of loans to any one member or as to the type of loans which may be granted.

### **Loan Rescheduling and Refinancing**

65. Each credit union's credit risk policy should clearly document the loan rescheduling and refinancing process proportionate to its size and complexity.
66. For loan rescheduling<sup>4</sup> process, a credit union should clearly detail the criteria, terms, conditions, interest rate and fees acceptable and allowed for loan rescheduling and who should be responsible with the authority to approve loan rescheduling.
67. For loan refinancing<sup>5</sup> process, a credit union should clearly detail the criteria and procedures for granting loan refinancing and approvals with exceptions.

### **Managing Problem Loans**

68. A credit union's credit risk policy should clearly document how problem loans should be identified, circumstances under which problem loan should be measured, assessed

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<sup>2</sup> "Large loan" means related aggregate loans that is 10% or more of the credit union's total assets or 25% or more of the credit union's capital.

<sup>3</sup> "Institutional Capital" means the total of the credit union's regulatory reserve accounts, retained earnings, special reserves (designated for a specific purpose), and net income that has yet to be closed to the retained earnings account. [WOCCU, *Technical Guide: Credit Union Regulation and Supervision*, 2008]

<sup>4</sup> "Loan rescheduling" means changing the terms of the loan, which gives more time to the borrower to repay the loan.

<sup>5</sup> "Loan refinancing" means changing the type or the terms and conditions of the existing loan, which help the borrower to improve his/her current cash flow.

and managed; and who should be responsible for overseeing this function. The establishment of this responsibility should be dependent on the size and complexity of the lending operations of the credit union.

69. A credit union's credit risk policy should clearly document the loan recovery procedure that is proportionate to the size and complexity of the lending operations of each credit union. The loan recovery procedure is crucial to systematically recover loans from borrowers with past due or overdue loan repayments, and will help reduce problem loan.
70. A credit union must document all steps to take to pursue claims against a borrower with problematic loans, and should be visible to the responsible officers. This may include the process of foreclosures and repossession in case of assets used as loan collateral.
71. The rate of interest on problem loans should be treated in accordance with Regulation 4 of the credit unions Regulations.
72. A credit union should set its own acceptable internal limits in percentage of the total loan portfolio and capital for problem loans considering loans past due days. For prudent practice, a credit union should not grant new loans to pay off the outstanding principal and interest for the borrower with problematic loan.

### **Provisioning for Doubtful Loans**

73. All credit unions shall maintain an account on the balance sheet entitled "Provisions for Loan Losses" (also called "allowance for loan losses and reserve for doubtful debts"). The provisions account shall be created by charges to provision expense in the income statement and shall be maintained at a level that is adequate to absorb potential losses in the loan portfolio. Provisions for loan losses are the first line of defence to protect member savings against identified risk.
74. At the end of each calendar quarter, or more frequently if warranted, the board of directors shall cause responsible officers to evaluate the collectability of all loans, and shall require that appropriate entries be made to i) accurately report earnings, and ii) ensure that the provision for loan losses account is fully adequate to absorb identified and potential losses. Each credit union must maintain records to support their evaluations and shall make them available for inspection by Registrar's Office as requested.
75. Classification Grades Category:

- a. **Pass.** Loans in this category are fully protected by the current sound worth and paying capacity of the borrower or the security pledged, are performing in accordance with contractual terms, and are expected to continue doing so.
- b. **Special Mention.** Loans in this category are secured and repayment is not yet in jeopardy but deficiencies<sup>6</sup> exist which may, if not corrected, weaken the credit union's position at some future date. At a minimum, any loan which is past due 60 days or more but less than 90 days shall be classified as Special Mention.
- c. **Substandard.** Loans in this category are not adequately protected by the current sound worth and paying capacity of the borrower. The primary source of repayment is not sufficient to service the loan, and the credit union must rely on secondary sources such as borrower's savings and realizing on collateral, sale of fixed assets. There is a distinct possibility that the credit union will sustain loss if deficiencies are not correct. At a minimum, any loan which is past due 90 days or more but less than 180 days shall be classified as Substandard.
- d. **Doubtful.** Loans in this category have all the weaknesses inherent in Substandard but the loans are not well-secured. Weaknesses make collection in full highly questionable and improbable on the basis of existing facts, conditions and value. Any loan which is past due 180 days or more but less than 360 days shall be classified as Doubtful, unless (i) the loan is well-secured (ii) legal action has commenced, and (iii) the time to realize on security or on a guarantee does not exceed 180 days.
- e. **Loss.** Loans in this category are deemed uncollectible or of such little value that carrying on the books is no longer warranted. Loss classification does not mean there will never be a recovery, but rather that it is no longer appropriate to defer writing off the loan. Losses shall be taken when identified as uncollectible and shall not remain on the books while pursuing long-term recovery efforts. Any loan which is past due 360 days or more shall be classified as Loss, unless (i) the loan is well-secured, (ii) legal action has commenced, and (iii) the time to realize on collateral or on a guarantee does not exceed 180 days.

76. At a minimum, the following provisioning amounts are to be maintained:

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<sup>6</sup> "Deficiencies" means inability to properly supervise the loan due to an adequate loan agreement; deteriorating condition or control of security; deteriorating economic conditions or adverse trends in borrower's financial position which jeopardize repayment capacity.

Category	Aging (Past Due Days)	Provisioning
For loans graded <b>“Pass”</b> or <b>“Acceptable”</b>	0 days (active)	1%
For loans graded <b>“Special Mention”</b>	1 to 89 days	5%
For loans graded <b>“Substandard”</b>	90 – 179 days	20%
For loans graded <b>“Doubtful”</b>	180 – 365 days	50%
For loans graded <b>“Loss”</b>	>365 days	100%

77. The provisioning percentages above shall be applied against the gross loan balance for loans graded Pass and Special Mention to determine the minimum provisioning to be maintained. For loans graded Substandard, Doubtful or Loss, the “net loan balance”<sup>7</sup> or “net realizable value”<sup>8</sup> as shown in a current valuation report, of savings or collateral may be deducted from the balance of the loan before applying the provisioning percentages.
78. Classification grades category for loans should be based on an assessment of the primary repayment source, generally being an assessment of the financial capacity and/or cash flow of the borrower to repay the debt. Security is a secondary source of repayment and should therefore be considered in determining the severity of the classification grade.
79. The Registrar’s Office will require that credit unions retain on file sufficient documentation of their data record and board of director’s support on the credit union’s provisioning methodology and its estimates.
80. In the aggregate, the level of provisions must reflect the expected loss on each loan.

### **Write-Offs**

81. Each credit union’s credit risk policy should clearly state the write-off process which may include; when loans, which are considered to be in default or problem loans should be written off.
82. For prudent practice, a loan write-off is conducted when a loan is 100 percent provisioned or has reached 365 days past due on a quarterly basis. Particularly if there

<sup>7</sup> “Net Loan Balance” means outstanding balance of the loan deducting Savings.

<sup>8</sup> “Net realizable value” means outstanding balance of the loan deducting Market Value of collaterals.

is Residual Loan Balance<sup>9</sup>, the balance should be written off. Although a loan may be written off the books, the credit union should still seek to collect payment for the outstanding balance.

### **Managing Conflict of Interest in Lending Activities**

83. At a minimum, a credit union must specify in the credit risk policy the procedures and processes for:
  - a. identifying when individuals applying for loan are associated/related parties and pose potential conflict of interest, and such individuals should be classified and dealt with as related party members;
  - b. The granting of loan to associates or related parties and credit union Officers in accordance to the Act and by-laws;
84. A credit union must ensure that all lending assessment and associated transaction for a board of director, credit committee member, supervisory committee member, management, loan's officer and other officers of the credit union be at arm's length. Substantially, applying the same terms and conditions in respect of charges, fees, interest rate, liability, maturity, price, repayments, risk, security etc as the similar transactions between a credit union and a member or a third-party transaction.

### **Accountability**

85. Credit committee, loan officers and all other officers must comply with the credit risk policy and relevant procedures while also being ultimately accountable to the board of directors through reporting and decisions when discharging their responsibilities.

### **Segregation of Duties**

86. For a credit union, segregation of duties is for internal control intended to manage credit risk properly.
87. In establishing credit administration process, credit unions should ensure adequate segregation of duties is in place.
88. In implementing the segregation of duties, each credit union should aim to keep the following functions as separate as possible:
  - a. Loan initiation;

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<sup>9</sup> "Residual Loan Balance" means after the borrower's gross loan has been offset against his/her savings

- b. Approval;
  - c. Review and Administration; and
  - d. Disbursement (Payments and Work-out)
89. Single relevant officer must not perform the duties of all above specified levels simultaneously.
90. Any breaches of internal control and practices relating to segregation of duties should be reported to the board level.
91. A timely and accurate management information system proportionate to the credit union's size and operations should be in place whereby relevant reports on the loans, loan activity and loan performances are generated and available to various executive levels on a timely basis.

### **Risk Mitigation**

92. Effective controlling of credit risk involves risk mitigation techniques. Each credit union should adopt certain mitigation techniques proportionate to their size and nature of operations. Generally, these may include:
- a. Accepting security;
  - b. Netting arrangements;
  - c. Loan covenants; and
  - d. Prudential underwriting practices.
93. Credit unions should document the procedures and controls of such credit risk mitigation techniques and ensure adequate systems are in place to manage these arrangements.
94. Each credit unions should reappraise their security and mitigation techniques on a regular basis.

### **Independent Audits**

95. Each credit union should establish a system of regular independent credit and compliance audits. These audits should be conducted by independent parties like the Supervisory Committee as prescribed in Sections 63 of the Act and by-laws 20, who should report directly to the board or any relevant Committees.
96. A credit audit must be performed to assess credit activities to ensure their compliance with the credit union's credit risk policies and procedures, laws and regulations, on a sampling basis and the overall quality of the loan portfolio. Such credit audits are

considered practical for evaluating the effectiveness of the credit process and risk management.

97. The findings of these credit audits should be reported to the board or relevant committee on a timely basis and ensure appropriate remedial actions be taken to address any concerns and weakness identified.

### **Borrowings by Credit unions**

98. Borrowing by a credit union should be done in accordance with section 64 of the Credit Union Act and keep within the specific limits as prescribed by the Act.
99. Where a credit union wishes to borrow, it must only borrow from any relevant financial institutions licensed by the Central Bank of Solomon Islands.
100. Investment by a credit union shall not proceed without prior approval by the Registrar of Credit Unions.

### **Reporting Requirement to the Registrar of Credit union**

101. Each credit union must submit to the Registrar of Credit union such report as may be required and, in the form, and frequency as the Registrar's Office may prescribe.


### **Enforcement and Corrective Measures**

102. The Registrar's Office will monitor credit unions for sound and prudent Credit Risk Management, through a combination of on-site examination and off-site supervision.
103. A credit union, which fails to comply with the requirements contained in this PGN4 or to submit certain reports to the Registrar's Office, which are materially inaccurate, will be considered as following unsound and unsafe practices.
104. The Registrar's Office may, if it has grounds to believe that the actions of the credit union is detrimental to the interest of members, and to the confidence and stability of the financial system, direct the credit union to pursue all corrective actions, impose additional conditions that the Registrar's Office may consider appropriate, or issuance of an order to deregister.

**Effective Date**

105. The effective date of this Practice Guidance Note is July 1<sup>st</sup>, 2023.

Issued this 22<sup>nd</sup> day of June 2023.

A handwritten signature in dark ink, appearing to read 'Dr Luke Ferau', is written over a horizontal line.

Dr Luke Ferau  
Registrar of Credit union