

Corporate governance in credit unions

Key findings report

Executive summary

This report gives the detailed findings from our review of corporate governance in credit unions. The review found that many credit unions are well run and have effective corporate governance, but there is room for improvement in many – and, in some, room for significant improvement. All officers of credit unions should read this report and consider how they can improve their own contribution to the effective running of their credit union.

Other material is available, including a summary of this report in the January 2007 credit unions newsletter, and web pages which summarise the key roles within credit unions.

Key findings

[back](#)

The main messages from this review are:

1. The Board is responsible for good corporate governance and each member has a role to play.
2. Agree clear, written roles and responsibilities for the Supervisory/Internal Audit Committee. Frequently review the work of this committee and of the General Manager.
3. Be clear – and ensure everyone else is clear – about the roles and responsibilities of all key people.
4. Make sure the only people voting at Board meetings are those who have been elected to the Board (or have been appointed to fill casual vacancies).
5. Avoid dominance by one or more individuals.
6. Give all Officers, especially new appointees, relevant training.

Introduction and background

[back](#)

What is corporate governance?

Corporate governance is the high-level management of a business. It involves putting in place the structure, systems and controls to achieve the business goals.

Background

Many problems at credit unions are due to corporate governance failures. For instance, there have been failures in systems, controls and the financial situation because no-one took adequate responsibility for monitoring the situation. We have seen some extreme examples of corporate governance failings. In one instance, a chairman of a large credit union was allowed by his colleagues to take ultra vires actions that cost the credit union a significant sum and led to a breakdown in relationships and trust between board members, supervisors and staff. In others, Board members were barely on speaking terms, leading to a breakdown in control and a focus on personal interests, rather than the interests of members.

We have looked further into corporate governance to provide help to credit unions. This report aims to highlight the principles for good practice in corporate governance, in line with rules in CRED and SYSC. Firms should refer to CRED and SYSC for full details, and to their own rules.

This report also aims to help people in corporate governance roles at credit unions to understand:

- their roles (and what is not their role);
- their responsibilities (which should be defined clearly); and
- the expected behaviours (so policy-making and policy implementation are more effective).

What did we do?

The project team identified a population of 30 credit unions, divided evenly between small, medium and larger firms. The sample incorporated version 1 and version 2 credit unions. The population also included credit unions within each category, who had staff (paid or non-paid) to make sure the sample was representative.

The division between small, medium and larger credit unions was determined by the credit union's assets (according to the credit union's audited accounts for 2004):

< £500k	- small
£500k -£1m	- medium
> £1m	- large

Credit unions that had already taken part in other FSA projects (Auditor, Key Persons and Lending Policies & Practices) were excluded from the sample.

Once the population of credit unions had been determined, we wrote to 429 individual officers and asked them to complete a questionnaire anonymously. These individuals were all Approved Persons - performing formal roles, such as Directors of the Board, members of the Supervisory/Internal Audit Committee, Chief Executives and General Managers. Due to the poor response rate to our first deadline we sent the questionnaire again to all the individuals in our sample.

The questionnaire was designed to help us identify strengths, weaknesses and good and bad practices within credit unions. We also hoped the questionnaires would help us determine how those individuals operating in a corporate governance structure interacted, assigned responsibilities and made decisions. We sent the questionnaire to individuals in the hope of getting honest personal opinions, rather than any corporate line or agreed responses.

Breakdown of responses

In total, 161 individuals responded which was 37.5% of those surveyed. This was a disappointing number, particularly as the need for a good response was highlighted at both the Scottish League of Credit Unions (SLCU) and Association of British Credit Unions Limited (ABCUL) annual conferences).

The breakdown by size of firm was:

	LARGE	MEDIUM	SMALL	Grand Total
Total sent	169	143	117	429
Responses received	67	58	36	161
Response rate	40%	41%	31%	38%

Key findings

[BACK](#)

Overall, we found examples of good and poor practices in credit unions. We have set out the good practice below so more credit unions can apply these standards.

1. The Board is responsible for good corporate governance and each member has a role to play.

A clear majority of respondents say good corporate governance was the responsibility of the Board and that good Boards hold regular meetings and ensure decisions and changes are carried out in good time. Over three-quarters felt the Board had the necessary skills to carry out their duties – which means that a quarter do not.

Further findings: role of the Board

[back](#)

Responsibility for Corporate Governance

We asked individuals if they understood the importance of corporate governance within credit unions. We also asked individuals to name the person or group responsible for corporate governance. It was encouraging to find that nearly all respondents said they understood the importance of corporate governance. A clear majority believed good corporate governance was ultimately the responsibility of the Board. We would agree with this majority.

Disappointingly, a small minority of respondents from large credit unions believed corporate governance responsibilities rested solely with the General Manager.

Quality of the Board

Respondents said the Boards of credit unions have highly skilled individuals who fully understand their roles. For example we found that:

- nearly all respondents felt the roles and responsibilities of the Board and senior management were clearly defined and understood;
- over three-quarters felt the Board had the necessary skills to carry out their duties;
- nearly all felt it was unusual for meetings to be cancelled due to too few people attending;
- nearly all said the Board made sure any changes or recommendations were carried out effectively and in good time; and
- almost all respondents said the Board communicated its decisions to those responsible for implementing them in good time

These responses are encouraging, but are the roles and responsibilities that are “understood” the “right” ones? We are also concerned that one-fifth of all respondents do not think their Board has the skills necessary for the role.

Board Culture and Decision Making

In our experience, for corporate governance to be effective, the Board should have: a balance of skills and experience; strong challenge from its Supervisory/Internal Audit Committee; and adequate systems and controls to ensure decisions are made and acted on in an appropriate manner. This will ensure that no individual or small group of individuals can dominate the Board's decision making process.

Taken together, the rules in CRED and SYSC and the rules set out in a credit union's own rule book require the Board to have the ability to direct, control and inspire the credit union through broad written strategies and policies that reflect its values and perspectives (and, of course, statutory and regulatory requirements).

To test the effectiveness of the Board we asked respondents:

- who tended to make proposals to the Board?
- were Directors given enough time to have their say?
- were all Board members sufficiently involved in the decision making process? and
- does a dominant culture exist?

Who tended to make proposals to the Board?

Almost a third (over a third in larger credit unions) said it was the General Manager who proposed what the Board discussed; a minority said the Chair tended to propose what was discussed. Encouragingly, well over half of respondents were made aware of what was proposed before the meeting; but this means that many people are attending meetings without prior knowledge of what they will be discussing.

Less than half of respondents said the General Manager or Chair decided what was on the agenda. We expected this figure to be 100%. While we would hope suggestions for discussion would come from Directors, the General Manager, the Supervisory/Internal Audit Committee and even trade bodies, the final decision on the agenda and items for discussion lies with the Chair and Secretary.

Were Directors given enough time to have their say?

Most respondents believed they were given enough time to have their say and felt at ease putting forward their ideas at meetings. However, a third of respondents from medium-sized credit unions felt discussions were dominated by one or two individuals.

Were all Board members sufficiently involved in the decision making process?

In general, respondents felt that all relevant parties were sufficiently represented and involved in the decision making process. However, one-fifth of respondents from medium-sized credit unions felt detached from the decision making process.

Once a decision is reached, almost all respondents said credit unions move on to the next item.

2. The Board should be clear – and ensure everyone else is clear – about the roles and responsibilities of all key role holders.

Over three-quarters of respondents said they understood their own roles. Over half believed the roles and responsibilities of senior management were clearly defined and understood and said the division of responsibilities between the Board and General Manager was set out in writing. However we would expect this understanding to be more widespread.

Further findings: key role

When excluding those who perform a specific role, we found two significant differences. Less than a third of respondents from large credit unions who did not sit on the Board seemed to understand the role of the Board. However over half of respondents from small credit unions who did not sit on the Board did understand the role.

A clear majority felt they understood the roles of the General Manager and the Supervisory/Internal Audit Committee.

Training

Our review looked at whether training would help to improve an individual's understanding of the various roles relating to corporate governance. We found that:

- where individuals claimed they had not had thorough training, almost all still believed they had a clear understanding of their role and those of others; whereas,
- where individuals believed they had received adequate training and had the necessary skills to carry out their role effectively, their self-professed understanding of the roles of others within their credit union was slightly reduced.

This shows training is worthwhile because it helps people fully to understand their role and that of others.

Most respondents believed senior management met statutory and regulatory standards. A clear majority of respondents believed the roles and responsibilities of senior management were clearly defined and understood, and the division of responsibilities between the Board and General Manager was set out in writing.

3. Agree clear, written roles and responsibilities for the Supervisory/Internal Audit Committee. Frequently review the work of this committee and the General Manager.

Over half of respondents said their credit union had a Supervisory/Internal Audit plan and that the Supervisory/Internal Audit Committee feed back to the Board with a formal report. Almost half believed the Board of Directors set the remit of the Supervisory/Internal Audit function and most felt the relationship remained professional. We found good practice where good, clear written terms of reference were provided by the Board and regularly reviewed. We also found instances where the Supervisory/Internal Audit Committee set up formal feedback to the Board.

A large majority said the General Manager updated the Board with a formal report. A clear majority said the Board set the remit of the General Manager and review their work annually.

Further findings: the Supervisory/Internal Audit Committee

Most respondents felt the Supervisory/Internal Audit Committee had the right number of people and offered an effective challenge to the Board and General Manager. However, a significant minority of respondents from larger credit unions disagreed:

- over a third of respondents who are members of their Supervisory/Internal Audit Committee felt that they did not have the ability to challenge the Board.
- almost a quarter of such respondents felt that they did not offer a suitable challenge to the General Manager.

Our experience is that a significant number of credit unions find it difficult to attract people to the Supervisory/Internal Audit Committee. This is regrettable as the challenge they can provide is beneficial to the Board, and therefore to members.

A clear majority of respondents said their credit union had a Supervisory/Internal Audit plan. Over half said the Supervisory/Internal Audit Committee feed back to the Board with a formal report, and just under half said the Board of Directors set the remit of the Supervisory/Internal Audit function.

A clear majority of respondents also said the Supervisory/Internal Audit Committee were able to influence the Board, although in certain cases the influence is excessive in that a significant number voted at Board meetings. The vast majority of respondents felt the relationship between the Board and Supervisory/Internal Audit Committee remained professional.

Despite our disappointment that, in some cases, the Supervisory/Internal Audit Committee voted at Board meetings when they should not, we were encouraged to find that in most cases Board meetings took place at least monthly, and the Board were good at communicating information in a timely manner. More importantly, respondents also felt those individuals who were responsible for carrying out changes or the decisions of the Board were given information and direction in good time.

A clear majority said the General Manager updated the Board with a formal report.

Well over half of respondents said the Board set the remit and reviewed the work of the General Manager, and almost in every case that review was carried out yearly. However, just under half of respondents whose credit union employs a General Manager did not know how often the Board carried out a review. Interestingly, while the vast majority said a professional relationship existed between the General Manager and the Board, most of these also said their Board got involved in the day-to-day running of the business at least occasionally, if not more often.

4. Make sure the only people voting at Board meetings are those who have been elected on to the Board.

This was an area in which most credit unions showed good practice, but our attention was drawn to the poor practice. Almost one-third of credit unions whose rules only allow Board members to vote, allowed the Supervisory/Internal Audit Committee members to vote as well. Over one in four respondents said the General Manager/Chief Executive votes at Board meetings.

Boards are strongly advised to check their credit union's registered rules on this subject so they meet the required standards and cannot have their decisions challenged.

Further findings: voting at Board meetings

We were very disappointed to find that ineligible people vote at Board meetings.

While ACE-affiliated credit unions have rules that lead to members of the Internal Audit Committee being appointed from elected Board members, at credit unions affiliated to other trade bodies members of the Supervisory/Internal Audit Committee are not Board members so cannot vote at Board meetings. Even excluding respondents from ACE-affiliated credit unions, a third of respondents said such committee members are allowed to vote at Board meetings.

Further, over a quarter of respondents said the General Manager/Chief Executive votes at Board meetings. There may be a few exceptions or misunderstandings by respondents but General Managers/Chief Executives who are employees are answerable to the Board but are not part of it. They cannot vote at Board meetings. Allowing them to do so is almost certainly a breach of a credit union's own registered rules and is also a failing in good corporate governance practices.

We recognise the results may not be as bad as they seem as there will have been more than one respondent from any one credit union. However, any cases of ineligible voting are disappointing.

5. Avoid dominance by one or more individuals.

Most credit unions showed good practice in this area. Boards need leadership, but leadership should not be dominance. Almost a quarter of credit unions have individuals who dominate to a degree considered excessive by their colleagues. We found examples where credit unions have taken action to address this, such as:

- bringing in new members with new skills and fresh ideas;
- offering learning opportunities to members like training or by rotating roles;
- involving all Board members sufficiently in decision making;
- accepting proposals to the Board from a spread of role holders; and
- agreeing to give all members of the Board the opportunity to have their say.

Further findings: dominance of a credit union by an individual or group

We asked individuals whether they believed a dominant culture existed within their credit unions. The vast majority said a dominant culture did not exist. However, almost half of respondents from medium-sized credit unions said a dominant culture did exist. When asked if the Board members followed the propositions of these dominant individuals, without challenge, a clear majority said the Board often followed the recommendations of the dominant individuals, especially in smaller firms.

Where a credit union was dominated, the dominant person was said to be (in order of frequency):

- the Chair
- the Treasurer
- the Chief Executive Officer (CEO)
- the Executive Committee

Furthermore:

- a significant minority of respondents from small firms said the Board was dominated by the senior members acting collectively;
- a significant minority of respondents from small and medium firms said the Board was dominated by the Treasurer; and
- half of large firms said their Board was dominated by the Treasurer.

Corporate governance in credit unions

We then tried to find out why a dominant culture existed, as respondents clearly also felt their Boards were well run and roles were clearly defined. As stated earlier, revitalizing committees and swapping roles around leads to a reduction in a dominant culture. A good way to achieve this is by injecting new blood through contested elections and rotating roles. But does this happen? We asked Directors how often elections were contested for the Board at their credit union. We found the following results:

	Larger	Medium	Small	Grand Total
Always /most years	77%	53%	62%	64%
Never	5%	10%	33%	13%
Occasionally / rarely	19%	38%	5%	23%

When analysing how long individuals had served in their roles we learned that, among respondents:

- 18% had been in that role for less than 3 years
- 34% had been in that role for between 3 and 6 years
- 23% had been in the role for between 7 and 10 years, and
- 25% had been in the role more than 10 years
- 60% of those who have been in their current role for at least seven years reported that they had contested elections every year; and
- 68% of board members of large credit unions and 100% of those from small credit unions who had been involved in running the business for at least 7 years stated that they also had contested elections every year.

These statistics show a significant number of those who have been actively involved in running credit unions for several years remain through choice, as opposed to not being able to find replacements. Alternatively, although people volunteer to take on roles, they are either put off by Nominations Committees for not having the required skills and experience (or for other, less understandable reasons), or the members re-elect those already in post. A lack of turnover of officers within a credit union can help to foster dominance; it also prevents fresh eyes being cast over systems and methods and fresh ideas being suggested.

It is good practice for credit unions to review the training available to all officers and employees and, where necessary, seek to improve the training they offer so all involved have a clear understanding of all roles within the credit union. This will let more people contribute to debates and offer ideas for improvement. It will also reduce dominance.

6. Give all Officers, especially new appointees, relevant training plans, and implement them

The survey also told us most respondents who have received training believe their credit unions have a good understanding of regulatory and statutory requirements. However, sometimes we find credit unions who do not meet our minimum standards are unaware they were doing wrong. It is good practice for credit unions to review the training they offer in this area, particularly on prudential rules (that is, rules governing the finance) and on the FSA's principles for businesses.

Final summary of good and poor practice

[back](#)

Here is a summary of the good and poor practice we found:

Good practice found

- Board meetings held monthly
- Decisions and changes carried out in good time
- All Board members sufficiently involved in decision making
- Internal audit plans set up and reviewed by the Board
- Formal feedback is provided from Supervisory/Internal Audit Committee to the Board
- Staff being well informed about the running of the credit union
- Good understanding of the importance of good corporate governance
- Clear understanding that corporate governance is ultimately a Board responsibility
- Senior management roles and responsibilities clearly defined and understood
- Proposals to the Board coming from a spread of role holders
- All members of the Board having the opportunity to have their say
- Boards with a good range of skills
- Committees are refreshed from time to time to bring in new ideas and also to broaden the skills base of individuals. In some cases this was done by rotating roles within the credit union. In others, by Board members actively seeking members with suitable skills to join the governance structure.
- Good, clear, written terms of reference for the Supervisory/Internal Audit Committee (and any other committee).
- Regular review by the Board of the Supervisory/Internal Audit Committee's work, of the work of the General Manager and of the Board itself.

Poor practice found

- Lack of Board involvement in setting the remit of the Supervisory/Internal Audit committee
- No Supervisory/Internal Audit Committee plan
- No clear written terms of reference for the Supervisory/Internal Audit Committee
- No regular reviews of the work carried out by the General Manager
- General Manager and members of Supervisory/Internal Audit Committee voting at Board meetings
- An over-dependence on the skills of an individual or individuals
- Dominance by an individual or individual.
- Lack of appropriate training within some credit unions. In some cases training had been given at the outset, but ongoing training needs were rarely reviewed
- Officers and staff having a poor understanding of roles – their own and others - within the credit union
- Unclear division of responsibilities between the Board and those running the business on a day-to-day basis
- Potential volunteers for elected roles being discouraged, or at least not actively welcomed.

Further help and next steps

[back](#)

A summary of this report is available in the January 2007 credit union newsletter, which can be found on the credit unions web pages: www.fsa.gov.uk/smallfirms/creditunions. Here you can also find information on the different corporate governance roles at a credit union.

The FSA recognises the widespread reliance on volunteers within the credit union sector and of the difficulties in attracting and keeping competent individuals. We take a pragmatic approach and do not expect them all to have the resources to meet all their training needs.

It is not our role to prescribe how each credit union should improve or to provide all the training and support that might be needed. However, we offer “surgeries” around the country (free of charge). Where surgeries are being held in your part of the UK, your credit union will receive an invitation. Details are also available on the credit union web pages. We are also thinking of offering training on corporate governance. If you would benefit from this, please let us know at smallfirmscommunications@fsa.co.uk

Also the various trade bodies offer support and training to their member credit unions and, in many parts of the country, groups of credit unions work together. The movement is a co-operative one and we know there are many good examples of mutual self-help.

Each credit union - and each individual officer - should consider whether there are gaps in their understanding and shortcomings in their procedures, relationships and behaviours and do something about them, to the benefit of their members.