Desjardins

Montréal, March 1, 2024

Mr. Mark White,
Chief Executive Officer
Financial Services Regulatory Authority of Ontario
25 Sheppard Avenue West, Suite 100
Toronto, ON M2N 6S6
contactcentre@fsrao.ca

Re: Consultation: Proposed Guidance: Commercial Lending

Dear Sir,

We have reviewed with great interest the Financial Services Regulatory Authority of Ontario's (FSRA) draft *Commercial Lending Guidance (the "Guidance"),* which has been submitted for public consultation.

As the leading cooperative financial group in North America, with more than $423 billion in assets[1] and 7.5 million members and clients[2], Desjardins Group (the "Group") offers a wide range of products and services across Canada for both Investors and Businesses, including Wealth Management, Individual Insurance, and Damage Insurance. Desjardins Ontario Credit Union ("DOCU") is the seventh largest credit union in the country and the second largest in the province of Ontario, with more than 140,000 members, 46 service centers, and nearly $12 billion in assets[3].

The regulatory environment is constantly evolving, particularly in the current economic environment marked by rapid risk growth, high inflation, and rising interest rates, which increase the risk of borrower default. Indeed, financial institutions are facing several new threats that require a sound and robust risk management framework in order to respond appropriately.

Desjardins Group shares FSRA's objectives to strengthen the resilience of Ontario's financial sector by encouraging credit unions to adopt and comply with prudent commercial lending policies and practices. Our comments on this consultation are consistent with this and are based on the premise that FSRA is committed to providing policyholders with the flexibility to apply the principles of the Guidance given the nature, size, complexity, operation, and risk profile of said policyholders.

1 2023 Financial statements (Desjardins Group)
2 Fact sheet for investors
3 2023 Financial statements (DOCU)

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To this end, we welcome FSRA's commitment to move towards more principles-based regulation, thereby promoting an appropriate and balanced regulatory framework for all financial institutions involved.

Acknowledging DOCU's relationship with Desjardins Group

It is important to note that DOCU is an integral part of Desjardins Group and that the interconnectedness of our integrated business model makes it possible to diversify risks for all of its components, in addition to centralizing many activities for the benefit of the entire Desjardins ecosystem.

Since 2013, the Group has been designated as a "Domestic Systemically Important Financial Institution" ("D-SIFI") according to the criteria established by the Basel Committee on Banking Supervision. This status is reflected in particular in increased supervision and a bail-in regime, as well as additional risk management, capitalization, and disclosure requirements. As a result, DOCU benefits from a robust risk management framework, which contributes to prudent commercial lending practices through the combination of Desjardins Group's D-SIFI status and Ontario's legislative and regulatory frameworks, to which it is subject.

Financial ratios and stress tests

We understand that FSRA wants the credit union to provide financial ratios and stress tests that assess the borrower's ability to repay the loan under normal conditions and in a crisis situation. However, the Guidance does not refer to the possibility for the credit union to consider standard criteria for assessing the borrower's ability to repay. Indeed, the methods of assessing the ability to repay may differ depending on the complexity of the transaction and the risk profile of the borrower. These may include, but are not limited to, an assessment of the borrower's repayment history and current repayment capacity based on financial statements and cash flow projections. We believe that maintaining a diversity of valuation methods promotes flexibility and sound risk management. Therefore, in order to better address the concerns set out, we suggest that FSRA consider this factor in this Guidance.

Technology and commercial lending

We understand FSRA's desire to provide clarity on the use of technology in commercial loan management. However, FSRA already has the *Guidance on Information Technology ("IT") Risk Management*, which sets out the general standards for this purpose. If FSRA wishes to raise general principles about its IT expectations, we believe these should be reflected in the IT Guidance to reinforce all expectations for the use of technology. The proliferation of interrelated frameworks complicates the understanding of expectations, increases duplication, and consequently contributes to an increase in the compliance burden. However, if FSRA intends to maintain these expectations in this Guidance, then we suggest that they reflect only the targeted expectations for commercial lending management.

Credit risk management practices and internal controls

We understand that FSRA expects a credit union to set concentration limits based on its nature, size, complexity, operations, and risk profile. Nevertheless, we are of the opinion that a credit union can legislatively seek to capitalize on its experience in a particular sector in order to be properly compensated to support certain concentrations of risk, provided that the risk of its portfolio is adequately controlled and that its quality respects its risk appetite. Mitigation measures, such as capital increases or risk sharing with other partners, could be considered to reduce dependency on one sector or type of borrower.

In this regard, we believe that it would be beneficial for credit unions if FSRA considered the possibility of establishing mechanisms for managing concentration risk that could include a variety of approaches without limiting the imposition of limits, such as sector-specific limits. This approach would offer each institution the opportunity to manage its concentration risk according to the most appropriate method, taking into account its peculiarities.

Effective date

Given the level of maturity of the financial industry with regard to issues related to the quantification and integration of Environmental, Social, and Governance (ESG) criteria, as well as the low availability and quality of related data, we recommend that FSRA determine an effective date that fully reflects the above factors. Indeed, a reasonable implementation period would facilitate the effective implementation of the objectives of this Guidance and ensure a smooth transition for credit unions, while promoting the effective integration of ESG aspects into their risk assessment practices. In this sense, FSRA could also promote an iterating approach to the integration of ESG criteria into the evaluation of commercial loans in order to allow credit unions to benefit from a phased and adaptable implementation that provides them with the necessary time to adequately comply with the new requirements.

On behalf of Desjardins Group, we thank FRSA for the opportunity to provide feedback and look forward to moving ahead with this project.

Sincerely, Senior Director, Regulatory Relations,

Giuseppina Marra, CPA auditor, ICD.D

Cc.
Mr. William Boucher, Chief Executive Officer and Chief Operating Officer, DOCU
Mr. Olivier Lareau, Chief Risk Officer, DOCU