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Ontario’s financial regulator gives PACE $500-million credit facility

Ontario’s financial regulator has given an extraordinary lifeline to PACE Savings and Credit Union after the troubled financial institution’s capital levels fell below minimum requirements, threatening to put its financial stability in doubt.

The Financial Services Regulatory Authority of Ontario, or FSRA, revealed on Monday that PACE’s regulatory capital – which acts as a cushion to absorb losses or unexpected shocks – will come up short when its 2020 financial statements are released this week. In response, FSRA temporarily lowered minimum capital thresholds for the credit union and will provide a $500-million credit facility to make sure PACE has enough money to meet demand to withdraw deposits.

It is the first time the regulator has extended such a loan to a credit union. FSRA has also barred PACE from paying dividends, redeeming investment shares owned by members except in special circumstances, or paying bonuses to managers and employees.

The rare and significant steps the regulator is taking are to help PACE “continue to operate as a credit union,” and to protect its members, according to FSRA. They are also to bolster confidence that PACE remains viable and to calm nervous members, providing extra financial capacity should members choose to pull their deposits. The credit union has been under varying levels of administrative control and oversight from FSRA and a previous regulator since the fall of 2018, and has suffered repeated false starts while trying to recover from allegations that former senior executives engaged in fraud and self-dealing over a period of years.

In a letter to members on Monday, FSRA chief executive officer Mark White said the $500-million credit facility, which will be secured by PACE’s assets, is to help ensure the credit union can “pay its deposits without disruption or delay.” At the end of 2019, PACE deposits totalled more than $1-billion.

One condition of granting capital flexibility to PACE is that, by May 6, the credit union must contact all members with uninsured deposits – money in accounts that exceeds the $250,000 limit for provincial deposit insurance, or does not qualify for coverage – and either reorganize those deposits so that they are insured, or offer to immediately return them to members.

In an e-mailed response to questions from The Globe and Mail, Mr. White said uninsured deposits are equal to less than one-third of PACE’s liquid financial resources, and that the facility “is indicative of FSRA’s commitment to maintaining stability and confidence in PACE Credit Union and in the sector.”

Normally, PACE must hold capital equal to at least 4 per cent of its total assets, and 8 per cent of risk-weighted assets, but those ratios had dropped to 2.82 per cent and 6.51 per cent as of Dec. 31. Mr. White attributed the capital shortfall to “events of the past year,” including the COVID-19 pandemic and the failure of businesses tied to the credit union that triggered losses for PACE.

Ontario credit unions have a legal right to apply to FSRA to lower capital requirements, but the regulator only considers such requests in exceptional circumstances.

Late last month, FSRA also issued a revised order tweaking the terms of its administration of PACE, giving the credit union’s management more control over day-to-day matters. Since December, PACE has been led by CEO David Finnie, who was appointed after the previous board of directors, CEO and chief risk officer abruptly resigned last November. Mr. White said FSRA has “full confidence in David and the current PACE management team.”

The order still gives FSRA significant power over PACE, allowing the regulator to act in lieu of a board of directors. FSRA also has full control over PACE’s role in two separate lawsuits that could shape the credit union’s fate.

The first was launched against PACE's former president Larry Smith, former CEO Phillip Smith, and ex-directors alleging an array of misconduct and negligence that the Smiths have denied. The second is on behalf of hundreds of investors who collectively lost about $49-million after investing in products tied to Pace Securities Corp., a now-defunct dealer that PACE owned. Those investors are seeking as much as $60-million in compensation, and the dispute has raised questions over who bears responsibility for the harm done to them.

In its order providing PACE with capital relief, FSRA says that it expects funds recovered through the lawsuit against the Smiths will help solve the credit union's capital deficiency, though there is no certainty it will recoup that money. Any sum that is recovered from that legal action could be dwarfed by a potential settlement to end the lawsuit with investors, which is in mediation.

On Jan. 29, FSRA put PACE under a "comprehensive stabilization plan" that requires management to cut costs, reduce leverage, make its commercial lending less risky, and improve governance and controls.

In his letter to members, Mr. White acknowledges that PACE members and employees "have faced much adversity since 2018." In the e-mail to The Globe, he said, "the current environment and its duration will play a major role on how quickly PACE can recover and return to profitability," but insisted the credit union is "solvent and viable."