Banc Ceannais na hÉireann
Central Bank of Ireland

Eurosystem

Feedback Statement on CP113: Consultation on Potential Amendments to the Fitness and Probity Regime for Credit Unions

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1. Introduction

Following a review of the Fitness and Probity regime for credit unions, the Central Bank of Ireland (the Central Bank) published Consultation Paper CP113 Consultation on Potential Amendments to the Fitness and Probity Regime for Credit Unions (CP113) on 8 September 2017. In reviewing the Fitness and Probity regime for credit unions, the Central Bank's objective is to ensure that the regime remains appropriate for the sector and to ensure that credit union members can have confidence that the persons holding key roles in credit unions are fit and proper to hold those roles. The review took account of recent developments such as sector restructuring and business model development, the findings of the themed inspections on Fitness and Probity in credit unions conducted in 2016, and supervisory findings around governance and systems of control arising from on-site inspections conducted by the Central Bank in credit unions.

CP113 set out potential amendments to the Fitness and Probity regime for credit unions, along with a Regulatory Impact Analysis (RIA), and sought views from credit unions and other sector stakeholders on the potential amendments outlined. Feedback was also sought as to whether a tailored regime remains appropriate for credit unions and whether there were additional Pre-Approval Controlled Functions (PCFs) and/or Controlled Functions (CFs) that would be appropriate for credit unions. CP113 posed nine specific questions for respondents to address. The closing date for submissions was 10 November 2017.

In response to CP113, three submissions were received from credit union bodies and one from an internal audit service provider. The Central Bank would like to thank all parties who took the time to make a submission on CP113 to inform the policy development process. All submissions are available on the Central Bank website at the following link.

This feedback statement summarises the feedback received on CP113 and sets out the Central Bank's considered decisions. It is intended to be read in conjunction with CP113 and makes reference to proposals and terms used in the original consultation document, which can be found on the Central Bank's website at the following link.

Section 2 of this feedback statement provides a high level summary of the proposals set out in CP113, the feedback received and the Central Bank's response to this feedback. Sections 3 - 7 provide details on the proposals set out and questions posed in CP113 along with a summary of the feedback received on each question posed in CP113 and the Central Bank's response. The final section of this feedback statement, Section 8, outlines the next steps to be taken in relation to the new requirements for credit unions. The final draft amending regulations for the Fitness and Probity regime for credit unions are set out in Appendix 1.

This feedback statement is published to promote understanding of the policy formation process within the Central Bank and is for information purposes only. This document does not alter legal or regulatory requirements for credit unions. This document does not constitute legal advice and should not be used as a substitute for such advice. It is the responsibility of all credit unions to ensure their compliance with legal and regulatory requirements.

The final Regulations will be effective from 1 July 2018. The Central Bank will provide additional guidance material to support credit unions in complying with the new requirements. The existing Standards of Fitness and Probity for credit unions (the Standards) will continue to apply; due diligence and pre-approval will be required for the 3 newly designated PCFs in the same way as for the existing 2 PCFs, CUPCF-1 (Chair of the Board of Directors) and CUPCF-2 (Manager).

2. Executive Summary

Review of the Fitness and Probity Regime for Credit Unions

In order to ensure that the Fitness and Probity regime for credit unions remains appropriate for the sector at this time, the Central Bank undertook to review the regime in 2017. It had been indicated by the Central Bank at the time of introduction of the tailored Fitness and Probity regime for credit unions in 2013 that a post-implementation review would be undertaken following implementation of the regime for all credit unions.

This review gave consideration to the continued appropriateness of a tailored regime for credit unions, as well as the designation of additional CFs and PCFs for credit unions.

The review was undertaken in the context of recent developments such as sector restructuring and business model development, the findings of the themed inspections on Fitness and Probity in credit unions conducted in 2016, and supervisory findings in credit unions around governance and systems of control arising from on-site inspections conducted by the Central Bank.

Consultation on Potential Amendments to the Fitness and Probity Regime for Credit Unions

Following a review of the Fitness and Probity regime for credit unions, the Central Bank published Consultation Paper CP113 Consultation on Potential Amendments to the Fitness and Probity Regime for Credit Unions (CP113) on 8 September 2017. CP113 set out potential amendments to the Fitness and Probity regime for credit unions, along with a Regulatory Impact Analysis (RIA), and sought views from credit unions and other sector stakeholders on the potential amendments outlined.

CP113 set out the Central Bank's view that a tailored regime remains appropriate for credit unions and that no additional CFs should be introduced at this time. CP113 also outlined current developments with the Minimum Competency Code (MCC) which will have a future impact on the designation of additional CFs for credit unions.

CP113 also set out the Central Bank's proposals for the introduction of three new PCFs for credit unions with total assets of at least €100 million. The proposed new PCF roles are:

(i) Risk Management Officer (CUPCF-3);
(ii) Head of Internal Audit (CUPCF-4); and
(iii) Head of Finance (CUPCF-5).

Feedback Received

The feedback received is broadly supportive of the proposals set out in CP113. All respondents agree that a tailored Fitness and Probity regime for credit unions remains appropriate at this time. Respondents have mixed views on the alignment of the credit union regime to the regime applying to all other regulated financial service providers (RFSPs) at a future stage. Respondents who comment on additional CFs are in agreement that no additional CFs are required within the Fitness and Probity regime for credit unions. Feedback is broadly supportive of the three proposed PCFs for credit unions with total assets of at least €100 million, with some clarity being sought around transitional and outsourcing arrangements.

Central Bank Response

The Central Bank is of the view that a tailored Fitness and Probity regime for credit unions remains appropriate at this time, although the future alignment of the credit union regime to the regime applying to all other RFSPs will be kept under review.

No additional CFs will be introduced for credit unions at this time. However, it is the intention of the Central Bank to undertake further work to gain a better understanding of the impact of extending the scope of the MCC on the credit union sector which will apply to credit unions for their core business, and will have an impact on the designation of additional CFs for credit unions.

The introduction of the three proposed PCFs for credit unions with total assets of at least €100 million, as outlined in CP113, will proceed. The Central Bank has decided to move the commencement date for these PCFs from 1 April 2018 to 1 July 2018 in order to allow for the preparation of the introduction of the new requirements. Supporting documentation will be provided to credit unions in advance of the commencement of the new requirements.

3. Tailored Fitness and Probity Regime for Credit Unions

Proposals set out in CP113

CP113 set out the Central Bank's view that a tailored Fitness and Probity regime for credit unions remains appropriate at this time. Having considered the current profile of the sector and sector characteristics, it is considered that now would not be an appropriate time to align the credit union regime with the Fitness and Probity regime which applies to all other RFSPs.

CP113 sought views on the appropriateness of a tailored Fitness and Probity regime for credit unions at this time.

Question 1

Do you agree that a Tailored Fitness and Probity regime for credit unions remains appropriate at this time?

Question 2

Do you feel that the Fitness and Probity regime for credit unions should be aligned to the Fitness and Probity regime applying to all other RFSPs at a later stage? If so, please indicate what timeline you feel is appropriate for this to occur?

Submissions to CP113

All respondents agree that a tailored Fitness and Probity regime for credit unions remains appropriate at this time, particularly taking into account the unique structure and ethos of credit unions, including the contribution made by volunteers in the sector.

Respondents have mixed views on the alignment to the Fitness and Probity regime applying to all other RFSPs at a future stage. While two respondents explicitly consider the widening of the regime to be inappropriate for credit unions due to their unique model and volunteerism, another respondent considers that it may be appropriate to review this in the future, once credit unions have had sufficient time to embed the requirements of the existing regime.

Two respondents do not believe that it would be appropriate to align the fitness and probity regime for credit unions to the regime applied to other RFSPs, due to the distinctive business model of the credit union sector, its ethos and structure, which includes volunteerism. One of these respondents suggests that if the regime was widened to align with that applying to all other RFSPs, the pre-approval process may have a deterrent effect on certain competent and capable individuals applying for a position in the credit union. This respondent also believes that, on an operational level, the alignment of the regime would give rise to a disproportionate impact on credit unions, and at the very least would give rise to an excessive and disproportionate volume of paperwork. The respondent comments that as credit unions are categorised as medium–low risk by the Central Bank, and carry an inherently lower risk, the Fitness and Probity regime applying to them should reflect this. A second respondent also refers to the inherently lower risk of credit unions, noting that the fitness and probity regime for other RFSPs is therefore not appropriate for the credit union sector.

One respondent comments that closer alignment to the Fitness and Probity regime applicable to all other RFSP's should be considered in due course. While no specific timeline is given, the respondent suggests that an evaluation of lessons learned from the ongoing embedding of the current and proposed changes to the regime could form part of such a consideration. A second respondent also notes that it would be important that any problems are identified and resolved before consideration is given to broadening the designations of additional CFs and PCFs.

In the context of this question, one respondent specifically supporting the designation of the Internal Audit function as a PCF notes that *"it is in the interest of the credit union, its' members, internal and external stakeholders that the quality and value of internal audit services are on par with professional, legal and regulatory standards and the Regulator's expectations for the credit union movement and with wider RFSP sector."*

Central Bank Response

The Central Bank notes that there is agreement from all respondents that a tailored fitness and probity regime remains appropriate for credit unions at this time.

For the purposes of providing clarification on a comment made in one of the submissions to CP113, where it is stated that "*credit unions are categorised as medium–low risk by the Central Bank, and carry an inherently lower risk*", the Central Bank would like to point out that an impact categorisation (e.g. Low, Medium-Low) is applied to each credit union and not to the overall sector. Similarly, the risk rating for a credit union is calculated by considering the individual circumstances of that credit union.

It is the Central Bank's view, having considered the current profile of the sector and current sector priorities around restructuring and business model development, that a tailored Fitness and Probity regime for credit unions remains appropriate. It is considered that now would not be an appropriate time to align the credit union regime with the Fitness and Probity regime which applies to all other RFSPs.

Accordingly, the tailored fitness and probity regime will remain in place for credit unions at this time. However, the Central Bank will keep under review the alignment of the tailored Fitness and Probity regime for credit unions to the Fitness and Probity regime applying to all other RFSPs.

4. Controlled Functions

Proposals set out in CP113

In CP113, the Central Bank outlined its view that now is not an appropriate time to designate additional customer facing CF roles for credit unions. It is considered a priority that credit unions increase their focus on the existing CF roles in order to ensure that the persons in these roles are fit and proper, competent and capable of contributing positively to the governance and internal control framework in credit unions.

CP113 also outlined further work that the Central Bank intends to conduct with regard to the application of the Minimum Competency Code (MCC) to credit unions for their core lending and term deposit business, which would introduce additional customer facing CFs to the Fitness and Probity regime for credit unions.

CP113 sought views on whether additional CFs should be prescribed under the Fitness and Probity regime for credit unions.

Question 3

Are there any additional roles within credit unions which you consider should be prescribed CFs under the Fitness and Probity regime for credit unions? If so, please specify them along with a supporting rationale.

Submissions to CP113

Three respondents comment on this question, with all three expressing the view that no further CFs are required within the Fitness and Probity regime for credit unions. One of the three respondents notes that credit unions themselves determine if an individual has significant influence on the conduct of the affairs of the credit union or is carrying out a compliance related function. The respondent notes that as roles have developed, credit unions have designated certain roles as CFs which had previously not been categorised as falling within a controlled function.

Central Bank Response

The Central Bank notes that respondents consider the existing CFs in the Fitness and Probity regime for credit unions to be sufficient and no additional CFs are being proposed at this time.

However, the Central Bank reiterates the close link between customer-facing CFs and the Minimum Competency Code (MCC).

The MCC sets out minimum professional standards for staff of financial service providers when they are dealing with customers in relation to retail financial products.

The MCC was updated in 2017 (following consultation on the topic through CP106) to reflect requirements arising from EU legislation. The updated MCC has been effective since 3 January 2018 and applies to credit unions authorised as retail intermediaries with respect to their retail intermediary business and to all credit unions when providing mortgage credit agreements.

As part of the consultation on changes to the MCC, views were sought in CP106, on whether the MCC should be applied to credit unions in respect of any retail financial products offered by credit unions that fall within the scope of the MCC. This would mean that the MCC would apply to credit unions for their core lending and term deposit business. Also, the designation of additional customer facing CFs within the Fitness and Probity regime for credit unions would be required in order for the MCC to be applied to credit unions for their core lending and term deposit business. On publication of the updated MCC, the Central Bank communicated that the scope of the MCC would not be extended to credit unions for their core business at this time but indicated that it was the intention of the Central Bank to undertake further work (seeking information from the credit union sector about the level of qualifications already held by staff) to gain a better understanding of the impact of extending the scope of the MCC on the sector and to determine an appropriate implementation approach. When the implementation approach for the application of the MCC has been decided, this will necessitate the creation of additional customer facing CFs for credit unions. The Central Bank will liaise with the sector on these changes in due course.

5. Pre-Approval Controlled Functions (PCFs)

Proposals set out in CP113

CP113 outlined the Central Bank proposal to prescribe an additional three PCF roles for credit unions. It is proposed that these roles would initially be prescribed as PCFs in credit unions where the total assets of the credit union are at least €100 million.

These proposed PCF roles are the:

(i) Risk Management Officer (CUPCF-3);

(ii) Head of Internal Audit (CUPCF-4); and

(iii) Head of Finance (CUPCF-5).

It was proposed in CP113 that these roles would be designated PCF roles from 1 April 2018. CP113 posed four questions in relation to the proposed introduction of additional PCF roles.

Question 4

Do you have any comment on these proposed PCF roles?

Question 5

Have you any comment on the application of these proposed PCF roles on a tiered basis to credit unions with total assets of at least €100 million only at this time?

Question 6

Do you have any comment on the proposed commencement date for these roles being designated PCF roles?

Question 7

Are there any other roles which you feel would benefit from being designated PCF roles at this time?

Introduction of Three Proposed PCF Roles

Submissions to CP113

All respondents comment on the three proposed PCF roles for credit unions with total assets of at least €100 million. One of these respondents comments only on the proposed PCF role of Head of Internal Audit (CUPCF-4), which they are in favour of, and view the *"proposed strengthening of the HIA [Head of Internal Audit] role by way of introduction of a PCF regime"* as positive. A further two respondents are in favour of the three proposed PCF roles. One respondent queries why the role of Compliance, Money Laundering Reporting and Vice Chair are not proposed PCF roles, due to the key part they play in credit union operations and governance, and also succession planning in the case of the Vice Chair.

One respondent notes that, in their experience, the calibre of individuals fulfilling the three proposed PCF roles in credit unions is very high and they are not convinced that the conversion of these roles to PCF roles is the correct response to some of the concerns identified by the Central Bank in CP113. They also note, however, that individuals of this calibre will have no concern with the additional pre-approval requirements, and that a different impetus on these roles through the Fitness and Probity Regime may help alleviate the weaknesses and concerns documented by the Central Bank. The respondent notes that they would expect to see a proportionate approach being adopted to the pre-approval process, taking into account the risk categorisation of the credit union sector, especially in comparison to certain other RFSPs.

One respondent requests that the Central Bank provide clarification on the criteria that it will apply in assessing applicants for the proposed new PCF roles, so that credit unions are in an informed position when recruiting individuals to perform these roles. The respondent also requests that the Central Bank provide a clearer definition of the Head of Finance role (CUPCF-5) in order for a credit union to assign this PCF role to the appropriate person, where there is no specified Head of Finance appointed within the credit union. The respondent seeks confirmation that an individual in an in-situ PCF role would not require pre-approval, similar to other PCF roles in the existing regime, and also seeks confirmation that where the individual who carries out the Head of Finance is already a PCF (e.g. a Manager) that additional pre-approval will not be required for this individual as Head of Finance.

Central Bank Response

The Central Bank notes that there is broad support for the introduction of the three proposed new PCF roles for credit unions with total assets of at least €100 million. It is proposed to proceed with prescribing these roles as PCFs in recognition of their importance in credit unions and to focus more attention in credit unions on these roles.

All credit unions are required to have a Risk Management Officer and an internal audit function under the Credit Union Act, 1997. There is no statutory requirement to have a Head of Finance, however from our supervisory experience we have observed that a large number of credit unions with total assets of at least €100 million have a dedicated finance function in place.

The Central Bank views these potential PCFs as key roles and are central roles for credit unions seeking to embed restructuring and to further develop their business model and ensure viability into the future. It is viewed that there should be suitably experienced, competent and capable persons, placed in these roles in credit unions in order to ensure that the tasks and deliverables associated with these key roles are carried out to the expected high standard. From a Central Bank perspective prescribing these roles as

PCFs will provide increased visibility for credit union supervisors through the pre-approval process, on the individuals seeking to hold key roles in the credit unions that they supervise.

The Central Bank acknowledges that not all credit unions may have a designated Head of Finance and that this role in some cases may be performed by the manager. Where this is the case and the Head of Finance role is designated a PCF role, the credit union will be required to ensure that the person performing this role is fit and proper to perform this role regardless of the title assigned to the role, and regardless of whether that person performs another PCF or CF role in the credit union.

In the scenario where an individual performs both the roles of Manager and Head of Finance, if the individual is the in-situ Head of Finance on the date of introduction of the new requirements, then they must be included in the in-situ return to the Central Bank. As part of the in-situ return, the credit union will be required to confirm that the individual is fit and proper for the role according to the Standards of Fitness and Probity for credit unions issued under section 50 of the Central Bank Reform Act 2010 (the Act) and that they have agreed to abide by the Standards. The in-situ individual may continue in their position without applying for pre-approval from the Central Bank, unless they are subject to re-appointment.

The requirements mentioned above for an in-situ Head of Finance also apply to all individuals who are in-situ in any of the three proposed PCF roles.

Any new persons taking up any one of the three proposed PCF roles after the date of commencement of the new requirements will be required to seek pre-approval from the Central Bank prior to taking up the role. In the above scenario where an individual is to perform both the roles of Manager and Head of Finance, if the individual were to take up the role of Head of Finance after the date of introduction of the new requirements, then they must seek pre-approval for the proposed new PCF role, regardless of any prior pre-approval that they had already obtained from the Central Bank for the role of Manager. The same approach is to be taken in any instance where more than one PCF role is to be held by an individual, e.g. Manager and Risk Management Officer.

As is stated in the Guidance on Fitness and Probity for Credit Unions, any pre-approval obtained is solely for the specific PCF role applied for in the specific credit union for which the application is made. This approach also applies to the three new PCFs proposed in CP113. Separate pre-approval is required from the Central Bank for each PCF role. In the scenario where the Head of Finance role is held by the manager, the individual is required to obtain pre-approval for the role of Head of Finance in addition to obtaining pre-approval for the role of Manager.

For clarity, it is the responsibility of the credit union to identify the persons holding CF roles, based on the role and functions of each person. PCFs are a sub-set of CFs, and are therefore by definition also CFs. In determining whether a person is performing a CF, the credit union should assess the role and functions of each person in line with the definitions prescribed in the Central Bank Reform Act 2010 (Sections 20 and 22 – Credit Unions) Regulations 2013 and, for credit unions that are also authorised as retail intermediaries, in the Central Bank Reform Act 2010 (Sections 20 and 22 – Credit Unions) that are also authorised as Retail Intermediaries) Regulations 2015.

The credit union should consider the responsibilities of the specific function and determine the specific competencies expected of a person performing that specific CF. The credit union should be well placed to determine the particular demands of a CF, i.e. what qualifications, experience, knowledge and other relevant factors will make a person fit for the performance of that function. Further details on determining whether a person is performing a CF may be found in the Guidance on Fitness and Probity for Credit Unions.

The three proposed PCF roles for credit unions with assets of at least €100 million are currently CF roles in all credit unions and will continue to be CF roles for those credit unions with total assets of less than €100 million. The Central Bank expects credit unions to undertake adequate due diligence for all CF roles to ensure that only financially sound, honest and ethical individuals who act with integrity and have the competence and capability required, take up these key roles in credit unions.

Tiered Basis of Application of Proposed PCF Roles

Submissions to CP113

All respondents comment on the application of the three proposed PCF roles to credit unions with total assets of at least €100 million only at this time, with three respondents in broad agreement with the proposal. One respondent expresses the view that requirements for additional PCF roles should be based upon risk-based criteria, and not on an arbitrary figure of €100 million in asset size. This respondent also remarks that it is not unreasonable that the same requirements be applicable to all credit unions regardless of size, as all credit union members are entitled to the same high standard of good governance and best practice.

One respondent suggests that the application of the proposed new PCF roles would require monitoring before consideration is given to their introduction in credit unions with total assets below €100 million, and that it may be considered unnecessary to introduce the proposed new PCF roles to all credit unions.

One respondent who comments solely on the introduction of the Head of Internal Audit (CUPCF-4) as a PCF, expresses the view that where a credit union with total assets below €100 million wishes to adopt the proposed changes to the Fitness and Probity for the Head of Internal Audit role for example, this could be done on a best practice basis with the Central Bank being open to considering applications for PCF approvals if so presented.

Central Bank Response

The Central Bank notes that there is broad support for the introduction of the three proposed new PCF roles for credit unions with total assets of at least €100 million only, at this time.

The introduction of the proposed new PCFs for credit unions with total assets of at least €100 million is in acknowledgment of the increased scale and specific characteristics of these credit unions and in recognition of the important role that the key roles of internal audit, risk management and finance in these credit unions have to play in embedding restructuring and assisting the development of strong foundations to underpin sector development including the strengthening of systems and risk controls in individual credit unions.

The Central Bank reminds all credit unions that the proposed PCF roles fall under the current CF roles CUCF-1 and CUCF-2, and in this context, it is the expectation of the Central Bank that all credit unions, regardless of asset size, conduct due diligence on individuals carrying out these functions within, or on behalf of, the credit union. At this time, the Central Bank will not require the pre-approval of the three proposed PCF roles for credit unions with total assets below €100 million.

The proposal that the introduction of the three new PCF roles will apply only to credit unions with total assets of at least €100 million will therefore proceed as outlined in CP113.

Proposed Commencement Date for Proposed PCF roles

Submissions to CP113

All respondents are in broad agreement with the proposed commencement date for the three proposed PCF roles.

One respondent notes that the commencement date is reasonable provided the Central Bank give clarity on the criteria that would be applied during the pre-approval process, while another respondent comments that the focus must be on "*the practicalities of the roles requiring pre-approval going forward and that any prolonged vacancy does not have a negative impact on the credit union*".

One respondent, who queries why the roles of Money Laundering Reporting Officer, Compliance Officer and Vice Chair are not being proposed as PCFs, notes that a commencement date towards the end of AGM season, e.g. 31 January 2019, would be more suitable for the commencement of the designation of Vice Chair as PCF, should these roles become PCFs. This respondent notes that commencement dates for other roles could be earlier than this if in-situ roles are recognised for PCF purposes.

Central Bank Response

The Central Bank notes that there is broad support for the proposed commencement date of 1 April 2018, as outlined in CP113, for the designation of the three proposed new PCF roles. Having considered the timing aspect and in order to allow sufficient time for the collection of in-situ data from credit unions and for the preparatory work needed prior to the introduction of the new requirements including the updating of guidance documents, the commencement date will now be 1 July 2018.

Transitional arrangements will apply to the three proposed PCF roles. All individuals holding these proposed PCF roles in credit unions, at commencement of the application of the respective PCF in the regime, will be deemed in-situ and may continue in their position without applying for pre-approval from the Central Bank. Credit unions will be required to ensure appropriate due diligence on all individuals holding in-situ PCF roles has been undertaken. Credit unions will be required to submit to the Central Bank electronically a list of individuals holding these PCF roles in the credit union and to confirm that the individuals are fit and proper according to the Standards of Fitness and Probity for credit unions issued under section 50 of the Act, and that they have agreed to abide by the Standards. Any new persons taking up one of these PCF roles post 1 July 2018 will be required to seek pre-approval from the Central Bank prior to appointment to the role.

An outline of the next steps involved in the introduction of the three proposed PCFs is given in section 8 of this document.

Other suggested PCF roles

Submissions to CP113

Three respondents provide feedback on whether there may be other roles that would benefit from being designated PCF roles at this time. Of these, two express the view that the proposed roles are sufficient and that no further roles should be designated PCF roles at this time. One respondent queries why the roles of Compliance Officer, Money Laundering Reporting Officer and Vice Chair are not proposed PCF roles, as these roles all play a key part in credit union operations and governance.

Of the two respondents who comment that no further roles should be designated PCF roles at this time, one respondent reiterates the view that a further increase in the number of PCFs could have a negative impact on credit unions in seeking appropriate volunteers, could give rise to prolonged periods of vacancies and therefore the absence of a function being performed, and would lead to a disproportionate amount of administration.

Central Bank Response

The Central Bank notes that there is broad support for the three proposed PCF roles and that the majority of respondents who comment on the designation of other roles as PCF roles are not in favour of the introduction of further PCF roles.

In reviewing the Fitness and Probity regime for credit unions, the Central Bank's objective is to ensure that the regime remains appropriate for the sector and to ensure that credit union members can have confidence that the persons holding key roles in credit unions are fit and proper to hold those roles. It is proposed to introduce the three new PCFs as outlined in CP113, in recognition of their importance in credit unions in embedding restructuring and assisting the development of strong foundations, to underpin sector development including the strengthening of systems and risk controls in individual credit unions, and to focus more attention in credit unions on these roles. It is of the utmost importance that the persons holding these roles are capable, competent and financially sound individuals with the appropriate skills, experience, knowledge and integrity required for the roles relative to the nature, scale and complexity of the credit union. From a Central Bank perspective, prescribing these roles as PCFs will provide increased visibility for credit union supervisors through the pre-approval process, on the individuals seeking to hold key roles in the credit unions that they supervise.

It is the intention of the Central Bank to proceed with the introduction of the three PCFs as proposed in CP113. The Central Bank will, at a future stage, review the possibility of introducing further PCFs and the possible extension of the three PCFs proposed in CP113 to credit unions with total assets of less than €100 million.

6. Transitional Arrangements

Proposals set out in CP113

CP113 outlined that transitional arrangements would apply to the three proposed PCF roles. All individuals holding these proposed PCF roles in credit unions, at commencement of their application in the regime, will be deemed in-situ and may continue in their position without applying for pre-approval from the Central Bank. Credit unions will be required to ensure appropriate due diligence on all individuals holding in-situ PCF roles has been undertaken. They will also be required to submit to the Central Bank electronically a list of individuals holding these PCF roles in the credit union and to confirm that the individuals are fit and proper according to the Standards of Fitness and Probity for credit unions issued under section 50 of the Act and that they have agreed to abide by the Standards. Any new persons taking up one of these PCF roles post the commencement date will be required to seek pre-approval from the Central Bank prior to appointment to the role.

Question 8

Do you have any comment on the proposed transitional arrangements for the designation of the proposed PCF roles?

Submissions to CP113

All respondents provide feedback on this question. Three respondents support the transitional arrangements proposed in CP113, whereby a person taking up one of the new PCF roles from 1 April 2018 and onwards would be required to seek pre-approval from the Central Bank prior to taking up the role, and that credit unions would be required to submit an in-situ PCF return to the Central Bank within a 4-month timeframe.

One respondent comments that, from a risk based perspective, transitional arrangements should take account of the urgency in relation to supervisory concerns outlined in CP113. The respondent comments that the transitional arrangements should also take account of the natural business cycle of credit unions. In this regard, it is suggested by the respondent that the requirements for a voluntary role such as Vice Chair, if designated a PCF role, could be introduced on or after 31 January 2019, a date which would mark the end of the next phase of AGMs. Requirements for in-situ officers could commence in a more telescoped time frame.

One respondent requests clarification around pre-approval for an in-situ individual in one of the proposed PCF roles whose fixed-term contract is extended or who is made permanent.

Central Bank Response

The Central Bank notes that there is broad agreement for the transitional arrangements as outlined in CP113. The proposed date for the introduction of the new requirements is given as 1 April 2018 in CP113. However, in order to allow for the preparation of the introduction of the amending regulations, the Central Bank has decided to move the commencement date for the new requirements to 1 July 2018.

The Central Bank will be in contact with credit unions in relation to the next steps. An overview of the transitional arrangements is given below:

- 1 July 2018 – 31 Oct 2018: In-situ data collection
- 1 July 2018: commencement of new regulations
- 1 July 2018: pre-approval required from this date for all new persons taking up one of the three proposed PCF roles
- 1 July 2018: pre-approval required from this date for an in-situ person whose contract is being renewed

All individuals holding the three proposed PCF roles in credit unions, at commencement of their application in the regime, will be deemed in-situ and may continue in their position without applying for pre-approval from the Central Bank, unless a change in circumstances occurs which constitutes a new appointment or a break in service. Credit unions will be required to ensure that the appropriate due diligence on all individuals holding in-situ PCF roles has been undertaken.

As part of ongoing performance monitoring, the credit union should ask all persons performing CFs, including the three proposed new PCFs, to certify that they are aware of the Standards and agree to continue to abide by those Standards on an annual basis at a minimum.

As part of the in-situ data collection, credit unions will be required to submit to the Central Bank electronically a list of individuals holding these PCF roles in the credit union and to confirm that the individuals are fit and proper according to the Standards, and that they have agreed to abide by the Standards.

Any new persons taking up one of these PCF roles after the date of commencement of the new requirements will be required to seek pre-approval from the Central Bank prior to appointment to the role.

As is currently the case with applications for the role of Chair or Manager, the Central Bank expects that the pre-approval process for the three proposed PCFs will be based on the Individual Questionnaire, reference checks, and in some cases requests for further information. Where the Central Bank considers it necessary, it may conduct an interview with proposed holders of PCFs before deciding on whether or not to approve an application.

Persons who are in situ in PCF roles which are subject to employment contract renewals or reappointments (which constitute a break in service) will be required to be pre-approved on re-appointment to the PCF role. The approval given by the Central Bank will outline any future requirements on the credit union with regard to the specific applicant. Once a person who has been through the pre-approval process for a specific PCF role that is subject to re-appointment, it is the intention of the Central Bank that the initial approval given shall state that s/he shall not be required to undergo the approval process again as long as s/he remains in that specific PCF role. The credit union however will be required to confirm to the Central Bank upon re-appointment that his/her circumstances have not changed since pre-approval was granted.

Guidance material will be developed to assist credit unions with the introduction of the new requirements.

7. Practical Considerations re. Outsourcing

Proposals set out in CP113

CP113 set out the proposal that the outsourcing arrangements applicable to RFSPs under the existing Fitness and Probity Regime will apply to credit unions where they outsource any of the proposed PCF roles. The Central Bank would expect that in the majority of cases, where roles are outsourced, they will be outsourced to unregulated entities. Where this occurs, the outsourcing agreement between the credit union and the entity will be required to specify the individual within the entity who will be responsible for carrying out the PCF role. The credit union will be required to seek pre-approval from the Central Bank prior to appointing the individual to the PCF role and the individual will be required to comply with the Standards of Fitness and Probity.

Question 9

Do you have any comment on the requirements and obligations on the credit union where PCF roles are outsourced?

Submissions to CP113

Four respondents comment on this question. While no objections to the proposed requirements or obligations are made, three respondents raise some concerns or seek clarification on specific areas relating to outsourcing.

One respondent notes that, while they have no difficulty with the principle of requiring pre-approval as proposed in CP113 for outsourced roles, they have a number of comments. Clarification is sought on whether an individual already pre-approved to carry out a specific PCF would be required to obtain pre-approval to take up the same PCF role in another credit union. The respondent's view is that since a RFSP providing an outsourced role to a credit union is not required to seek pre-approval, the same type of exemption should apply to a pre-approved individual from an unregulated outsourced provider who is already providing the same service to other credit unions. The respondent also seeks clarification on the naming and pre-approval of an individual in cases where more than one individual from the outsourced service provider carries out the PCF role in practice.

One respondent raises a concern that outsourcing of the Risk Management function to a third party is not compliant with the Credit Union Act, 1997, as the 'outsourced' Risk Management Officer in this case would not be considered an employee of the credit union.

Another respondent raises a concern that individuals or firms undertaking PCF functions on an outsourced basis to credit unions may use this as an opportunity to increase fees charged to credit unions. The respondent comments that they have no objection to the proposals and believe that it will assist in raising the standards for outsourced providers. The respondent also welcomes the Central Bank's proposal that guidance would be provided in relation to requirements on the credit union where PCF roles are outsourced.

Another respondent, who comments on the introduction of the Head of Internal Audit (CUPCF-4), states that the Central Bank's intention to issue guidance in relation to Fitness and Probity requirements for outsourced roles in credit unions is a *"proactive and positive step"* towards strengthening engagement between the Head of Internal Audit role and the Central Bank.

Central Bank Response

The Central Bank notes that no objections are raised regarding the proposed requirements and obligations on credit unions where PCF roles are outsourced, and that a number of clarifications are sought in relation to some practical considerations.

While the Central Bank will issue guidance on these requirements and obligations, it is important to note that, ultimately, it is the responsibility of each credit union to undertake due diligence to ensure that an individual is fit and proper to perform the role, taking account of the nature, scale and complexity of the credit union, irrespective of whether the role is outsourced or not.

A credit union cannot rely on another credit union's or regulated financial service provider's due diligence and assessment that a person complies with the Standards. The credit union must take appropriate steps to satisfy itself on reasonable grounds that the person complies with the Standards.

Individuals from unregulated outsourced service providers who hold one of the three proposed PCF roles at commencement of their application in the regime will be deemed in-situ PCF role holders and will be subject to the requirements for in-situ individuals, as described in the section on Transitional Arrangements (section 6) in this document.

All in-situ PCF role holders may continue in their position without applying for pre-approval from the Central Bank, unless their contract is renewed or there is a break in service. Credit unions will be required to ensure that the appropriate due diligence on all individuals holding in-situ PCF roles has been undertaken.

Any new persons taking up one of the three proposed PCF roles after the date of commencement of the new requirements will be required to seek pre-approval from the Central Bank prior to appointment to the role. In the event of a contract renewal, the individual is required to seek and obtain Central Bank pre-approval before the renewal takes place. The approval given by the Central Bank will outline any future requirements on the credit union with regard to the specific applicant.

The process for seeking pre-approval for individuals from an unregulated outsourced service provider will remain the same as in the existing Fitness and Probity regime. A pre-approval is only valid for the PCF role being applied for, in the institution that sought the pre-approval. Where an individual who has already obtained pre-approval for a specific PCF in a specific credit union is proposed to hold the same PCF role in a different credit union, a separate application for pre-approval must be made in order for the Central Bank to assess the applicant based on the most up to date information, and on their ability to conduct the PCF role in that specific credit union based on its nature, scale and complexity, and on their ability to conduct the PCF role in an increased number of credit unions.

Where more than one individual from an unregulated outsourced service provider conducts the PCF role in a credit union, pre-approval must be obtained for the individual who has ultimate responsibility for, and who ultimately signs off on reports submitted to the credit union.

Finally, the Central Bank would like to clarify that the role of Risk Management Officer may be outsourced by the credit union; the requirements outlined above in which a PCF is outsourced will apply to this role. Further details on the role of the Risk Management Officer may be found in the Risk Management and Compliance chapter of the Credit Union Handbook.

8. Next Steps

The proposed date for the introduction of the new requirements is given as 1 April 2018 in CP113. However, as noted in an earlier section of this document, and in order to allow for the preparation and collection of in-situ PCF data, the Central Bank has decided to move the commencement date for the new requirements to 1 July 2018.

An overview of the proposed next steps is as follows:

- 1 July 2018 – 31 Oct 2018: In-situ data collection exercise
- 1 July 2018: commencement of new regulations
- 1 July 2018: pre-approval required from this date for all new persons taking up one of the three proposed PCF roles
- 1 July 2018: pre-approval required from this date for an in-situ person whose contract is being renewed

In-Situ Data Collection

As part of the in-situ data collection exercise for credit unions with total assets of at least €100 million, credit unions will be required to identify those persons who hold the three proposed PCF roles at that time.

Credit unions will be required to ensure that the appropriate due diligence on all individuals holding in-situ PCF roles has been undertaken.

Within 4 months, credit unions will be required to submit to the Central Bank electronically a list of individuals holding these PCF roles in the credit union. The list must be provided to the Central Bank in the format required; the Central Bank will provide further guidance on this process in due course.

Credit unions will be required to confirm that the individuals holding these in-situ PCF roles are fit and proper according to the Standards and that they have agreed to abide by the Standards.

Commencement of New Regulations

From the date of commencement of the new regulations, any new person intending to take up one of the three proposed PCF roles in a credit union will be required to seek and obtain pre-approval from the Central Bank, via the submission of an Individual Questionnaire. Further details on this process is available on the Central Bank website.

All in-situ PCF role holders may continue in their position without applying for pre-approval from the Central Bank, unless their contract is renewed or there is a break in service in which case pre-approval will be required from the Central Bank.

Where more than one individual from an unregulated outsourced service provider conducts the PCF role in a credit union, pre-approval must be obtained for the individual who has ultimate responsibility for, and who ultimately signs off on reports submitted to the credit union.

Appendix 1: Draft Regulations

S.I. No. XX of 2018

CENTRAL BANK REFORM ACT 2010 (SECTIONS 20 AND 22 – CREDIT UNIONS) (AMENDMENT) REGULATIONS 2018

S.I. No. XX of 2018

CENTRAL BANK REFORM ACT 2010 (SECTIONS 20 AND 22 – CREDIT UNIONS) (AMENDMENT) REGULATIONS 2018

In exercise of the powers conferred on the Central Bank of Ireland (“the Bank”) by section 20(1) and section 22(2) of the Central Bank Reform Act 2010 the Bank hereby makes the following regulations:

1. These Regulations may be cited as the Central Bank Reform Act 2010 (Sections 20 and 22 – Credit Unions) (Amendment) Regulations 2018.

2. In these Regulations, “Principal Regulations” means the Central Bank Reform Act 2010 (Sections 20 and 22- Credit Unions) Regulations 2013 (S.I. No. 171 of 2013).

3. Regulation 4 of the Principal Regulations is amended by the insertion of “and Schedule 3” after the phrase “Schedule 2”.

4. The Principal Regulations are amended by the insertion therefor of the Schedule of these Regulations after Schedule 2 of SI 171 of 2013 (as amended).

Schedule

Schedule 3

Pre-Approval Controlled Functions

In relation to

Credit Unions with minimum total asset size of €100 million according to the credit union's latest audited balance sheet.

A person who holds or performs the duties of any of the following positions or offices in the credit union:

(a) Risk Management Officer (CUPCF-3),
(b) Head of Internal Audit (CUPCF-4),
(c) Head of Finance (CUPCF-5).