MULLINGAR CREDIT UNION

Response to Consultation Paper CP125

Consultation on Potential Changes to the Lending Framework for Credit Unions

January 2019

This document contains the views of the Board and Management of Mullingar Credit Union on the proposals contained within Consultation Paper CP125

Comment:

All figures quoted relating to Mullingar Credit Union (MCU) are in reference to the financial statements for the year ended 30 September 2018.

Removal of 5 and 10 Year Lending Maturity Limits:

1. **Do you have any comments on the proposal to remove the 5 year and 10 year lending maturity limits contained in Regulation 14 of the 2016 Regulations (taking account of the other changes to the lending framework)?**

   A. MCU is broadly in favour of the proposal to remove these limits, notwithstanding comments in relation to other questions set out below.

Maximum Loan Maturity Limited for Unsecured Loans

2. **Do you have any comments on the proposal to introduce a maximum maturity limit of 10 years for unsecured loans?**

   MCU is in not in favour of the introduction of a maximum maturity limit of 10 years for unsecured loans; such a measure is unnecessary and restrictive. There was no such specific limit in place and up to now this has not caused any significant issues.

3. **Do you have any comments on the proposed definition of a secured loan?**
   MCU also requires clarification and expansion of the issues highlighted in the ILCU response to CP125, which are as follows:
   - Will the proposed regulation be prescriptive on the minimum % cover required for shares pledged and deposits assigned?
   - There are circumstances when a second legal charge can provide adequate tangible security cover if there is sufficient equity after a first legal charge is satisfied. This could be very relevant in the home improvement loan sector.
   - There are circumstances when an irrevocable solicitor's letter of undertaking can provide adequate security e.g. in relation to the sale of an asset or a court award.

Concentration Limits on House and Commercial Loans

4. **Do you have any comments on the proposal to require that all commercial loan exposures utilise the concentration limit for commercial lending?**
   The proposed ceiling for commercial lending (5% of Total Assets or part of the total concentration for House Loans and Commercial Loans of 7.5% of Total Assets), when applied to MCU, is actually lower than the current amount permitted under the 2016 Regulations.
   Proposed 5% of Total Assets: €12.1m
   Current 50% of Regulatory Reserves: €12.3m

Therefore, to include **all** commercial loan exposures under this concentration limit could significantly hamper MCU's potential for growing the loan book in this sector of lending.

MCU does not consider small commercial loans (under €25,000), particularly to members with established businesses (often small sole traders), to be particularly risky.

MCU is currently utilising approximately [redacted] of its permitted amount of commercial lending, however, this is likely to grow significantly in the coming years with the introduction of the Cultivate Agri-lending product, and the planned introduction of specific SME commercial loan products.

In conclusion, MCU does not agree with the proposal to include all commercial loan exposures in calculating the concentration limits for commercial lending, unless this limit is significantly increased.

5. **Do you have any comments on the Central Bank's intention to introduce board reporting requirements for house loans?**
   MCU is in favour of this proposal.

6. **Do you have any comments on the proposal to introduce a base combined concentration limit for house and commercial loans of 7.5% of Total Assets?**
   MCU does not agree with the principle of a "combined" concentration limit for two entirely different classes of loans. Such a combination will only lead to confusion and potential errors in reporting, and possible non-compliance.

   The two classes of loans are completely different and do not share any cross-over characteristics, it is difficult to see why they are being grouped together?
   House loans are extended based on a member's individual income and secured on that member's principal private residence.
   Commercial loans are extended based on a business profitability and cashflow and may or may not be secured on business assets.

   MCU is of the opinion that separate base concentration limits should be introduced for the two classes of loans, and reporting on such loan classes should be kept entirely separate.

   MCU's views on the proposed limits for each class of loan are set out in the next sections.

7. **Do you have any comments on the proposal to limit the maximum amount of house or commercial lending which a credit union may undertake to 5% of Total Assets within the base combined concentration limit?**
   MCU is not in favour of a concentration limit of 5% of Total Assets in relation to commercial lending. In addition, the proposal to include loans under €25,000 would actually decrease the amount allowed under the proposed new regime for MCU when compared to the current Regulations (again, see (4) above).

   MCU instead would propose a limit of 10% of Total Assets for commercial lending: such a limit would be required in order to be of any significant benefit to MCU in growing this sector of the loan book, and to have any tangible impact on the local commercial economy.

MCU is not in favour of a concentration limit of 5% of Total Assets for house loans. For MCU, this change would only increase the amount allowed by less than €6m.
Current lending over 10 years: [redacted]
Current limit: 10% of total loans over 10 years: €6.3m
Proposed limit: 5% of total assets: €12.1m

While the above may look like a fairly substantial increase, in reality, the potential growth in relation to home loans is very restricted. If an average home loan is €150,000, MCU would be able to lend approximately 70 new home loans before the limit is used up. This is a very small number when compared to the member base of almost 39,000. A higher limit is required in order to give potential headroom so that MCU can really participate in the business of home loans, and be a significant provider of such loans in the local area. MCU needs sufficient headroom so that the home loan / long term lending book can be grown steadily and in a controlled manner.

The ILCU submission on CP125, section 7, contains illustrative data for multiple credit unions. This data shows clearly that the proposed 5% limit is simply not sufficient to allow credit unions to have any potential in growing their home loan business over time.

MCU is in broad agreement with the views expressed within this section of the ILCU submission, but would instead propose an introductory 10% limit of total assets for house loans.

8. Do you have any comments on the proposal to permit an increased combined concentration limit for house and commercial loans for those credit unions who can demonstrate the necessary financial strength, skills, expertise, operations and risk management capability to undertake increased lending in these loan categories?

As mentioned in section (6) above, MCU is not in favour of the "combined" concentration limit for house and commercial loans, for all of the reasons outlined previously.

However, MCU is in favour of the proposal to allow such increased concentration limits (in principle) to credit unions who demonstrate the qualities necessary to undertake increased lending in the relevant categories. However, the two categories of lending are so diverse, that they should require separate application and approval processes in order to avail of the increased concentration limits.

9. What skills, expertise, operational and risk management capabilities do you consider necessary to support increased lending in house and commercial loans?

In terms of house loans, MCU is broadly in agreement with the criteria as set out in the Central Bank document, "Long Term Lending, Guidance for Credit Unions". Section 9 of the ILCU submission on CP125 contains detailed requirements in relation to increased lending in house loans, and MCU is in agreement with these requirements.

MCU is a participant in the ILCU Home Loan CUSO, which in addition to MCU's own internal resources, utilises the expertise of an outsourced supplier (Link) in the assessment and administration of home loans. MCU considers that credit unions who intend to enter the home loan market on any kind of significant scale should consider the use of this shared service or something comparable.

In terms of commercial loans; the skillset is different. Greater expertise is required in relation to the interpretation of SME financial statements, business plans, financial projections and cashflow statements (historical and projected). Credit unions should consider the employment of additional resources where necessary, both in personnel and in the form of automated solutions (analytical tools / credit assessment software), depending on the scale of commercial lending that they intend to undertake. Credit Unions have previously demonstrated their willingness to employ and/or train additional resources in various specialised areas such as risk, compliance and internal audit, acquiring skill sets in commercial lending would be no more onerous.

10. Do you have any comments on the proposed increased combined concentration limit for house and commercial lending of 15% of Total Assets?

MCU does not agree with the principle of combining concentration limits for house and commercial lending.

MCU does not agree with the initial base proposed limit of 5% for either category, and proposes instead an initial 10% of Total Assets as a base for each category.

MCU then proposes that the increased limit for each category should be 15% of Total Assets.

11. Do you have any comments on the application process referred to above?

As set out in (8) above, the application process should be separate for each class of lending. The application and approval process should be robust but transparent, with clear timelines and deliverables. Detailed feedback should be made available where applications are unsuccessful.

Definition of Commercial Loans

12. Do you agree with the proposal to re-name the commercial loan lending category to small business loan?

MCU does not agree with the re-naming of the commercial lending category, particularly the reference to "small". This may be perceived by members, or potential members, that the credit union will only lend "small" amounts of money for business purposes.

13. Do you have any comments on the proposed definition for a small business loan?

The proposed definition for a small business loan is "a loan made for the purpose of financing the working capital or capital investment needs of owner managed small business enterprise". As mentioned in the ILCU submission on CP125, the requirement for the business to be "owner managed" may be problematic. The member may own and control a business, but not necessarily manage it; or the member may manage and control a business, but not necessarily be the sole owner of that business.

MCU also does not support the prohibition on lending for buy to let properties and agrees with the views expressed in Section 13 of the ILCU submission on CP125.

Large Exposures

14. **Do you agree with a large exposure being prescribed as an exposure to a borrower or group of borrowers who are connected of 2.5% or greater of the regulatory reserves of the credit union?**
    MCU is supportive of this amendment.

Transitional Arrangements

15. **Do you have any comments on the proposed transitional arrangements?**
    MCU is in agreement with the proposed transitional arrangements.

Liquidity and ALM Considerations

16. **Do you have any comments on liquidity and broader ALM considerations for credit unions wishing to increase the proportion of their loan books held in house and commercial loans particularly where those loans have longer maturities?**

    MCU is in agreement with the views expressed in Section 16 of the ILCU submission on CP125.

    Credit Unions are highly liquid and experienced very few liquidity issues during the period of the recent recession.