

Submission to Registry of Credit Unions of the Central Bank of Ireland

Consultation on Potential Changes to the Lending Framework for Credit Unions (CP125)

9th January 2019

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)?

We welcome the proposal

Maximum Loan Maturity Limit for Unsecured Loans

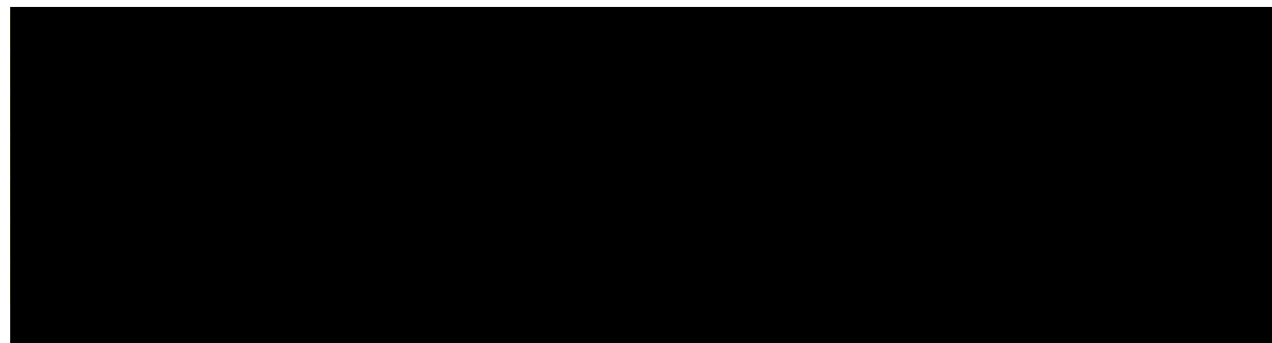
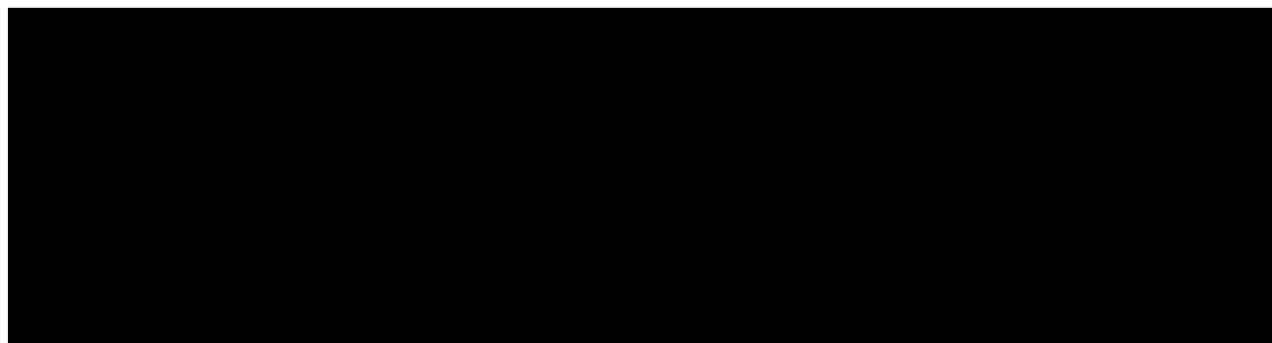
2. Do you have any comments on the proposal to introduce a maximum maturity limit of 10 years for unsecured loans?

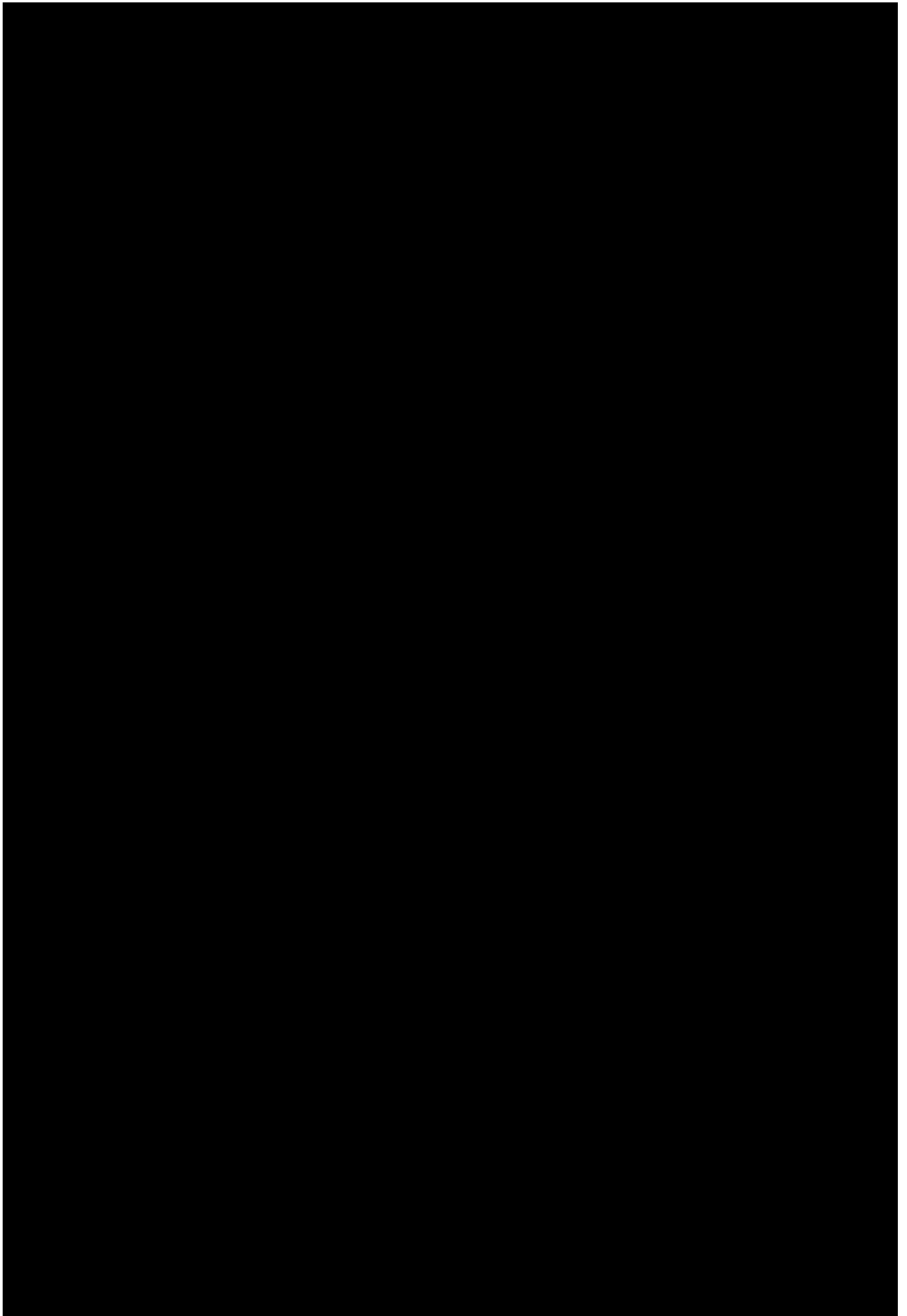
In principle we reject the proposal and ask that a counter proposal of a maximum term of 15 years be considered. This counter proposal is based on St Anthony’s & Claddagh Credit Union’s (SACU) experience and in particular that of the Property Renovation Loan. Currently long term lending is a small part of our business [REDACTED] being 1% of the total number of loans, with a term greater than 120 months. It is an area of growth and in our experience it provides long term security of income from good quality assets particularly Property Renovation Loans which were introduced in November 2015 and have been very successful.

Property Renovation Loans

Background

This loan was modelled on the Special Rate Car Loan which historically had significantly lower arrears than that of the standard rate loan. Beyond standard underwriting conditions this loan required that payment was made to the vendor. A similar condition was included in the Property Renovation Loan and in other Special Rate loans introduced since then.

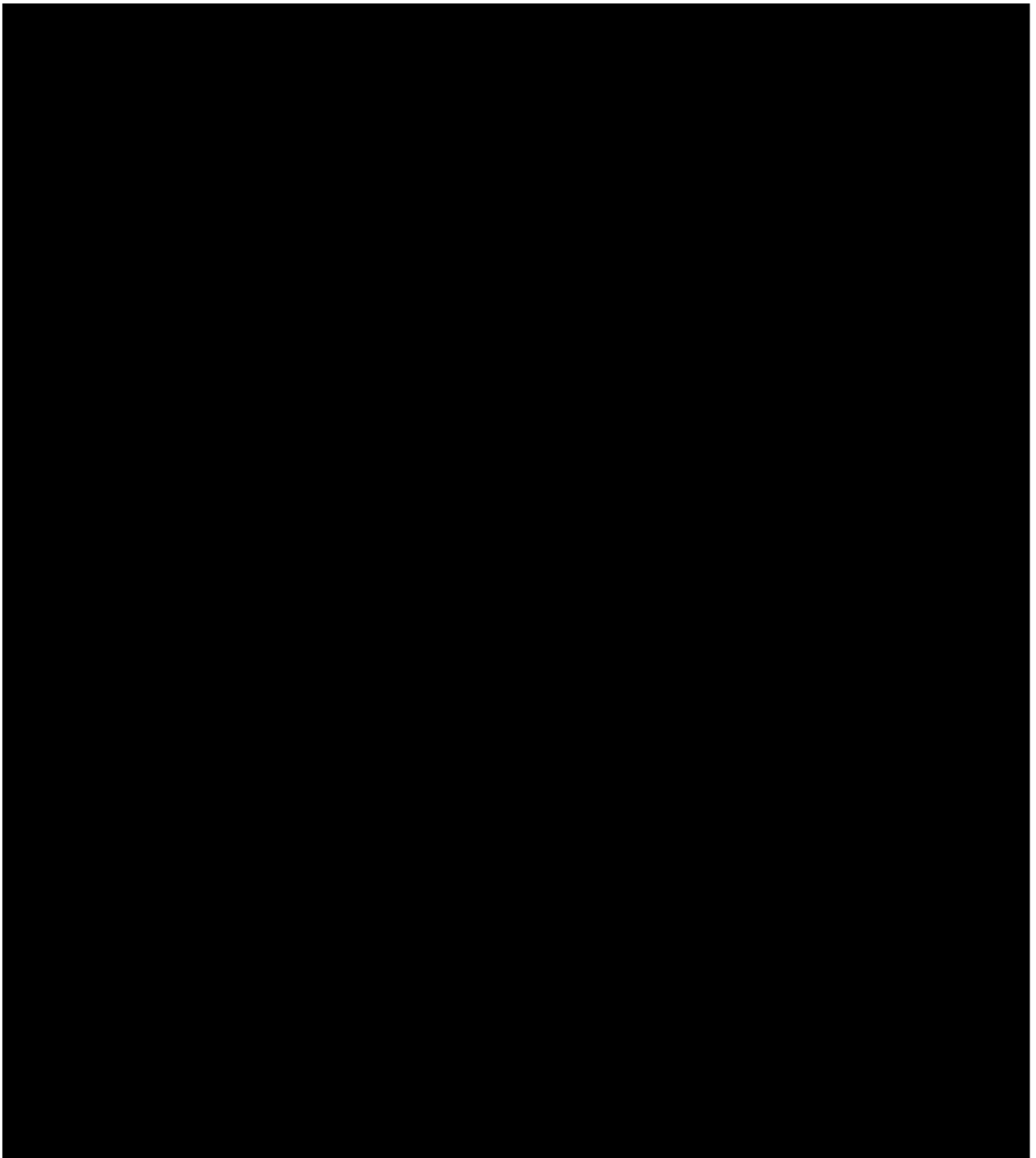




Underwriting

When considering the appropriate term for a Property Renovation Loan the loan policy sets out the standard term as 10 years and the maximum term as 25 years. In practice the term offered will depend on the longevity of the work being carried out the rule of thumb used is

- 180 months for major refurbs or extensions to property
- No longer than 120 months for bathroom or kitchen. Based on feedback from members at counter they will only change the kitchen/bathroom in the family home twice in their lifetime
- 60 months for minor refurbishment e.g. painting, carpets, curtains or furniture etc.





Other Considerations

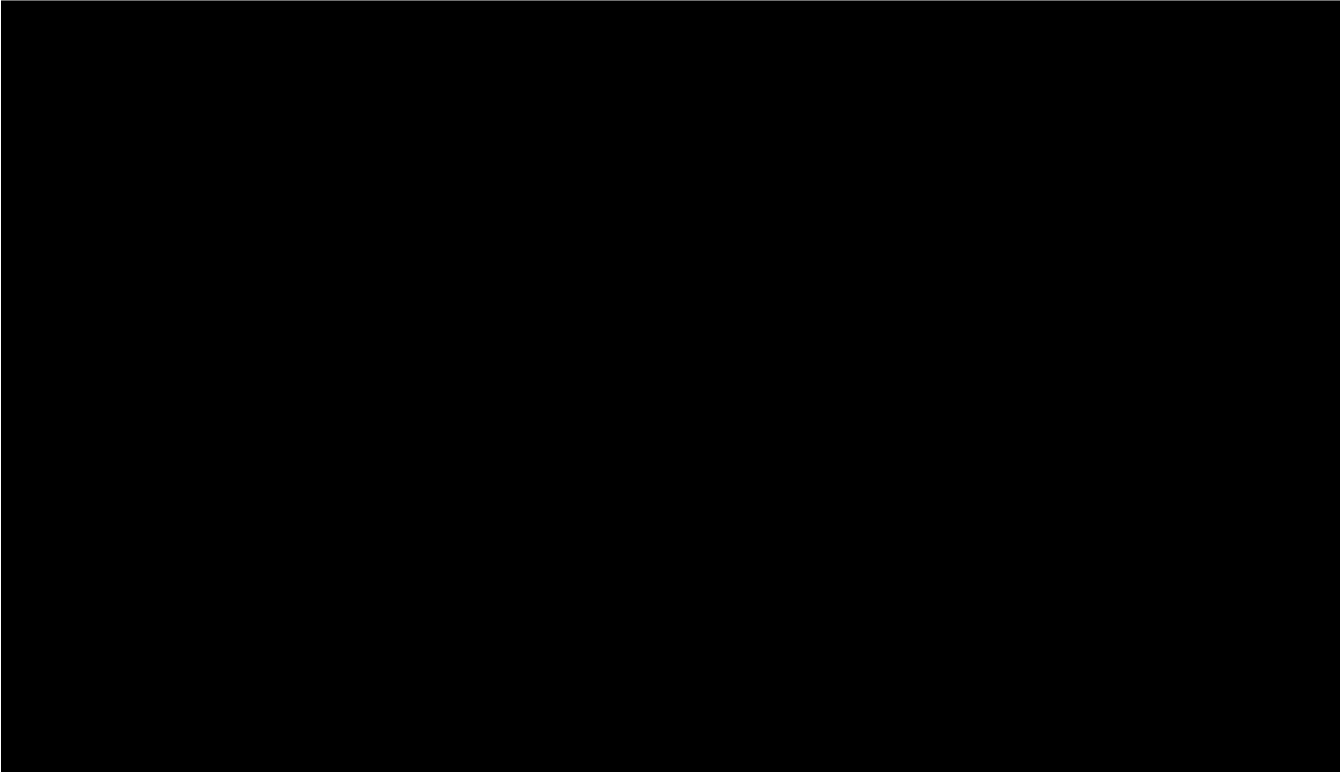
An analysis of the [redacted] other loans with term greater than 120 months [redacted]



The trend in these loans is in line with that seen in the overall loan book i.e.

- Standard rate loans for business & personal use are higher risk as seen in high Current Expected Credit Loss rate. However a term longer than 10 years is sometimes used to manage the repayment for these members. In the context of the Central Credit Registry this option is now more critical as the maintenance of a clean credit history is a significant incentive for members to continue paying.
- Home Improvement Loans are lower risk, [redacted]





To restrict the loan term for unsecured lending to 10 years would remove good business opportunities from the Credit Union. Other examples of such opportunities include:

- Property Renovation for those in niche situations such as
 - No mortgage, high saving and/or low Loan To Value Ratio and reluctant to take on mortgage again
 - Adapting house for
 - Change in personal needs arising from conditions related to
 - Old age
 - Disability
 - Accident or serious illness
 - Multi-generational use
 - In response to the difficulties posed by the housing crisis in Galway many families are adapting the family home to cater for multi-generations. Anecdotally the front counter have had a number of such enquires and we understand that by 2023 1 in 4 homes will be multi-generational.
 - To generate income, opportunities previously identified by members
 - To avail of the rent a room scheme for students. As NUIG is located between both our branches the demand on the Rent A Room Scheme in the common bond is very high

- Air BnB. While we recognise that this may not be a long term option in its current form given government policy, tourism is an integral part of the Galway economy and will always provide opportunities to earn income from property.
- Professional use such as consulting rooms
- Purchase of property in non-traditional circumstances where a legal charge may or may not be an option for example:
 - Buying out a co-owner following divorce/separation
 - Inheriting a property but have to pay CAT or renovation costs
 - Inheriting a share in family property and have to buy out other beneficiaries
 - 2nd residence to be used as holiday home, or where family member s bi locate e.g. working/studying away from home

SACU recognises that we cannot compete head on with banks; therefore our market will not be traditional mortgages such as first time buyers or rate sensitive switchers. We must be a niche player offering good value, not necessarily best price, for non-traditional circumstances such as those detailed above. Members have advised that the attraction of the Credit Union over the bank offering relates to:

- Flexibility including early pay back and option to top up subject to ability to repay
- Free life cover

To leverage these strengths we must be flexible in our approach to lending while recognising and managing the inherent risk of the profile of the loan and of the member. This is critical to our long term sustainability based on our experience of the Property Renovation Loan. Expanding our long term lending effectively will

- Secure an increase in income in the short and long term
- Diversity our loan profile
- Diversify our member profile
- Open opportunities for cross selling of other financial services

3. Do you have any comments on the proposed definition of a secured loan?

We are pleased to note the inclusion of pledged shares and the assignment of a deposit. Covered loans provide a risk free source of income for the Credit Union and support the member in their financial management.

Consideration should be given to the

- Value of a financial guarantor
- Implications of a high or low Loan to Value ratio and/or at Risk Value. Where there is a high level of security the risk is significantly mitigated and as such greater flexibility relating to terms and conditions including length of loan term are appropriate.

Concentration Limits for House and Commercial Loans

we are satisfied that the current proposals will allow us to achieve our plan in this regard. Our concern relates to the prohibition on Buy to let properties and the definition of same. Given the changing member profile i.e. increase in Professional/Managers and Public Sector workers there are opportunities to lend to such members for Buy to let properties in niche circumstances such as those described previously and particularly on the inheritance of a property or the adaption of property to generate income. Our experience of the property renovation loan documented above would indicate that these loans would be good quality. Rather than simply exclude such lending, the risk inherent in the property bubble as seen in the Celtic Tiger days, could be mitigated by imposing Lower Loan to Value requirements.

4. Do you have any comments on the proposal to require that all commercial loan exposures utilise the concentration limit for commercial lending?

No. The current proposal will allow us to achieve our strategy subject to the changes discussed above

5. Do you have any comments on the Central Bank's intention to introduce board reporting requirements for house loans?

No. We strive for a culture of transparency but would be mindful of the work load of the Board and would propose that the reporting be risk based and focus on the key issues rather than a simple box ticking exercise.

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?

No. The current proposal will allow us to achieve our strategy subject to the changes discussed above

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?

No. The current proposal will allow us to achieve our strategy subject to the changes discussed above

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?

No. We would support the concept of tiered regulation and earned flexibility subject to clarity on prudential and conduct requirements and transparency on the implementation of same.

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

As with all lending the key requirements are:

- A strong culture of compliance and risk management embedded in efficient and effective operational process and procedures.
- Competent staff and volunteers who understand the business model, the common bond and the overall strategy of the Credit Union.
- Effective underwriting supported by an understanding of the risk profile of:
 - The loan in terms of purpose, maturity and conditions
 - The member in terms of sources of income and financial management behaviour
 - The local economic environment in terms of security of income
- An overall risk management framework to include policies, processes and risk limits to manage risks inherent in
 - The loan book such as concentration risk be that in relation to a loan type, maturity profile or an industrial sector.
 - The balance sheet relating to maturity transformation

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

No. The current proposal will allow us to achieve our strategy subject to the changes discussed above

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

No, but we would respectfully ask that the application and decision making process be clear and transparent.

Definition of Commercial Loans

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

The change will better reflect the thinking behind commercial lending but we would ask that a separate category be created to account for the opportunities for loans associated with the renovation of property with income generating characteristics.

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

As above

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?

The proposed limit is sufficient for the purposes of our current strategy plan and lending opportunities. However in order to future proof the regulations consideration should be given to the potential of community lending for credit unions individually and as part of a syndicate. Such a hard limit would stifle the potential to develop this business.

Transitional Arrangements

15. Do you have any comments on the proposed transitional arrangements?

We welcome the thrust of the transitional arrangements but would raise concerns of the inclusion of “would only apply to loans which were in compliance.....” History cannot be changed and such a hard line may force the crystallisation of a loss unnecessarily

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?

We welcome the Central Banks view that the Liquidity Coverage Ratio and Net Stable Funding Ratio are not appropriate for the Credit Union sector and the acknowledgement that access to liquid funding is limited. We would be concerned that the requirements in relation to the application for an extension of the limit are vague at this time and would again respectfully ask that the application and decision making process be clear and transparent.