



SUBMISSION FROM

THE CREDIT UNION DEVELOPMENT ASSOCIATION

IN RESPONSE TO

**The Central Bank of Ireland's Consultation on  
Impact Based Levies and  
Other Levy Related Matters  
CP61**

**21<sup>st</sup> February 2013**

## **Introduction**

CUDA (Credit Union Development Association) is a progressive representative & development association that was formed in 2003 by Ireland's most progressive and leading Credit Unions, in recognition of the real need for progressive credit union leadership and development in an increasingly complex financial environment.

CUDA is the only legally incorporated representative association for Credit Unions in the Republic of Ireland. Its membership has over 250,000 members.

We would be happy to elaborate further on any points made in this submission, if required. Please direct any queries on the comments that follow to Ms. Elaine Larke, Head of Legal and Compliance at the contact details at the end of this submission.

We have corresponded with our member Credit Unions. General commentary is provided in Part 1. In Part 2 we have addressed some of the questions, in particular those pertinent to the Credit Union sector.

## 1. General Commentary

Credit Unions have been in Ireland since 1958. They are financial co-operatives that operate on a not-for-profit basis and are managed by voluntary boards of directors elected from among their members. Credit Unions offer a unique range of core products and services, some at no direct cost to members. They have operated successfully in Ireland for 50 years; their services are accessible across all socio-economic groups in local communities. Their services are commendable as are the volunteers that make the credit union sector one of the most popular and wide-spread in developed countries.

CUDA welcomes the opportunity to put forward its comments to the Central Bank of Ireland in consideration of proposed amendments to current levies payable by the Credit Union sector.

We support the Central Bank's aim to optimise the allocation of its finite resources in the performance of its regulatory responsibilities. That said we would not fully be in agreement with the approach proposed by the Central Bank in sourcing the funding to finance its regulatory responsibilities. We believe the approach proposed by the Central Bank will merely create additional financial problems and burdens within the credit union sector which could have the opposite effect as desired on the sector and the economy.

We are opposed to the introduction of a "one size fits all" approach to levy calculation across the financial services sector. Credit unions are recognised in this State as being unique in the financial services' industry. They operate within the financial system but are unique to it. Minister Noonan acknowledged this uniqueness when he stated that "*the Government recognises the important role of credit unions as a volunteer co-operative movement and the distinction between them and other types of financial institutions*" (14th October 2011 on the Publication of the Interim Report on the Commission of Credit Unions).

We appreciate an appropriate measurement is required for all regulated entities however, if the purpose is to sustain the credit union model, the means to achieving this will have to contain important differences.

## 2. Replies to Questions

1. **Do you agree with the Central Bank's proposal to use firms' impact categorisation under PRISM as the basis for the setting of the levies it charges regulated entities on an annual basis? If you disagree, what would you propose instead?**

We have no difficulty in principle with the firm's impact categorisation under PRISM being used as the basis for the setting of the levies. We agree that the development of levy calculation based on a number of variables (ie for Credit Unions Category F metrics are:- member size, regulatory reserves and asset size), as opposed to the application solely on asset size, is progressive.

However, having said that, we have a number of issues that should be addressed. We would question the category selection process. For example, a credit union placed in the same impact category as, for example, global investment firm is, in our view flawed, and we believe the category process should focus equally on probability of failure as on impact.

We are also concerned that whilst PRISM in monitoring current and evolving risks it does not reward regulated entities for controlling and effectively reducing risk within their organisation. Whilst we appreciate this would imply the Central Bank would be required to adopt a subjective test to each entity in levy calculation, we are concerned that the proposed approach does not factor in a mechanism for the reduction of supervisory costs to a sector.

We would welcome the development of a two tier system – the existing objective test coupled with ability for the regulated entity to move downwards from their existing category where they demonstrate clear and effective risk management; secondly, a subjective test based on the likelihood or probability of failure. The impact based approach is bias on the impact to the economy as opposed to the probability of failure. If there is a means for a regulated entity to move down to a lower category – and thus reduce the levy payable - whilst still being permitted to grow the business, we believe this would incentivise entities to focus on the preventing the likelihood of failure through effective risk management.

This is especially relevant for larger credit unions (assets greater than €100m) that are categorised as MEDIUM HIGH \ MEDIUM LOW and are not rewarded for

proper and effective management of risk and a very low probability of risk, which is inherent in their business model.

We would also be concerned that the approach provides no guarantee of the level of the regulatory service provided, and, therefore, our concern is further intensified when aligning this approach with a requirement for regulated entities to contribute to the cost of administering the service.

For the Central Bank to adopt the proposed approach we are of the view more transparency is required. PRISM is not without complication and weaknesses and this, in our view, is reflective in the Central Bank failing to place sufficient attention and resources to a participatory or supportive role. CUDA appreciates the obligations and responsibilities of the Central Bank in protecting the consumer and the economy as a whole. However, we believe for the regulated entity, that is discharging a percentage of the cost to administer this service, there should be a greater sense that they are benefitting from the supervisory approach and related resources. We also appreciate that indirectly regulated entities are benefitting via financial stability. The approach however to date experienced in the credit union sector is that this supervision is somewhat retrospectively applied – and that this in itself comes at a cost to a credit union. We can provide many examples of this from the application of Section 48 to the reactive approach adopted to applying Restrictions on a credit union.

**2. Do you agree with the Central Bank’s proposal to allocate the cost of financial regulation activity on a basis consistent with the allocation of supervisory resources to regulated entities? If not, what cost allocation methodology would you propose?**

We would be of the view that PRISM as a means of levy calculation ignores value benefit; this we have referred to above. We would urge a more proactive approach which should assist this sector in performing their responsibilities and ultimately it is hoped achieve a more favourable impact categorisation for credit unions – this will reduce supervisory requirements and cost. Whilst we appreciate and understand PRISM is a supervisory platform we would caution against acting in a supervisory capacity without providing the guidance and supportive role. We have set out in our Response to Question 4 below, that approach would be greatly assisted through the introduction of an advisory panel.

We believe it is imperative that all stakeholders, should be focused on the means of reducing the likelihood of failure and as a result reduce the level of supervision required – which should undoubtedly be the ultimate goal, and, secure a reduction in the levy calculation. The Consultation Paper does not clarify the means in which all stakeholders can contribute to optimising the cost of supervision and the amount of supervisors required, and, in the long run, the costs incurred in regulating. We note the costs to regulate the credit unions sector for one year amounted to over €9 million.

Whilst we appreciate the responsibility to protect the economy and consumers, there is a concern that the impact based approach, and, the attachment of levy calculation thereto, punishes success - increasing asset and membership does not equate with a deterioration of a good and effective internal risk management.

**3. Do you agree with the Central Bank’s proposal to apply a minimum levy per umbrella plus an additional levy per sub-fund subject to a maximum number of sub-funds (i.e. Option 2)? If not, what alternative approach would you propose and why?**

We are not proficient on this topic and therefore are reluctant to comment.

**4. Do you agree that the credit union sector should be required to fund the relevant proportion (currently 50 per cent) of the cost of financial regulation that would apply under an impact based approach to the levy process? If not, what alternative approach would you propose and why?**

From our analysis on the 14 categories devised by the Central Bank, credit unions are the only industry that operate on a ‘not for profit’ basis. As stated in our introductory comments above, we are not in agreement that a “one size fits all” approach should or can be adopted for all regulated entities which include credit unions. Credit unions are unique in their business model. This is reflective in the unique role credit unions play in society – which unlike some financial institutions are accessible to all socio economic groups. Credit unions do not let people down and this is particularly important in combatting financial exclusion. The sector has its own legislation since 1966, which recognises the distinction between credit unions and other financial service providers. Under the legislation a Regulator is established with statutory powers to regulate specifically for the sector. CUDA has serious concerns that the ethos of credit unions – which is

central to their operating model - is being eroded by applying one approach to all regulated entities without consideration of the distinctiveness of credit union.

Furthermore, we cannot agree that the credit union sector should fund the relevant proportion (currently 50 per cent) of the cost of financial regulation that would apply under an impact based approach, or, indeed under any other calculation methodology, without an assessment of the ability of the sector to shoulder the costs. We stress the importance of a regulatory impact analysis which will take into account recently applied levies, forthcoming additional levies and the increased costs on credit unions as a result of compliance with the forthcoming requirements under the 2012 Act.

The Consultation Paper refers to the need to reduce “the burden on the taxpayer”. We do not disagree with this statement – the need to reduce the burden on the taxpayer is justifiable across all sectors in society and not merely by reflecting on the credit union sector. We have also highlighted above the need for such costs to include and/or emphasis value benefit for the credit unions themselves, with an increased proactive and supportive role being adopted, and, also the need for further transparency on the composition of costs.

We would welcome the establishment of an advisory panel for the sector to help inform the Central Bank of sectoral concerns in the application of PRISM and also to open the channels of communication that will drive the appropriate evolution of this approach. It may be the case that such advisory groups could appropriately be established under the Central Reform Act 1210 (Ref: Section 18).

**5. Do you agree that this change be phased in over a period of 5 years? If not, what alternative approach would you propose and why?**

With the increased costs imposed on credit unions over the last year, in the forthcoming year by way of additional levies, and, increased costs under the 2012 Act, it is appropriate to phase in any increase of levy payable. Furthermore, due to uncertainties with regard to the impact of restructuring on the sector it is appropriate to withhold the application of any increased costs currently. We would also propose at that stage an impact analysis is conducted on the sector; the landscape of the sector may or may not be radically overhauled as a result of the restructuring process, and, as a result of the level of engagement by credit unions with ReBo.

Following the outcome of the restructuring process, of which there are many unknowns – what, for example, will be the scale of the sector, and, the nature and size of credit unions in 5 years. Coupled with the new internal checks and balances imposed on credit unions under the 2012 Act, to agree on an amount or percentage at this stage is untimely. In a 5 year period the matter should be reviewed for the credit union sector. Any change in levy cannot be measured in isolation of the many changes affecting credit unions over the coming years. A balanced view on the ability of a differing credit union sector that may exist in 8 years – when it is proposed that a levy of 50% will be fully operational – cannot be formulated at this point in time.

However, we are in agreement that any change in levy can only commence once ReBo is at an end, and, an assessment is made of the continuance of the credit union levy (restructuring and stabilisation), as well as assess the effectiveness of the improved governance under the new Act and the regulations thereunder. If the desired effect is achieved one would anticipate less supervisory capacity will be required for the sector. To make an assessment now is to base the assessment on the current system; we would caution against this.

**6. Do you agree with the Central Bank’s proposal to impose an application fee in respect of each industry funding category proportionate to the average time taken to consider an application for authorisation? If not, what alternative would you propose?**

CUDA is not in a position to agree with this proposal as we do not have adequate information to formulate a constructive view. In fact Section 7.1 (Application Fees) generated many questions here amongst our member credit unions.

Section 7.1 sets out that “the amount of the application fee will take into account the cost to the Central Bank of processing an application” Appendix C sets out an example of illustrative proposed application fees. On what basis are the fees arrived at? We would caution against the imposition of applying application fees without the Central Bank being satisfied that they have provided clear guidance and instruction for obtaining Central Bank authorisation and leadership to entities in providing successfully completed application. The Consultation Paper states an application fee would deter applications from “those who are not fully satisfied that they can meet the requirements for authorisation”. Whilst we do accept the need for Central Bank independence, we would welcome a more informative role



on the part of the Central Bank - we believe this would circumvent a great portion of applications being rejected, or indeed inappropriately or incorrectly submitted.

It would seem odd to us that, as suggested in the Consultation Paper, there is a great portion of applications from entities “who are not seriously interested in establishing in Ireland”. Has the Central Bank considered the ability of imposing an application fee just on such entities as referenced in the Paper i.e entities outside Ireland wishing to establish in Ireland – one would think that additional oversight and investigative work is required by the Central Bank for such entities in any event.

**7. Do you agree that such a fee should be payable at the time an application for authorisation is submitted and that it should be non-refundable in the event that an application for authorisation is withdrawn or refused? If not, what alternative would you propose?**

We are not in a position to agree to this. With the limited information provided in Section 7.1, if an application for authorisation is refused we do not believe this should warrant retention of any application fee payable. Further clarity is required. In the event that an application is refused, we are uncertain whether the Central Bank provides feedback to the applicant as to the reasons for refusal. Furthermore, would a subsequent application also incur a fee? In this scenario, if a prospective credit union were to submit an application on two occasions to seek authorisation they would potentially incur a cost of €10,000. Specifically, for a credit union which is a group of individuals with a common purpose we would have to question if this is a fair and equitable approach.

Finally, on this issue, if it is the intention for the Central Bank to propose a fee at application stage, CUDA would suggest that a process is developed whereby the application is not refused but merely passes to a second stage where additional supporting information may be sought and provided, perhaps, under the process of an appeal.

**8. Do you agree with the Central Bank’s proposal to maintain the policy of imposing pro-rata levies in respect of the period in relation to which a regulated entity holds an authorisation from the Bank? If not, what alternative do you propose?**

We have no difficulty with this proposal. It would appear a fair and equitable approach.

**9. Do you agree with the Central Bank's proposal to impose a penalty on any and all firms who do not pay their levy within the time allowed? If not, what alternative course(s) of action would you propose to ensure that all regulated entities pay their Industry Funding Levy?**

The approach adopted by the Central Bank is dependent on the Policy formulated and communicated to all financial entities as to the intended steps to be adopted by the Central Bank in the collection of a levy.

An informative approach is required by the Central Bank to ensure that regulated entities are familiar with the process adopted by Central Bank from early warning letter to the imposition of penalties. Further consultation with stakeholders will be required on this issue. CUDA would caution against the imposition of penalties on the sector without prior dialogue.

As a precautionary step, CUDA would suggest an appeals process is adopted internally by the Central Bank with further recourse, and reassurance, that such regulations are appealable to the IFSAT. Recourse must be in a cost effective manner to cater for all category of regulated entity.

**10. Do you agree with the Central Bank's proposal to seek the power to unilaterally revoke the authorisation of those firms which continue to fail to pay their Industry Funding Levy? If not, what alternative would you propose?**

Please see response to Q9 above. Strict guidelines, properly communicated, plus an appeals process, affordable, and, therefore assessable by all regulated entities is paramount in applying a fair and equitable approach.

It is advisable that regulated entities know at what point authorisation will be revoked. Revoking authorisation clearly creates its own complications – the degree obviously dependent on the category in which the regulated entity is categorised under PRISM. One must weigh up the implications of non payment of levies and whether revoking an authorisation is too punitive a step impacting on the financial system, economy or consumers.

**11. Do you agree with the Central Bank's proposal to remit 100 per cent of the value of monetary penalties to the Exchequer? If not, how would you propose to treat monetary penalties?**

We have no difficulty with this proposal. It would appear a fair and equitable approach.

We again thank the Central Bank for the opportunity to part-take in the consultation process and are happy to elaborate on any matters raised in our Response. As always, we are happy to meet with the Central Bank and/or the Registry of Credit Unions to communicate further on any issues, in particular those affecting credit unions.



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