To Registry of Credit Unions

Submission “Introduction of a Tiered Regulatory Approach for Credit Unions.”
from Henry Bauress, 58 River Forest View, Leixlip, County Kildare.

In my submission to the Commission on Credit Unions (see appendix for full report), I summarised my views as follows:

1. Any new legislation/changes should make sure that key aspects of the credit union movement, particularly its local network, are not destroyed. A series of mergers will destroy that.

2. Ireland should look to other European Union models where co-operative banks have second and third tiers, such as Germany and France. It should set up a second tier – a bank, run and owned by the credit union movement, but staffed with specialist expertise, which would provide competition for private retail banks and an alternative co-operative type bank/investment advisory service for credit union members.

3. This second tier could provide, not only banking services such as current accounts, ATMs, credit cards, debit cards etc – all the types of services which merged credit unions might like to provide to their members. It would also enable the provision of mortgages, pension fund and investment services for both individuals and basic credit unions.

4. The move would enable the credit unions to gain economies of scale and scope without sacrificing the local credit union or regulating it out of existence.

5. The local credit union’s should continue to operate as currently, possible with lower than current limits on maximum loans. They could concentrate on the non secured personal small loan sector and pass on the larger more complex lending to their second tier bank. Current credit union offices could provide services for the second tier bank, if required, as well as financial inclusion/social welfare services. Regulation need not be so strict and the regulator could focus main attention on the second tier bank.

6. There should be a single public credit register, similar to the Irish Credit Bureau, for the credit union movement.

7. New legislation should require accounts/call reports of all credit unions to be publicly available.

8. The CU movement needs a dedicated research centre. It could be named after pioneer, Nora

Herlihy.
(See full report in appendix).

INTRODUCTION to submission on Consultation Paper CP 76

Since the Commission work, the new 2012 Act and other legislation, has been put in place.
My initial concern was that we will end up with an overly complex (and more expensive) credit union movement, where many credit unions have an average loan size of E3,000. I am still fearful of that and do not believe increasing mergers are the long term answer. I understand there have been over 50 of them. Mergers leading to larger credit union could create excessive complexity for those who wish to have available a low level lending model. If it bring them into Category 2 based only on asset size, rather than complexity of lending, damage will be done.

The less complication possible, with mainstream community credit unions sticking, for the most part, to low level non mortgage personal lending, remains the best option. They can handle small business and community loans.
To maintain this model, the credit union will most likely have to shrink, staff wise, have lower opening hours etc. if lower lending and much lower investment returns become the norm.

MAIN POINTS

4.8 Do you agree with the proposed tiered regulatory approach for credit unions?
A: No, it would be better to have no tiers. Get credit unions to apply individually to the Regulator on changes it wishes to make. One size does not always fit all. The savings or loans per member may be more relevant than the total asset size of a credit union, not including the number of members its serves. A large asset credit union (due to mergers) may just want to run a simple low level loan model, as I do.
As I said in my submission to the Commission, I favour a simple easy to manage loan/savings institution with a single second tier bank to deal with mortgage, pension and other services, in which economies of scale will be necessary to compete in the financial services markets.
I believe the levies now being charged by the Regulator, allied with the requirement to appoint Internal Auditors, should be sufficient to pay for regulation of credit unions.

5.12: Proposals for the operation of the two category approach.

A: Subject to my view on tiering, I believe the proposals here are, for the most part, no difficulty. On the subject of investment, however, (5.1.2), small credit union currently invest non loan money in a very restricted way, for either risk or maturity matching reasons. Most have an investment advisor. My idea for a single co-operative bank for the movement included making provision for money to be invested in it, and hence managed more expertly by specialists, as far as possible. I see it is proposed to enable Category 2 credit unions to invest in senior unsecured

bank bonds and corporate bond. I don’t see why. If they are unsuitable for a well advised smaller union, are they not unsuitable for a Category 2 union.
The idea of relating lending to reserves is a good one. But I think a single co-operative bank would be in a much better position to deal with business/mortgage type lending/PRSAs some want.
Concern about insufficient return on investments and lower lending should lead small credit unions to restrict what they will take in savings. This should lead to a lowering of costs in risk management. Investment surplus to the small credit union requirement can be directed elsewhere.

5.12 (ii) Regarding additional services, I believe that, at minimum, each service provided should recover its costs. Many new services require expensive IT and other investments, such as training, which are very costly and would be best undertaken by other institutions with higher economies of scale. Many services are provided by others on an agency basis and are not under the control of the small credit union. Some of these services are proposed to be provided by joint service companies. If so the companies should carry the cost of risk management/compliance, not the credit union.

6.3 Regarding Provisioning framework, there should be no framework other than what is in the Acts. Keep the guidance simple. Let the Regulator a issue guidance for the “provisioning policy.” A large part of the provisioning policy should be confined to loans which might properly be made by a larger institution or bank.
I would also like to see frameworks based on research across the credit unions. We are very poorly served when it comes to research. Is anybody monitoring the effect of credit union mergers, for example? Are they efficient? Can a credit union member see the results?

7.2 (i) Re timing, I do not favour tiering. If tiering has to be introduced, much more time/research is needed to decide on efficient tiers. There is enough supervision for the moment. Tiering could push the movement down a road it may not want to go and force credit unions out of communities because of high compliance costs.

7.2 (ii) see above

End of Submission on CP 76

(See APPENDIX below full submission to Commission)

APPENDIX

SUBMISSION TO COMMISSION ON CREDIT UNIONS

Henry Bauress*

58 River Forest View, Leixlip, Co. Kildare
Home Tel: 01-6245732
Mobile Tel: 086-8547558
E-Mail: hbauress@gmail.com

SUMMARY OF KEY POINTS

1. Any new legislation/changes should make sure that key aspects of the credit union movement, particularly its local network, are not destroyed. A series of mergers will destroy that.

1. Ireland should look to other European Union models where co-operative banks have second and third tiers, such as Germany and France. It should set up a second tier – a bank, run and owned by the credit union movement, but staffed with specialist expertise, which would provide competition for private retail banks and an alternative co-operative

type bank/investment advisory service for credit union members.

1. This second tier could provide, not only banking services such as current accounts, ATMs, credit cards, debit cards etc – all the types of services which merged credit unions might like to provide to their members. It would also enable the provision of mortgages, pension fund and investment services for both individuals and basic credit unions.

1. The move would enable the credit unions to gain economies of scale and scope without sacrificing the local credit union or regulating it out of existence.

1. The local credit union's should continue to operate as currently, possible with lower than current limits on maximum loans. They could concentrate on the non secured personal small loan sector and pass on the larger more complex lending to their second tier bank. Current credit union offices could provide services for the second tier bank, if required, as well as financial inclusion/social welfare services. Regulation need not be so strict and the regulator could focus main attention on the second tier bank.

1. There should be a single public credit register, similar to the Irish Credit Bureau, for the credit union movement.

1. New legislation should require accounts/call reports of all credit unions to be publicly available.

1. The CU movement needs a dedicated research centre. It could be named after pioneer, Nora Herlihy.

INTRODUCTION

The credit union movement in Ireland has come to yet another cross roads. While some of the issues for it have been bubbling away for years, obscured by the economic boom, the Government appointed Commission, chaired by Professor Donal McKillop, has a relatively short time span to come with new proposals for the future of the not for profit credit union movement in this country.
Set up here in the late 1950's, following the hard work of dedicated unpaid volunteers, like Nora Herlihy, who witnessed extreme poverty and lack of access to basic and cheap loans, they served around 65% or more of the population in 2006 (3), the highest proportion of any population in the world.
The movement has evolved from a largely volunteer one to where it is directed and controlled by voluntary boards but, for the most part, managed on a daily basis by paid staff.
This model has served us very well despite some difficulties.
The movement remains essentially solvent (7) but some made bad lending decisions during the boom years, under pressure to grow within a structure not geared for that as well as surplus

cash said to be demanding higher returns to members.
Nobody could say that credit unions are perfect but critics the complainants do not explain how the "experts" who ran Anglo Irish Bank and other great institution managed to fail so spectacularly, and not only at their own expense, in these profit maximising institutions. There are many wider issues in lending but the current credit union movement should be ring fenced to some extent, while not cutting its members off from essential services.

PRODUCT GROWTH NOT ANSWER

The major problem, as I see it, with the debate over credit unions, is that many of the suggested changes aimed at fixing its apparent problems do not bring the advantages they are claimed to bring.
One key problem underlying both cooperative and private banking has been too much surplus cash chasing too few lending opportunities which will bring a decent relatively risk free return on money. I would go further and say that the credit union movement should plan for a situation where, world wide, demand for goods and services of all kinds outstrip supply, where our income and resources are relatively lower than they have been over the last twenty years.
Before the collapse of the Irish economy, some had been questioning credit union movement viability.

Ironically, it remains much more viable now, than large banks which should have benefited from economies of scale, including their knowledge bases and economic expertise, to know what was happening in both the national, European and worldwide economy.
But even if some bankers warned of problems, the pressure of maintaining share prices/dividends pushed the banks into high risk or beyond their knowledge comfort zone.
Some of the larger credit unions appear to have caught the high growth/high risk disease, despite not having stock market pressures. It may be that empire building by increasingly highly paid management of some of these credit unions won out over the good sense of other voluntary directors.
Credit unions should, ran the argument, diversify away from earning money from interest alone, going into "services" and "financial products."
But studies done by the Journal of Banking and Finance (JBF) and others, including one on US credit unions (1) co-authored the chairperson of the Commission, Prof. Donal McKillop, suggest that such new avenues of business have not been able to replace the basic loan business lost

due to the increasingly competitive environment following the deregulation of financial services industry.
It was found that in some cases that profits fell as banks diversified.
In Australian credit unions, the move into “fee income” led to more risk.
Major retail banks, which have the large economies of scale not available to the credit union movement, are moving away from the more exotic products back to more basic banking. The pressure of market forces has led to many banks, effectively taking excessive risks or charging high prices on products where they had market power.
The selling of these products and the pressure to perform led many people buying inappropriate products, without proper scrutiny.
Some credit unions will know this in relation to their investment advice.

CREDIT UNIONS LESS RISKY ON AGGREGATE

The last fifteen years has seen credit unions apparently come under pressure, like other bodies, to find homes for increasing quantities of cash. They may have unwittingly attracted tax evading cash into the bargain.
Despite statistics indicating a decreasing level of savings, particularly among younger members, credit unions appear to have been pushed to either loan out more money than was wise in an attempt to make get a return on their member's money, or get attracted into areas of investment which they might have been better to avoid.
The nature and legal structure of credit unions, along with the good sense and wisdom of many in the movement, has led to a situation where credit unions are much more solvent than the major banks, whose expertise in managing risk was said to much greater.
The nature of the credit union model, even in the United States, where many provide retail banking services such as current accounts in addition to the basic loan and saving services, appears to be less risky, when measured by bad debt criteria.
One study of US credit unions in 1986-2000 period (4) concluded that their legal structure led to credit unions having less risky portfolios leaving them better able to absorb economic shocks, such as recessions. The study found, for example, that commercial loans comprised just 2% of the US credit union loan portfolio.
It compared bad debt with unemployment figures across states and found a 1% increase in the employment rate was correlated with a 23.7% increase in bank delinquencies but a 10% rise in credit union delinquencies.
Write off’s rose 30.8% in banks but 19% in credit unions.
A key conclusion/argument of the paper was that credit unions need have lower reserve or

reserve ratios to cover bad debts, because of their less risky business.
Is it the case now that increased regulation, particularly the requirement to have higher reserves to cover potential bad debt losses, could make solid credit unions so uncompetitive that they will be forced out of business or into merged bodies, perhaps leaving rich pickings for new leaner private retail banks, the home credit/legal money lending industry or the illegal loan shark waters. Like bad debts, reserves, however necessary, are a form of cost.
I am not suggesting there should not be concern over debt, far from it – it has to be reduced and the 2006 average write off of E508,100 (3) was far too high - but some has to be expected in a serious recession. However, a sledge hammer should not be used to crack a nut to use the proverb.

MERGERS

On the question of mergers few commentators have spelled out the likely effect or disadvantages of these on the institutions involved.
A key question is the purpose of the merger and I would suggest that very strict cost/benefit analysis of any merger proposed should be made.
In the USA, most credit union mergers involved very small credit unions and consolidation was spurred by consumer's increased financial sophistication, said one report (5).
The study said that the growing regulatory burden and the rising cost of compliance forced many smaller credit unions to seek out merger partners.
In the US, where around 35% of the population is a member of a credit union, the merger trend helped double the median (or average) credit union size from $2.8 m in 1990 to $5.7m in 1997. In the 1990's, the greatest reduction occurred among credit unions with less than $500,000 in

assets with 52.8% of them either merging, liquidating or failing between 1992-1998. Most of the 2,841 mergers from 1990-1996, were voluntary according to the National Credit Union Administration.

Before 1982, it said, most mergers were due to poor asset quality, inadequate reserves or profitability, or the retirement of a chief executive without a successor.

Some may have been linked to disappearing companies.

But as credit unions returned to prosperity in the 1990's the trend declined but those mergers which did take place were driven by different motivations. These included "specific business objectives." Few had financial problems which forced them to consolidate.

It said credit unions were merging to reach the critical mass needed to invest in technology, centralise certain functions and integrate new product delivery systems, achieve maximum efficiencies and enhance services.

By 1998, many viewed mergers, "not as a strategy to survive, but to do better."

But another study (2) on USA credit union mergers suggested the key reason for them was that regulator/insurance fund wanted solvent ones to take over those with bad debt problems.

It found that the acquiring – usually larger or dominant - credit union gained little or nothing from the consolidation but both the target or problematic institution and the regulator did gain. It is understandable that the regulator would want fewer institutions which need overseeing but it should not be the only or major reason for a merger.

It said that while for most credit unions growth is desirable, “since there *appear* to be economies of scale,” (my italics) the motivation for merger in credit unions is “not fully established.”

One study commissioned by the US credit union interests (6) found that at a certain level, the only small banks had potential for significant scale economies and efficiencies and these were around 5% of costs.

Credit unions here will find that the major difference in costs depends on the level of bad debt write offs. The same study said that consolidation “may increase or decrease efficiency in a number of different ways.”

The key characteristics of target banks were relative inefficiencies, high level of non performing loans and low capital ratios.

The study also pointed out that consolidation or merges increased profit or surplus in two main ways. One was by increasing efficiency at operational level including the reduction of bad debt. But the other was that increased size gave the merged institution market power to raise prices – interest rate above necessary due to a decrease in competition.

This study (6) felt that the US movement should look to the multi-tier co-operative banking structures in Germany and France. It said it was not a matter of “grow or die” for the US movement but “merge or co-operate.”

I believe there are advantages to co-operation between credit unions – and to centralisation of some elements of our operations - but I would argue the way we achieve some of these aims, if desired, is critically important.

Blending back office operation can lead to problems of who pays for what and how to cost shared resources.

For instance, the movement should be co-operating on the creation of a credit union credit register to help avoid some members running up multiple bad debts in different credit unions. A

cultural aversion to information sharing in Ireland has made us vulnerable on this front.
The economics of mergers are far from straight forward.
We run a big risk of losing the basic credit unions by creating a patchwork quilt of larger institutions. I believe a halfway house approach will eventually lead to the destruction of the ethos of credit unions, but, at the same time, not achieve the economic advantages we want to create from the mergers.
It has been said that retail banks have, at times, found the business of running current accounts, ATM's etc not very profitable at times.
Market pressures and cost cutting led them away from more personal services, which, it should be said, have a cost, for which someone, somewhere has to pay.
As a result, even with economies of scale much greater than common bond constrained credit unions; they felt pushed or pulled towards high risk business to feed to hunger for profit. I would not put everything down to "greed" as some would argue. The market pressures were there from shareholders but they would have probably been there in some form without the disadvantages of public companies. Credit union with falling loan to asset ratios took more risk they ought to have done, to get money out. Even today, there are those calling for someone, anyone, to start lending again to "get things going;" without any idea of what projects/wager earners will be able to pay the money back. Confidence has to be based on reality, however, unpalatable.
No business, private, public or cooperative will survive if the basic ground conditions are not right.
There is a serious danger that a less than cohesive credit union movement, trying to provide a wider banking service, will not achieve the necessary economies of scale and scope and crash.
To crack an extra unwanted nut, the sledgehammer could break the movement apart.
One answer to a low loan/asset ratio in the average credit union is not to give out more increasingly risky loans, but to hand deposits/shares back to members to find other outlets in which to invest.

MULTIPLE MARKETS

Retail banking, done on the scale of the Bank of Ireland and Allied Irish Banks, is not just concerned with one or two types of markets, say loan and deposits, but a large number of markets. Outside service providers have control over the costs of many of these market products, including IT costs, which are sometimes cited as a possible reason for mergers.
Most of these, payment cards fees structures, interchange fees, investments, pensions etc (9) will be best dealt with through a larger cohesive organisation.
There have been calls for credit unions/An Post's network/government to provide basic banking services. Why? Are they not profitable enough to the larger private banks, many of them now international? The credit union should take care. There is a cost to everything and the price might be too high to increasingly poorer members. Apart from anything else, as the population ages we will be less appealing to profit seeking banks.

Some see the provision of a basic access to the financial system not just as a product choice but as a basic human right. That argument has merit.
But it should not be achieved at the expense of the credit union movement without the taxpayer helping to create a level playing field.
The State, if it deems financial rights essential or desirable, must be prepared to provide a level playing field, and subsidise potentially loss making financial product services, current accounts/smart cards etc so that the credit union movement will not be competitively disadvantaged relative to the profit maximising private banks, who, despite the knowledge based provide by movements on current accounts, could decide to opt out of that particular product markets.

LOSS OF CONTROL

The problem with mergers and centralisation is that control will increasingly and speedily disappear at local credit union level with full integration.
Some argue that the main banks lost out when they transferred control away from the local manager and his/her deep local knowledge.
Without sufficient care on behalf of the Oireachtas, the ILCU and CUDA leaderships, the movement will evolve into just another private bank, perhaps pushed by the private markets, who would like to get their hands on much current relatively solid loan books.
Ireland is a small country with low density population.
If mergers/privatisation of credit unions is allowed, no sooner will one merger go ahead, than a further one will be deemed necessary. One possible scenario is that members, perhaps some desperate to sell off what little remains of their proverbial family silver, will be weakened in their resolve to block legislation enabling credit unions to privatise.
If a new law permitted, they may eventually vote to "sell" shares in their own credit union. Faults it may have, but the Oireachtas, elected by the people, and the law of the land it has created, did well with credit union legislation.

In the longer run, mergers and privatisation may leave the citizens of Ireland at the mercy of international markets, effectively looking into the begging bowls of foreign owned banks, who, like any private company, Irish or non Irish, could shut down their Irish operations, not just because they were loss making, but if they were less profitable than elsewhere.
With the collapse of the private profit maximising banking system in Ireland, now supported by the State/EU/IMF, some have suggested that the credit unions could enter the mainstream retail banking market and provide some form of “third pillar.”

SECOND TIER CO-OPERATIVE

But how could a “third pillar” avoid the pitfalls experienced by the mainstream banks here? There may be a way of doing this without obliterating the movement and, at the same time, embracing competition.

It may be possible to have an efficient “third pillar” which would give us access to services and economies of scale and scope, more of which we may soon need.

This move would enable us to keep the strength and independence of our current structures, merge some functions if we need to - and only if we need to – and, at the same time, achieve the economies of scale and scope associated with bigger institutions.

During my terms as a director of Leixlip & District Credit Union (1997-2006), I suggested to a regulatory official that the credit union movement investigate the creation of a second tier bank, controlled co-operatively and run by the movement on a non- profit basis.

My idea was that it could, given the strict guidelines/legal structure provide more services than loans, particularly to those financially excluded from current markets.

It was suggested to me, instead, that we could merge, for example, into the EBS Building Society. We now know, of course, that many of the mutual institutions, who shared structural similarities with credit unions, were damaged beyond repair with poor property related lending. Like everyone else, they overestimated the economic demand for property.

It is likely – though I am not aware of any study – that the main credit union debts are property related.

Subject to competition and legislation, the Oireachtas should enable the movement to create a second tier bank, which would operate like any private bank in most respects, but allow it to balance the market interest rates with the particular circumstances of the members at any point in time. It would be legally ring fenced from its owners, the current credit unions and have different regulatory standards.

We do not know what the banking markets will look like in the future, possibly even the short term future. Will banks go by the way of aviation where it is predicted mergers will leave that industry with just four companies in a few years time?

Even if we leave the European Union, in whole or part, we may be at the mercies of the banking markets. A home grown home owned banking system will be an advantage with further concentration of banks.

Key questions need to be asked about the direction of banking. In summary, some would like to see a cashless society with everyone possessing a personal pin number which gives access to all we possess. There are advantages, of course, but the risks are high due to possible loss of control, wars, private greed etc.

Even today, it is costly to maintain home internet services which enable one to conduct many financial transactions. What will happen to those who cannot afford them? A future credit union

movement may need to provide access to terminals if it wants the potentially financially excluded to have access to services.

EUROPEAN MODEL

It may well be that the existence of European co-operative banks will explain the relative better performance of banking in some countries compared to Ireland? I am offering no evidence either way on that?
A study of advantages and disadvantages of many European co-operative banking structures would be instructive.
Germany has a three tier system and the average size of a credit union was
$235 million, according to a US credit union report (6) which urged the movement there to look at the French and German model.
I strongly believe we can run a second tier, with a little bit of advice from our European Union friends who continue to run large co-operative banks.
This could give our members more choice in banking services, provide good unbiased financial advice on things like pensions on a non profit basis, and, importantly, provide economies of scale for the movement.
But it would also enable us to maintain our local network which could rent out space and contract local staff for a second tier bank.
These economies of scale probably cannot be achieved easily by our current structure which would in effect be entirely dismantled over time.
It has been noted that where co-operative non profit institutions grow, such as Credit Agricole, they tend to be cooperative in all but name and act like profit maximising institutions.
I believe that the framing of legislation leading to a second tier co-operative bank would have to be done with care so as to give flexibility to responsible experts to run it but avoid the owners – the credit unions – losing control.

INFORMATION

I have specific concern over education/information.
Apart from my work as a credit union director, I did a mini thesis on co-operative banking principles for a master’s degree at NUI Maynooth.
One option for me was to try and compare write offs with unemployment figures as was done in one US report (4). I approached ILCU it said the figures required were not available.
Despite the constantly stated mission to educate its members over the years, the credit union movement has, I would argue, failed miserably.
As stated earlier, there is a culture of secrecy here, and members and the Irish public have

accepted poor flows information from those in authority, even quite a well regarded authority as the ILCU leadership.
Individual credit unions and ILCU publish very little information or data other than brief marketing information on their websites or to their members. Annual reports are presented to members but not available to the wider public, including potential members in their common bond areas.
Contrast this with US credit unions, where detailed statistics – information of a non personal nature of course – is provided on the National Credit Union Administration website. I was able to select a credit union, in this case, Edwards in California, and find out how many loans it gave to senior officials and the total amount of loans in question over a period this year.
These figures, along with other aspects of call report information, were provided.
New legislation should require all credit unions in this country to supply, not only to their members, but to the general public, on websites, their full annual reports, all their Call Reports, quarterly and annual PEARLS reports, indeed any reports (of a non personal nature) which are required by credit union boards, credit union associations, regulators etc. A voluntary code will not work. The Oireachtas should require that all these reports are made available. IFSRA could be mandated to provide them in Excel or any other appropriate format to aid trained researches. I see from one of the papers, I have cited in this submission (3) that Prof. McKillop and his colleagues could not get data on some credit unions because they had not filed returns and as a result used data from only 388 of the 424 credit unions registered in Ireland in 2006.
It is disappointing to see that despite the huge influence of credit unions in Ireland there is so little academic research on the Irish movement.
Bodies like the Central Bank or the ESRI have very little academic work done on credit unions, given their social and economic importance.
Despite the efforts of Prof. McKillop and his colleagues, there is a serious danger that the movement could be forced down the wrong road.
It is deeply ironic that this is so. Ireland's most famous greatest credit union pioneer, the late Nora Herlihy, made research a very high priority in getting the credit union campaigning (14).

COMMISSION QUESTIONS

Hopefully, I have covered most of the key concerns I have. I will now briefly comment on some specific questions raised by the Commission.

(i) re support to local community, keep current CU's/common bonds, create second tier bank for investment/pension/current account/banking. New legislation, could, as it does in the UK and USA, require larger private banks to provide services in areas not regarded as financially viable, usually poor areas where bad debts are high.
The UK credit unions tend to look more towards the socially excluded but there is no easy way to lend to those with little money. The Commission might like to look at the UK Competition Commission's 2006 Home Credit Market investigation (10) to see some of the issues raised.
The current credit union view that it is for service not for charity remains a good one. Society

must transfer resources to those who need them not loans. On the wider question of interest rates and their role, we may, in the longer term like to look at other cultural approaches (11). Judging by history (12) we may not be able to rely on standard credit union interest rates to which we have been accustomed since the inception of the movement – in the 9-12% band.
(ii) changes to the credit union operating model should be made but as explained above, the current local common bond system should co-exist with a second tier which could capture economies of scale/scope and internalise the numerous different product markets coming under the umbrella of "banking."
(iii) consolidation/ restructuring via a second tier bank, owned and board directed by the movement – incorporating the possibility of referenda by all members of the movement in certain circumstances.
(iv) IT/MIS is a complex business.
On the question of management information, I believe that the basic systems work quite well and give anyone who wants to know more about their credit union. The PEARLS/CAMEL systems have worked well.
The big problem lies in the cost/access to information on borrowers.
Despite increasingly larger loans in recent years, the movement not got fully to grips with the idea that the early "peer" knowledge of the borrowers by his/her neighbour running the local credit unions, has, while still very relevant, diluted somewhat.
Credit unions have been vulnerable to fraud by those exploiting the fact there is no central credit reporting register system for the movement as a whole. In reality this will needs to be tied into other systems. A public register for all financial institutions would address this particular issue somewhat. There are (13) are crucial wider issues, including economies of scale and competitive issues in this market well.
IT systems are not unrelated to MIS but remain separate. Many credit unions feel their IT systems are very costly, particularly the maintenance ones.
There ought to be economies of scale in the purchase of systems but the IT sector has had a lot of market power because of lack of knowledge of costs on the part of purchasers. Many State IT projects have been costly failures.

(v) It is of course possible to share services on a formal basis.
Subject to other methods not working, credit unions who do wish to merge/provide a wider range of financial services, could contract out expertise on a shared basis.
Three or four medium sized credit unions, might like to hire an independent financial advisor who could make appointment with members. They might like to share a budget or bill paying services, if that was deemed viable. I should say that any services should be provided on an economic basis in that they should, for the most part, pay for themselves.
Any other services, cheques, current accounts etc would need wider co-operation to capture economies of scale.
Efforts by ILCU to organise a central system for member credit unions some years ago went wrong.
IT is one reason why a second tier credit union bank, with separate but easily linkable technology, might be a good idea.

Ultimately, if IT becomes too costly, we can go back to paper and pencil. We should not forget that, even if it is distasteful to us.
The Commission and the Oireachtas, should tread carefully, but not indecisively.
We should not let a structure which has served us well for over 50 years be thrown out because some have made bad lending decisions. While those who are in financial trouble are sometimes significantly so, most citizens manage their finances well.
(vi) governance standards are not poor in Irish credit union and 90% of them were in surplus in 2009, according to then ILCU President, Mark Bailey. It is possible to pile too many standards on any institution, bank or credit union, which, and still miss the key goal for most, to cut bad debts while serving members. The key to governance, in the longer run, will be found in lending the optimal amount of money which can be paid back. Credit scoring will become more important, in this regard. The Oireachtas may be better in some instances to enable the regulator to instruct certain limits to be maintained rather than "encourage" them to be retained. That does not have to reduce flexibility to nothing.
The problem for everyone is to assess the correct type of demand for all types of good, the creation and purchase of which, is part dependent on lending.
One report (15) quotes an IMF paper which concluded that the burden of mortgage debt restructuring had to be shared by the taxpayer.
(vi)Credit unions should get more involved in financial inclusion and micro lending but only on a cost efficient basis. We will be a poorer country in the future, most likely. Credit unions, with appropriate aid from the State, can provide, with expert advice, possibly via the second tier bank proposed above, financial management services, helping to smooth out each individual lifetime income needs and creation. They may have to provide technology for their members, if poorer people, on both a long and short term basis, are excluded from banking by high IT costs, such as PC or broadband services. The movement has been criticized in the past for not concentrating sufficiently on those financially excluded. Would an enhanced MABS service operate in conjunction with them? Could space be shared? Could the local CU office become a single location for a range of services, from social welfare payment, free legal aid centres, in a coherent and efficient manner? I believe they could, in some cases. I also think, however, one can only go so far in helping the financially challenged by way of loan or payment services. Ultimately some will need help from the Government/taxpayer.

(vii) I will not comment on the Credit Union Acts because of the very specific nature of the various parts. If the Oireachtas is proposing changes or has been lobbied to make it, there should be some economic based cost/benefit assessment of the changes and their likely effects. Too much Oireachtas legislation has been created on the basis of general principles or economic theory which is not backed up well by empirical research or real world experience.

NOTES:

(1) The Diversification and financial performance of US Credit Unions (Goddard, McKillop, Wilson)(2008)(Journal of Banking and Finance)
(2) The Effect of Mergers on Credit Union Performance (Bauer, Miles, Nishikawa)(2009) (Journal of Banking and Finance)
(3) Irish Credit Unions: Investigating performance determinants and the opportunity cost of regulatory compliance (Glass, McKillop, Rasaratnam)(2010)(Journal of Banking and Finance).
(4) Differences in Bank and Credit Union Capital Needs (Smith,Woodbury)(Centre for Credit Union Research, University of Wisconsin-Madison School of Business/Filene Research Institute)
(5) Credit Union Restructuring: A Response to the Developments in the International Finance Industry (World Council of Credit Unions Research Monograph Series No. 11, 27 February 1998).
(6) Consolidation of the Financial Services Industry: Implications for Credit Unions (Centre for Credit Union Research, University of Wisconsin-Madison School of Business/Filene Research Institute).
(7) As recently as March 2011, the Irish League of Credit Unions PEARLS indicators found the movement was solvent (116.2%), had reserves (13.5%) and sufficient liquidity (35.5%). Arrears (17.2%) were not low but could be managed.
(8)My name is Henry Bauress and this submission is made in a personal capacity.
I am a journalist since 1977, working for the Dungarvan Observer until 1980 and from then for the Naas based, Leinster Leader newspaper.
I have a Certificate in Journalism from the School of Journalism, Rathmines (1975-77), a B.Sc Economics degree from University of London (1993), a MSc. Economics (Competition and Regulation) from NUI Maynooth in the mid 2000's. In also took an econometric module from the

University of London's MSc programme in the 2000's.
I served on the board of Leixlip & District Credit Union from around 1997-2006.
(9) Report on the retail banking sector inquiry: European Commission Staff Working Document, Directorate-General for Competition (SEC (2007) 106 (31 January 2007)
(10) Home Credit Market Investigation (Competition Commission 30 November 2006). It contains a section on the Republic of Ireland (Appendix 3.3). The contents of this report should be well known to credit union directors/managers. The investigation suggests that the presence of credit unions has led to lower interest rates being charged by the home lenders in Ireland. It also said there is an overlap in Ireland between credit unions and these companies, stating that 42% of Provident customers in Ireland were saving with a credit union. Many of these private house lenders charge interest rates over a 100%. One reason is the cost to a company sending a representative door to door to collect installments and loan money. The other is that anyone who feels badly in need of a loan will not be too particular about the interest rate. Ultimately those living in poverty need transfers from the rest of society, rather than loans.
(11) Issues in Islamic Banking: Selected Papers, Muhammad Nejatullah Siddiqi (The Islamic Foundation UK 1994.
(12) A History of Interest Rates (4th Ed), Sidney Homer/Richard Sylla (Wiley Finance).
They say that since modern capital markets came into existence, long term interest rates have never been so high. Recent peak yields were far above the highest long term price rates reported in the USA since 1800, in England since 1700 or in Holland since 1600.
They show that interest was paid in many forms, not just money as we know it, and is related to slavery. A far thinking credit union movement might look at how it could formally enable a barter economy and cater for those who need pawn broking services.
They tell how around 1800 bc Hammurabi, a king of Babylonia, set a maximum 33% annual interest rate for loans of grain, repayable in kind. All loans had to be accompanied by written contracts witnessed before officials. If a higher than legal interest rate was collected by subterfuge, the principal of the debt was captured. By contrast the laws of Solon, in classical Greece 600BC, created followed economic crisis, limits on interest rates were abolished. But they reduced or cancelled many debts and forbade personal slavery for debt.
(13) The Economics of Consumer Credit (ed. Bertola, Disney, Grant (MIT Press) :
A very useful book with chapters on a variety of topics, including debt, credit cards, bankruptcy, credit counseling and credit information sharing. For example, in one paper, Jappelli and Pagano say that for private credit bureaus, lenders should have a greater incentive to share information when the mobility of credit seekers is high.
My view is that the more risk a borrower want to take with other people’s money, they more they should be willing to be monitored. Ultimately all lenders should be able to dip into a database to see the record of those who default. We could enable these databases to be enhanced to allow lenders see whether the default did so because they could not pay or would not pay. The difference is crucial.
To those who oppose such a move, I would say that ultimately private banks are collecting this type of information anyway. Mergers will provide them with the databases/information to separate the good from the bad. Banking is becoming more concentrated.
It is also a fact that banks which have good information will have a competitive advantage over

those who do not.
At the moment the credit union is already at a disadvantage on this front.
This is why Europe wide public credit registers are important. In an open world economy, it will be increasingly important to be able to access such registers anywhere. I have argued in the past that we could be lending to young people from our communities to emigrate to the USA or Australia. There are advantages to that from the point of view of communities where they live but good borrowers would be able to take advantage of good records and pay back their Irish credit union from abroad. That may be done, directly or indirectly, but ultimately the lender must be protected against reckless borrowing by access to appropriate databases.
It should be pointed out, that while some registers may record only bad debt information others use all types of information about a borrower, giving credit scores based on income, overdrafts, timing of payments as well as default information.
Around 95% of the information held about on lenders is positive in that it is not related to defaults but concerns the movements in and out of their accounts. It enables banks to build a financial profile of individual borrowers which will enable them to avoid those likely to default (and send them down to the local credit union).
Credit unions have not got access to this information and it may explain some of their poorer lending decisions. That is why, a second tier bank, could be useful, giving members an alternative to the private banks.
The reality is that probably 85% or more of all borrowers try their best to pay back and co-operate.
(14) Culloty A.T. “Nora Herlihy – Irish Credit Union Pioneer.” Irish League of Credit Unions.
(15) The IMF report (Foreclosure Mitigation Efforts in the United States: Approaches and Challenges, 18 February 2009) is copied into the Houses of the Oireachtas Joint Committee on Social & Family Affairs – Second Report – High Levels of Indebtedness in Irish Society (February 2010).