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Registry of Credit Unions
Central Bank of Ireland
PO Box 559
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31st March, 2014

Dear Sirs,

Further to the publication of "CP76 - Consultation on the Introduction of a Tiered Regulatory Approach for Credit Unions" and your invitation to make submissions in relation to the Consultation Paper, outlined below are the observations and comments of the Board of Directors and General Manager of Rathfarnham & District Credit Union Limited (hereafter referred to as "RDCU")

RDCU fully supports the principle of a tiered regulatory approach with the sophistication of the regulatory regime at each tier being proportionate to the nature, scale and complexity of the business undertaken by the credit union. However CP76 goes much further than its remit of a proposed tiered regulatory approach for credit unions; it significantly changes the regulatory framework for all credit unions by proposing changes to the regulatory requirements across a range of key business areas which will adversely impact the credit union business model and put credit unions at a competitive disadvantage relative to other financial institutions competing for the same business.

Credit Unions have been the subject of a much strengthened regulatory framework from the second half of 2013. This framework facilitates CBI oversight and, when necessary, intervention in credit union business activities. This strengthened regulatory framework, which is currently being embedded in credit unions, will result in credit unions being put on a much sounder financial footing and be a catalyst for restructuring of the sector.

RDCU would urge the CBI to give the required time for the regulatory framework and regulatory requirements implemented in 2013 to be embedded in credit unions and assessed for fitness for purpose before proceeding with the significant changes in regulatory requirements outlined in CP76. This would not delay the implementation of a tiered regulatory approach for credit unions; rather tiered regulation would be introduced on the basis that the current regulatory requirements applicable to all credit unions would in future be applied to credit unions in Tier 2 of a 3 Tier system, credit unions in Tier 1 of the 3 Tier system would be subject to a simplified regulatory regime while credit unions in Tier 3 of the 3 Tier system would be subject to more stringent regulatory requirements.

In the remainder of this submission we have responded to the individual questions raised in CP76.

Question 1: Do you agree with the proposed tiered regulatory approach for credit unions? If you have other suggestions please provide them along with the supporting rationale.

Credit Unions operate in many environments (regional, urban, rural, and industrial). Within this they comprise Credit Unions with a wide range of asset sizes, business diversification, service offerings, governance, and risk profile. The Commission on Credit Unions sought to enable classification of credit unions into groups which reflected physical size, complexity of operations, and the attaching risk.

We believe that it makes sense that a tiering approach is applied in order to bring a level of uniformity to groupings which display roughly similar characteristics. With a cohort of 400-odd credit unions, it will always be difficult to neatly categorize each credit union, but groupings must be found. While we have reservations on the groupings proposed, as outlined later in this document, we do agree in principle with a tiered regulatory approach.

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Question 2: Do you agree with the proposals for the operation of the two category approach for credit unions set out in sections 5.1 - 5.11? If you have other suggestions, please provide them along with the supporting rationale. It should be noted that tiering is possible where regulation making powers are available to the Central Bank. Where requirements are set out in the 1997 Act they apply to all credit unions and cannot be tiered.

Proposal – 2-tier model.

The 3-tier categorisation of credit unions, as proposed in the report of the Commission on Credit Unions, which was based on asset size, while crude and simplistic in its criteria, substantially achieved what it set out to do. It correctly assumed that larger credit unions are more likely to engage in bigger transaction sizes and volumes, and as a result create potential for events which could negatively impact on themselves and/or the industry.

Assuming that indicators for 2011, as outlined in the Final Commission Report, still hold true, just over 50% of credit unions have asset sizes below €20m, and account for 15% of the movement's asset base. This suggests that the 3-tier classification proposed by the Commission should be amended to:

- tier 1 up to €20m assets,
- tier 2 €20m to €100m, and
- tier 3 over €100m .

The CBI proposal to cut the number of tiers to two creates an oversimplified categorisation, and one which offers simply a yes/no response to many questions while disregarding many of the softer features unique to individual credit unions.

The discussion document proposes that where a credit union operates a more limited business model, the regulatory framework will apply in a proportionate manner. Given the diversity of credit unions, we believe it is well-nigh impossible to document the specific circumstances when a credit union in category 1 would, or would not, qualify to be treated under the less rigorous regime.

We therefore disagree with the proposed 2-teir system, and believe that a 3-teir solution along the lines outlined above would give a more balanced categorisation.

5.2 – Lending

Lending limits generally

Lending is the lifeblood of credit unions, and equally one of the biggest risks to its existence. Lending risk is in part mitigated by limiting loan size, and by ensuring that over-concentration of lending to a particular sector does not arise.

In principle therefore, we do not have any issue with the limits envisaged for large exposures, connected borrowers, concentration limits insofar as they affect our credit union.

Restricted persons limits

There are already in place significant oversight and controls over borrowing by credit union officers and separately to connected borrowers. Due to the wide definition of family, the proposed limit of the higher of €200k or 5% of Regulatory Reserves will soon be exhausted.

In our own particular case, our loans to officers currently relate to 9 directors, 3 supervisors, 2 volunteers, and 12 staff. Assuming that borrowing by officers will increase as overall sectoral borrowing increases, and adding an amount for family and associates of each individual, we will very quickly breach our proposed limit of approximately €300,000 (based on our present regulatory reserves of €6.3m).

We believe that this limit is discriminatory towards credit union officers, their families, and associates, and is not mirrored anywhere else within the Irish Financial Services Sector. This proposal will disenfranchise many individuals from availing of credit union loans as much of the population of the republic of Ireland are not in a position to join a second credit union due to common bond restrictions.

We also believe that there is a high probability that, if challenged, such restrictions would be found to be unconstitutional.

5.3 – Investments

The proposed changes regarding investments significantly restrict the products in which credit unions can invest, compared to existing regulations. In particular, while not expressly stated, credit unions may no longer invest in Collective Investment Schemes or Equities, and the capability to invest in Bank and Corporate Bonds is abolished for category 1 credit unions and curtailed for category 2 credit unions.

The reduction in the concentration and counterparty limit will effectively force a large-scale withdrawal of funds from the so-called Irish Pillar Banks at a time when they are attempting to shore up their balance sheets. Instead credit unions are being forced to invest with institutions whose centre of vital interest is outside the jurisdiction. We believe that a significant increase in these limits would benefit the economy as a whole, and merits consideration.

The reduction in the maximum maturities, when coupled to liquidity proposals, will create issues for credit unions of all sizes and categories. There is a direct link between the term of an investment and the rate which can be earned. By forcing credit unions into shorter maturity periods, additional pressure will be placed on declining investment income levels. In addition, the ability of the management and board to manage their business is significantly hampered.

5.4 - Savings

The capping of member savings at €100,000 places an unfair restriction on the ability of credit unions to raise funds from members. While the bulk of credit union members would have savings well below this threshold, many credit unions would have individual savings above this level.

The government guarantee is set at €100,000 and imposes a decision on members whether they wish to retain savings in a particular financial institution in excess of this limit.

In addition, many Credit Unions have implemented a self-imposed savings limit, and we believe that individual credit unions are best placed to judge what is an appropriate savings level for them, and to manage it accordingly.

We believe that this proposal is flawed, and should not be implemented.

5.5 – Borrowings

In our opinion, this area is likely to have minimal impact on most credit unions, and we have no comment in this regard

5.6 – Additional Services

We have included our comments on this point within our response to Question 3.

5.7 – Governance

We agree in principle with the need for additional levels of governance as entity size and complexity increases. However, the proposals impose additional regulatory requirements and costs for category 2 credit unions which are disproportionate to the size and risk profile of most likely category 2 candidates. For example, the requirement to have dedicated risk, compliance and internal audit functions mitigates against credit unions who might previously have outsourced the functions, or have shared them with other credit unions.

On top of what can be regarded as very detailed and personally probing fitness and probity and other requirements, we believe that the requirement for a 3-yearly external review of the board of directors will further discourage volunteers from giving of their valuable time to the ongoing development of individual credit unions and the sector. Perhaps, permitting the payment of directors' fees, or equivalent, might in some way serve to attract suitably qualified and experienced individuals to become involved in such onerous requirements.

We note the proposed requirements for Audit, Risk, Remuneration and Asset/Liability committees, and believe that they are necessary in any organisation of significant size.

5.8 – Fitness & Probity

This has been in operation since August 2013, and we have no further comment to make at this time.

5.9 – Reserves

At present, the basic reserves requirement is 10%, comprised of Statutory and Additional Regulatory Reserves. Many credit unions are well in excess of this requirement, and we believe that all are striving to reach a figure closer to 15%.

Credit Unions are in essence simple organisations, without elaborate product offerings, and with known areas of potential risk. Creating a new regulatory framework to facilitate the assignment of risk weights to individual CU activities seems to be an over emphasis on methodology, without a corresponding emphasis on desired result.

Following the extensive inspections carried out by Central Bank personnel, external consultants, and the ongoing efforts of external and (latterly) internal auditors, risk officers and compliance officers, one must deduce that the CBI have almost certainly homed in on the risk areas and riskier organisations within the movement, and engaged with them in an appropriate manner.

The CBI's own objective is to apply a level of regulation, governance, and oversight which is appropriate to the nature, scale and complexity of the organisation. We believe that if this objective were to be followed, there would not be a perceived need to implement further complexity into the regulation of the credit union movement.

5.10 – Liquidity

As previously outlined, the proposed combination of reduced investment maturities and the proposed liquidity requirements for 7 and 30 days further pushes investment pools into the shorter end of the market where low returns are the norm.

In a healthy investment portfolio there are ongoing maturities, with individual investments gravitating towards the 0-90 day segment before being reinvested for longer periods. This together with the existing liquidity requirements ensure that credit unions manage their affairs to ensure a stable organisation, which operates within guidance.

Proposals for liquidity such as those included in the discussion document are simply an attempt to micromanage individual organisations rather than create a regulatory environment where credit unions can operate, grow and prosper.

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Question 3. Are there any areas where credit unions could provide new additional products or services to their members? Should these be available to category 1 and category 2 credit unions or only category 2 credit unions? If you have suggestions please provide them along with the supporting rationale and the associated additional requirements.

In recent years, the onset of the recession has severely curtailed individual spending, and in turn created reduced appetite for borrowing. All economic indicators and forecasts point towards a more positive attitude to spending and borrowing in the months to come. It is therefore necessary that when the time comes that credit unions having weathered the recessionary storms, are capable of taking advantage of the economic upswing as soon as it appears.

Credit Unions are already permitted to perform a wide range of activity, but in some respects are unable to capitalise on their capabilities. Some examples are outlined below.

We believe that, with today's technology, the public expects an integrated Credit Union offering – i.e. shared online banking and shared transaction platforms, where, for example, a member with an account in Dublin could lodge/withdraw elsewhere in Ireland whether at the counter or at an ATM, whether provided by a credit union or a high street bank. It is our understanding that while technically possible today, it is prevented from happening by existing regulations, and we would ask for your consideration of options to remove these restrictions.

In recent years, the Central Bank has used the imposition of lending restrictions to curb lending practices in (we understand) approximately 50% of all credit unions. Across the movement, many of the reasons cited at the time of the imposition of the restrictions have long since been acted upon. Yet, despite approaches to the Registry of Credit Unions, many credit unions, including our own, report that there is minimal appetite to consider relaxation, or removal, of these restrictions. As economic conditions improve, it is imperative that such restrictions are eased, so that credit unions can properly accommodate members' personal borrowing requirements. In a properly run credit union, it is reasonable to conclude that the Board and management are in control of their business, and are ideally placed to consider the merits or otherwise of larger borrowing proposals.

We are pleased to note proposals to permit credit unions to lend over extended terms, particularly regarding mortgages. This will in turn create new challenges in the management of funding for such business, as well as the pricing of such products, but will enable credit unions to address a more comprehensive portion of member's financial services needs. However we believe that credit unions, irrespective of physical size, which possess the necessary expertise, systems, and controls, should be permitted to engage in lending forms which were prevented by legislation and regulation crafted in different circumstances to what applies at present. We therefore request that consideration be given to allowing category 1 credit unions to offer mortgage finance, initially in a limited manner, but with the possibility of reduced regulations governing this business as experience is built up.

We believe that consideration should also be given to permitting credit unions to become involved in hire-purchase and lease finance. While larger credit unións could provide this finance in their own right, smaller credit unions could perhaps offer this finance via a CUSO type organisation, with individual credit unions (and perhaps non-CU sales executives) earning commission from the business generated.

As is proposed for category 2 credit unions, such approval by CBI should be on the basis of well developed and tested business plans in advance of authorisation being given.

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Question 4: Do you agree that a provisioning framework should be developed for credit unions as proposed in section 6.2? If you have additional proposals please provide them along with the supporting rationale.

The CBI has been engaging at various levels within the movement for some years, including through the PRISM framework. It is therefore reasonable to assume that any entities carrying unacceptably high levels of risk have been identified and engaged with in further detail.

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Thank you for the opportunity to comment on the proposed regulatory changes. As a board, we are committed to the continued growth of our credit union and the movement. We are available to discuss any aspect of the foregoing with you should the need arise.

Yours faithfully,
Rathfarnham & District Credit Union

Pat Creighan
Hon. Secretary