



Office of The Registrar of Credit Unions

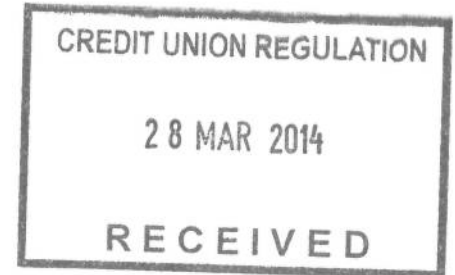
Central bank of Ireland

PO Box 559

Dame Street

Dublin 2

27/3/2014



**Response to Consultation Paper CP 76 on the Introduction of a Tiered
Regulatory Approach for Credit Unions.**

Dear Sirs,

The Board of Directors has examined the proposals outlined in the above document. We understand that CUDA, as our representative body, has responded to the paper and our credit union wishes to endorse the document previously forwarded by CUDA in this regard. We have also discussed the impact of these proposals with Davy, as our investment advisors. We understand that Davy will also be making a submission and would also support the input of Davy in respect to the impact of the proposals on our investment portfolio.

Having considered the Consultation Paper CP76 at length, our credit union is extremely concerned at many of the proposals therein, and in the cumulative effect of the proposals on our credit union, and the movement in general. Therefore, in addition to supporting the submissions mentioned above, our board considers it imperative that we outline our concerns directly in this document.

Background

Our credit union supports the introduction of tiered regulation in principle. We recognise **that** given the current levels of market penetration, and the vast diversity in size and nature of credit unions, it is difficult to support the differing business aspirations of all credit unions, within a single tier framework.

However, before addressing the proposals in the document, three high level issues must be addressed:

- **Purpose**
- **Timing**
- **Overall Impact**

Purpose

We note the comments in the Paper that the proposals on tiered regulation stem originally from the report from the Commission on Credit Unions. This report states that:

3.8 *The Commission recommends the introduction of a strengthened regulatory framework which credit unions will have to adapt to as it is phased in over time. However, credit unions should not be regulated on a one-size-fits-all basis; rather a tiered regulatory approach should be adopted.*

3.9 *The Commission considered that some of the new regulatory requirements may not be required for those smaller credit unions that want to operate a simpler business model. Therefore, it is recommended that those credit unions be permitted to opt for a more limited business model under a simpler regulatory regime.*

3.10 *Some larger credit unions that are capable of operating on a more sophisticated basis should be allowed to offer a wider range of products and services and engage in a broader range of lending and investment activities. This should be permitted under a more sophisticated regulatory regime for these credit unions.*

We believe that it is fundamental to these recommendations that they are “enabling” in allowing credit unions at all levels to determine their business model and implement strategies in keeping with their business capabilities and strengths. This will result in a stronger credit union sector, providing a real alternative to Irish consumers and business alike. The proposals outlined in the Consultation Paper, contain little that can be described as “enabling”. It is the view of our Board that the cumulative effect of the proposals would be to prevent the development of progressive credit unions and undermine the financial stability of those credit unions that have demonstrated high levels of business acumen through boom and recession.

Timing

In recent years credit unions in Ireland have experienced a huge increase in the level and application of legislative and regulatory requirements. We have seen implementation of new governance requirements under CUCOR, a new Risk Management and Compliance regime, new standards for Fitness and Probity, and Minimum Competency. These changes,

coupled with the introduction of the Prism regulatory code at the same time, have stretched the resources of many credit unions at this time, and will take some time to “bed in” at credit union level.

We are also concerned that the proposals outlined in the document be seen to be “forward looking”, taking into account the likely level of restructuring of the movement in coming years, and support the work of REBO, in particular. We believe that the proposals contain insufficient recognition of the future scale of individual credit unions, and their likely involvement in shared structures with other credit unions, to develop expertise and capabilities, currently unavailable to them.

Overall Impact

While this is an issue that we will expand on in this response, it must be stated at the outset that the proposals outlined in the Paper would, in our view, have the direct impact of preventing financially sound, progressive credit unions from developing new lending markets, while, at the same time, restricting their options in respect of investing surplus funds that they are consequently unable to lend. The inevitable long term consequence of this would be the decline and ultimate disappearance of credit unions in Ireland.

Overall there are concerns that while the additional regulatory requirements are significant and identifiable any proposed benefits are less well defined, subject to conditions, and not commensurate with the additional burdens proposed.

In addition, we have concerns that several of the proposals may be anti- competitive unless implemented across all financial institutions in an identical manner, and may give rise to challenge.

Specific Responses to CP76

4.8 The example structure as set out by the Commission, a three tier system, broadly reflected the differing capabilities and business aspirations of credit unions in Ireland. This model recognised that, while there are credit unions that might aspire to greater or less options in their operation, there are also a significant number for whom the current “status quo” represents the most attractive option.

We do not accept that the Paper sets out any compelling argument for deviating from this three tier model, which not only provides more flexibility, where required, but also means that those credit unions who are happy at their current level would not be required to undertake a formal application process to achieve a status comparable to that existing at present.

The Paper also proposes that all credit unions would automatically be classified as Type 1, on the basis that this allows credit unions “offer a comparable range of services” to those offered at present. A review of Section 5 of the Paper clearly outlines that, far from representing an “as is” scenario, the restrictions intended for Tier 1 credit unions are workable only at the lowest business levels. This forces the majority of credit unions to apply for Tier 2 status, a level that they may not require or want. This reiterates the need for a 3 Tier model along the following lines:

Standard

Tier 2 – Automatic “As is” scenario identical to current situation experienced by credit unions.

Available Options

Tier 1 – Subject to Application. Available to credit unions with limited business model, with proportionate relaxation of regulatory requirements.

Tier 3 – Subject to Application. Available to credit unions that require and are capable of implementing a more sophisticated business model, with proportionate additional regulatory requirements.

In proposing this model, we believe that it is of paramount importance that the benefits of each tier, together with the regulatory requirements attaching thereto, and the criteria attaching for upgrade, are clearly defined in advance of implementation. The current Paper contains little clarity around these issues. We would suggest that given the level of information now available to the Central Bank through PRISM and other regulatory mechanisms, the proposed tiering of each credit union could be known in advance.

5.12 (1)

We wish to make the following observations in respect of the proposals outlined in Sections 5.1-5.11:

5.1.2

Lending

We refer to our earlier observations regarding the “enabling” intent of the Commission proposals. Given the nature and scale of the additional regulatory burden for Tier 2 credit unions, it is inadequate to simply indicate that home loan lending “may be considered.” This should be an integral part of the proposals from the outset.

5.2.2 Concentration Limits

At the outset, we must point out that the imposition of lending limits, based solely on Regulatory Reserves, without consideration of other factors such as Expertise, Experience and History, Level of Provisions and Other Reserves, is inappropriate, and penalises credit unions that have been operating on a best practice basis for years. On this basis we suggest that the concentration limits set out in 5.2.2 should be replaced by a more broadly based matrix.

5.2.3 Maturity Limits

It is reasonable to consider the fact that a large number of credit unions in Ireland, if not all, are experiencing pressure on their ability to generate an annual surplus for their members. While many factors contribute to this, we believe that the core issue is the fact that the average loan to asset ratio for Irish credit unions is in the region of 30%. Our credit union, while strong financially, has recognised this in our Strategic Business Plans. It is our belief that credit unions must seek to achieve loan to asset ratios, closer to those in the US and elsewhere, at 60% approximately to achieve sustainability. In short, credit unions need to diversify outside of the existing personal lending market to achieve the required growth levels. This will not be achievable within the limitation proposed in the paper. Specifically, the continuation of the current Section 35 longer term limits will become totally unworkable in the context of home loan lending.

The following table utilises our current lending figures to demonstrate the impact of the proposals

Total Loans	Sec 35 > 10 Years = 15%	Existing Loans > 10 Years	Available to Lend in Homeloans	Average Homeloan	Number of Loans @ €100k avg.
	€8.85 mill	€3.49 mill	€5.36 million	€100k	53

This shows that our credit union, with total membership of over 35,000, would, under the proposals contained in this paper, be allowed issue 53 loans to members, and only facilitate 90 approx. at any one time over the next 25 years, even at the relatively conservative average of €100k per home loan.

This consequence is surely at odds with the stated aim of allowing capable credit unions expand the range of services offered, and greatly restricts the ability of credit unions to develop a business model to sustain and grow their business.

We would also point out that, in our opinion, the proposals in Sec 5.2.3 should be reconsidered to facilitate these long term growth strategies, and also to address the fact that such loans are secured against property, and or other assets. We would suggest that a more appropriate method to manage risk in respect of this lending is through proper provisioning policies.

5.2.4 Restricted Persons Limits

The inclusion of the members of the family of members of the Board of Directors and Management of a credit union in the category of Restricted Person is, we believe, discriminatory and unfair, and may be open to challenge.

In addition, an examination of the figures in the case of our credit union would indicate that the inclusion of such an extended group could give rise to unfair limits being placed on individuals within the Restricted Persons category:

Number of Directors	Number of Management	Total BOD & Mgmt	Family @ avg 8 per person	Regulatory Reserve	5% of Reg. Reserve	Max Loan Per Person
11	3	14	112	€22.6 mill	€1.13 mill	€10,100

We would recommend that the category of Restricted Person not include family. These loans can be monitored through internal audit, annual audit and PRISM processes.

5.2.5 Large Exposure Limits

While our comments elsewhere in respect of linking limits solely to Regulatory Reserve, we support the concept of controlling large exposures and consider the proposals in the paper appropriate.

5.2.6 Lending Practices & Policies

The additional systems and controls required in point three should be clearly spelled out in the next phase of the consultation process.

The requirement for a business plan & projections is unworkable without a lower limit and or clearly defined exceptions, given the new definition of commercial loan.

5.3 Investments

We are aware that both CUDA & Davy are addressing this area specifically in their responses to the document.

It is the view of our Board that the cumulative effect of the proposals as outlined in the Paper, and particularly the limits set out in section 5.3.3, will serve to limit the options available to Boards in investing surplus funds, and ensure that a larger proportion of such investments must be placed in lower yielding categories of investment, thereby placing further pressure on the credit union business model. We see no credible argument to indicate that the current investment parameters available to credit unions need to be restricted further.

In particular we again note the linking of limits to Regulatory Reserve, to the exclusion of all other considerations, and reiterate our previous comments in this regard.

We would argue that diversification is an important Risk management tool in any investment strategy, and that the option to avail of the diversification provided by equity based products should remain open to Boards, albeit within appropriate limits.

5.4 Savings

We would strongly oppose the introduction of such a limit as discriminatory and anti-competitive. It directly infringes the right of every saver to decide on where best to place

their savings and drives them directly into the hands of the banking sector, that is driven by the requirement to maximise profit.

5.6 Additional Services

We believe that category 2 credit union should automatically have the right to provide the following additional services:

- Home Loans
- Card Services
- Leasing (Vehicle & Equipment)
- Revolving Credit Facilities

5.7.2 Additional Governance Requirements

The definition of “dedicated” should be amended. We believe that it is in conflict with current legislation, and that such officers may have additional duties. In addition it should accommodate the option of credit unions resource sharing in respect of these functions. This ensures the utilisation of high quality resources on a cost effective basis.

The proposal that there be an external review of the performance of the board of directors every three years is unnecessary and should be removed. It interferes directly with the legal right of the members to elect a board of directors from their number. All candidates are now subject to Fitness & Probity, and Minimum Competency requirements. The operation of the Board is subject to monitoring by the Oversight Committee and the Auditors, who both report to the members at AGM. In addition each director is now subject to annual performance assessment, and the credit union is subject to ongoing PRISM assessment. The addition of a further layer of review would add further cost with no additional benefit to the credit union, or its members and could act as a deterrent to securing the involvement of the “Volunteer”

5.9.2 Operational Risk Reserve

While the holding of adequate reserves to protect the stability of the credit union is to be encouraged, it is our understanding that the rationale behind this new reserve was the purpose for which the Regulatory Reserve was required.

Overall, credit unions should not be subject to reserve requirements that are in excess of that required from other financial institutions in the jurisdiction.

5.10.2 Additional Liquidity Requirements for Category 2

We support efforts to ensure that credit unions maintain adequate liquid assets at all times. However greater clarity is required in respect of the management of maturity mismatches.

This should be provided as part of the next stage of the consultation process so that credit unions may properly assess the implications of such measures.

6.2 Proposed Provisioning Framework

We fully accept that credit unions should hold adequate provisions to manage the risk in their lending portfolio. We believe that the level of provisioning in our balance sheet, and the overall level of reserves attest to our commitment in this regard. However such provisions should not be at an excessive level to that required elsewhere in the financial services industry. An appropriate standardised framework would be welcomed on this basis.

However we have a number of concerns regarding the inclusion of the framework proposals within this paper:

- (1) As the proposed framework relates to all credit unions it should not form part of the investigation of tiered regulation, but be addressed separately.
- (2) It is regrettable that, in setting lending limits, no regard appears to have been taken to the level of provisioning already in place in credit unions. This should form part of a more considered matrix in setting appropriate lending limits.
- (3) The proposal to provide in full for a loan that is in arrears for a specific period constitutes unacceptable micromanaging of the affairs of the credit union, and is unfair and unworkable in practice. (As an example, a €100k 10 year loan may be €1 in arrears because of a once off one day delay in making a repayment, even though all due payments have been made. Under the proposals, this loan must be provided for in full)

Overall, we suggest that the level of provision required must be commensurate with, and appropriate to the risk inherent in the portfolio. The Regulatory requirements should assist the board of directors to determine and set aside the necessary level of provisions, not seek provisioning at inappropriate or unnecessary levels.

7.2 Timing

We have commented on the timing of the introduction of tiered regulation earlier in this document. While we support its introduction at the earliest opportunity, the proposals should consider allowing time for credit unions to assimilate the multitude of legislative and regulatory changes introduced in recent years.

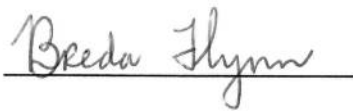
Conclusion

In conclusion, we welcome the opportunity to participate in this consultation process. We are supportive of the introduction of Tiered Regulation, subject to the concerns and reservations set out in this letter. However, we strongly believe that implementation of the

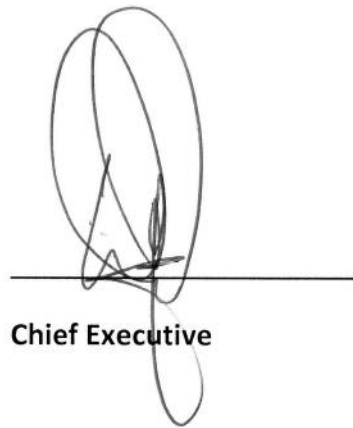
proposals as set out in the Consultation Paper could have drastic unforeseen consequences for the credit union sector. We respectfully request that consideration be given to the issues raised in this letter, and that, at a minimum, no measures be implemented without a full Impact Analysis being carried out.

We are available for further discussions on this document, if required.

Yours Sincerely

A handwritten signature in cursive script, reading "Beeda Flynn", positioned above a horizontal line.

Chairperson

A highly stylized, abstract handwritten signature consisting of several overlapping loops, positioned above a horizontal line.

Chief Executive