



Credit Union

Irish League of Credit Unions

Submission to Central Bank of Ireland in Response to CP 83

Fitness & Probity Regime for Credit Unions that are also Authorised as
Retail Intermediaries

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1. Introduction

In a 2013 speech to the National Supervisors Forum, the then Registrar for Credit Union, Sharon Donnery stated “I am of the firm view that the new legislation and the related regulatory reforms we are introducing are an important support that can drive and enhance the ability of credit unions to address the current challenges and the rapidly-evolving market in which they operate. The requirements, including strategic planning, also support an important forward-looking perspective where strategic direction and future viability are clearly articulated and understood within the credit union.....In the Registry, we see the implementation of proper governance as being a key element to bring about a financially strong and more sustainable sector which can continue to serve future generations of members.” The ILCU is in agreement that many of the new reforms will enhance governance, oversight and business structures within credit unions in the future. However, since the commencement of the new legislation and introduction of the Fitness and Probity Regime for credit unions, it is becoming evident that these same reforms are contributing to increased compliance costs, a reduction in income and a concentration of resources on compliance to the detriment of the credit union’s core business.

While credit unions have achieved a reduction in Gross Loan Arrears for ten consecutive quarters (up to June 2014) they are also continuing to experience a decline in both investment and loan interest income. Loan interest income in June 2014 is down 9.4% when compared to the same time last year. This is to be expected as lending restrictions combined with a suppressed demand for loans has led to a reduction in loan volumes across most of the credit union movement. Investment income has dropped by over 11% during the same period. This issue of reducing income is compounded by an increase in key operational expenditure, largely as a result of new legislative requirements.

There is no doubt that there is a need for adequate structures to ensure the prudent and compliant operation and governance of credit unions. The ILCU is increasingly concerned that the core business of credit unions is suffering at the expense of achieving this regulatory goal. This in turn could have the unintended consequence of placing credit unions in a financially precarious position in the future due to a lack of sufficient income combined with ever increasing operational costs. The cooperative nature of credit unions is a strength that protects its members from key governance and strategic risks that are systemic in other types of financial institutions. However, cooperatives by their very nature are not in a financial position to fund and sustain organisational reform at the same pace as other financial institutions, given their non-for-profit ethos and the requirement to serve all members equally, not just the “profitable” ones.

All stakeholders within the sector including the Central Bank recognise the important role that credit unions play in both local communities and the provision of financial services to members. Equally all stakeholders would like to see credit unions to have an enhanced ability to operate within an increasingly complex and competitive environment. Following the opportunity for meaningful strategic reform instigated by the Commission on Credit Unions three years ago; it would be unfortunate for the end result to be a stagnant and financially deteriorated movement mired in burgeoning compliance requirements. All stakeholders within the credit union movement including the regulatory authorities must play their part to avoid this outcome. It is of vital importance that the Registry of Credit Unions (RCU) moves quickly to restore a credit union’s ability to compete under

realistic conditions within the financial services market once the entity has demonstrated its underlying financial stability.

The ILCU had previously outlined the unworkable nature of transferring credit unions authorised as retail intermediaries to the F&P Regime for other Regulated Financial Service Providers (RFSP) in its submission in response to CP 62. As such, it is pleased to see the revised approach of the Central Bank detailed in CP 83 and is hopeful that a more nuanced approach to the application of regulatory requirements is continued in the future.

2. Executive Summary

In line with the views expressed in its 2013 submission in response to CP 62, the ILCU welcomes the introduction of a revised Fitness & Probity (F&P) regime for credit unions also authorised as retail intermediaries.

The ILCU has evaluated the suitability of the proposed regime detailed in Consultation Paper (CP) 83 for its affiliated credit unions under two broad criteria:

- (i) **Does the proposed regime enhance the interests of credit union members?** As regards this criterion the ILCU believes that, on balance, the revised F&P Regime for Credit Unions also authorised as retail intermediaries does enhance the interests of credit union members.
- (ii) **Does the proposed regime protect the co-operative ethos and democratic nature of credit unions?** The ILCU continues to be of the view that the F&P Regime for credit unions introduced on 1st August 2013 does not give adequate consideration to the voluntary and democratic structures of the credit union. The proposed amendments contained within CP 83 go some way towards rectifying the unworkable requirements for credit unions that are also authorised as retail intermediaries. Therefore with regard to the proposed tailored regime detailed in CP 83, the ILCU is of the view that this does offer better protection to the co-operative ethos and democratic nature of credit unions.

3. The Revised Approach for Credit Unions also Authorised as Retail Intermediaries

As prescribed in the Credit Union Act 1997 (Exemption from Additional Services Requirements) Regulations 2004 (as amended), credit unions may act as a restricted retail intermediary with regard to five basic general insurance products - (i) loan protection and life savings insurance (including related riders); (ii) travel insurance; (iii) home insurance; (iv) motor insurance; (v) repayment protection insurance. It is estimated that approximately 218 credit unions in the Republic of Ireland are authorised as a retail intermediary.

The ILCU is of the view that the revised approach outlined in CP 83 is necessary for credit unions which are also authorised as retail intermediaries. This position is supported by the following points:

- These credit unions are already subject to the full requirements of the F&P Regime for Credit Unions introduced on 1st August 2013 (or will be subject from 1st August 2015 if the credit union has assets of less than €10million). These credit unions are already required to comply with the Minimum Competency Code 2011 and the Consumer Protection Code relating to all financial services provided under their authorisation. Also, as detailed in CP 83 all officers involved in the provision of these financial services will be subject to the new tailored F&P regime. When considered collectively, the protection afforded to members (consumers) availing of these products are equal to that of any other retail intermediary. Also the level of regulatory oversight which can be applied to credit unions authorised as retail intermediaries is equal to that of other retail intermediaries.
- All credit unions subject to the F&P Regime for Credit Unions introduced on 1st August 2013 are already experiencing significant challenges regarding succession planning at board and management level. It is becoming increasingly difficult to identify suitable candidates willing to participate in an extensive due diligence process, particularly for voluntary positions. Some credit unions have informed the ILCU that experienced volunteers have vacated their position in the credit union as they perceive it to be an excessive, overly intrusive process. This challenge would simply become unmanageable for the majority of credit unions if the additional roles detailed in CP 83 were to require pre-approval from the Central Bank.
- As noted in CP 83, only 3% of a credit union's income is derived from commission from these authorised financial services. The services are provided on the basis that they are a convenience for members and are provided by an entity which they trust. As credit unions would be one of a very small number of not-for-profit providers of these services, it is in the interest of consumers that this choice remains. However, as such a small level of income is derived from this business; ILCU affiliated credit unions have indicated that they are unlikely to remain as authorised retail intermediaries if they were forced to transfer into the F&P Regime for RFSPs as the associated costs would greatly outweigh the income and associated benefits for members.

- The administrative costs incurred through the coordination of pre-approvals for PCF2 to PCF15 would be significant for both the 218 credit unions and the Central Bank. As there is no measurable benefit to consumer protection or reduction of enterprise-level risk associated with this requirement, the avoidance of these costs would be in the best interest of members and tax-payers alike.

4. Implementation of the Fitness and Probity Regime for Credit Unions also Authorised as Retail Intermediaries

The Standards

When the Standards of F&P for RFSPs were drafted, the suitability of these Standards for credit unions was never considered. Some consideration was given to the structure and ethos of credit unions when drafting the Standards of F&P for Credit Unions. As such, credit unions authorised as retail intermediaries continuing to operate under the Standards of F&P for Credit Unions is logical.

Indeed these standards require the credit union to consider the candidates' outstanding loans with the entity and also whether they were involved in a credit union which was in receipt of SPS funding. As such, these Standards offer additional protection to the credit union and members.

Guidance on Fitness and Probity

The ILCU is aware that all queries concerning individual questionnaires and processes involving the ONR system should be directed to the Regulatory Transactions Division within the Central Bank. The ILCU recommends that the contact point for credit unions that have queries relating to the general requirements of the F&P Regime is published along with the guidance.

Timelines

The ILCU believes that if possible an extension to the three deadlines outlined in CP 83 should be given in recognition of the fact that the requirements for credit unions also authorised as retail intermediaries have now changed. As the final details of the tailored regime are unlikely to be published in advance of the next AGM for many credit unions, this will not allow for consideration to the composition and structure of committees / roles which may or may not be affected by the tailored regime proposed in CP 83. This also applies to any decisions required regarding the credit union's continued authorisation as a retail intermediary. By extending the deadlines by a further six months, this would ensure all credit unions will have an AGM before the new requirements apply.

As highlighted in CP 83, the current deadlines coincide with those deadlines for credit unions with an asset size of less than €10million. The ILCU is of the view that keeping these deadlines aligned is beneficial and practical for all concerned. As such, the ILCU recommends that the same deadlines for credit unions with an asset size of less than €10million also be extended by six months to maintain this.

5. Conclusion

Overall the ILCU is supportive of the proposed tailored regime for credit unions also authorised as retail intermediaries as it is detailed in CP 83. The ILCU would be of the view that anything less than the full implementation of these revisions would result in an unworkable set of requirements. The negative effect of this has been clearly outlined in sections one and two of this document.

The ILCU is open to engaging with the Central Bank or the Registry of Credit Unions to advise on any matters relating to the implementation of the revised regime.