



ILCU Submission to CBI on

*CP 88: Consultation on Regulations for Credit Unions on
Commencement of the Remaining Sections of the 2012 Act*

Submitted to rcuconsultation@centralbank.ie on 27 February 2015.

1. Introduction

- 1.1. Following publication by the Central Bank of Ireland ('CBI'/'the Bank') of *Consultation on Regulations for Credit Unions on commencement of the remaining sections of the 2012 Act* ('CP 88'), the board of directors of the Irish League of Credit Unions (the 'League Board') undertook a process of the consideration of its contents both within the League itself (at League Board and Legislation Committee level) and with member credit unions at six roadshows which convened during February 2015.
- 1.2. We welcome the opportunity to provide comments to CBI by way of this submission which articulate views expressed during this process of consideration and consultation.
- 1.3. In order to do so, issues will be addressed under the various headings and in the order in which they appear in CP88.
- 1.4. For ease of reference, points made under the various headings are stated in a *Summary of Issues* section at the commencement of each.

2. Reserves (Section 5 of CP88)

(i) Do you have any comments on the draft reserves regulations? If you have suggestions please provide them along with the supporting rationale.

Summary of Issues

1. What is the rationale for a minimum reserve requirement of 10%?
2. A risk weighted approach to reserving (which exists in other credit union movements) would be preferable to the blanket application of 10% across all credit unions.
3. We do not agree that newly formed credit unions should be required to hold an *Initial Reserve Requirement* on top of a *Regulatory Reserve Requirement* plus any *Operational Reserve* CBI may require.

2.1 Issue 1 - 10% minimum reserve requirement.

And

Issue 2 - Employing a non-risk weighted approach to reserving.

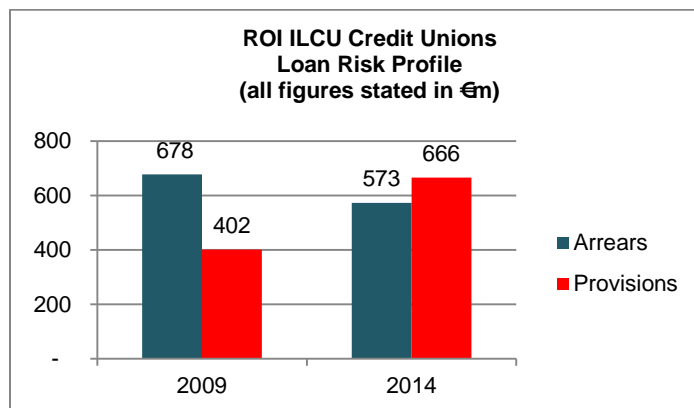
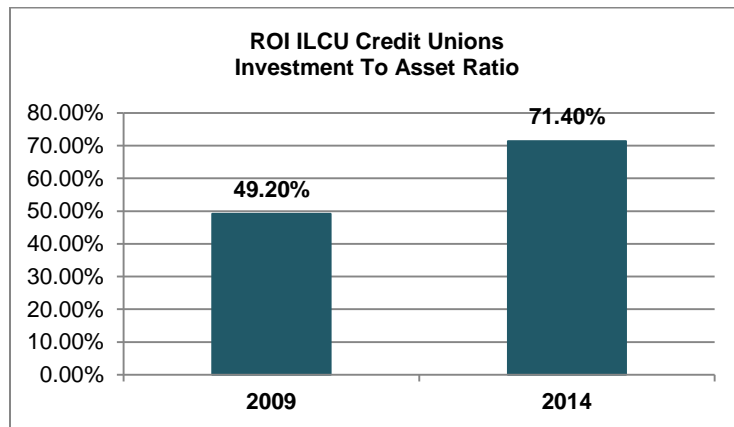
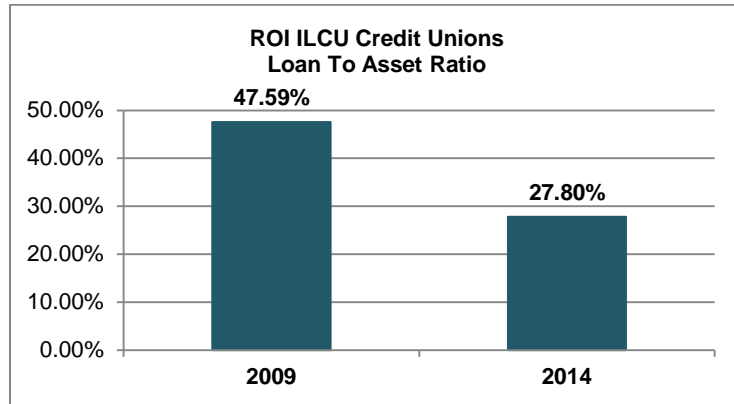
2.1.1 Comments

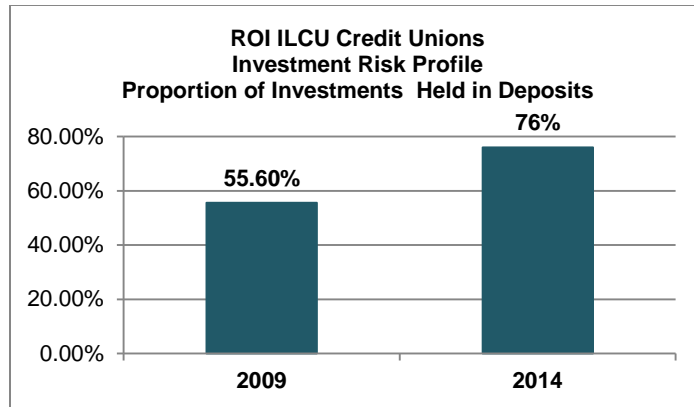
2.1.1.1 We note that the core underlying principle in this area as described in CP88 is that a credit union “*must maintain adequate reserves having regard to its nature, scale and complexity*”. This appears to be a sound and reasonable principle as it suggests that due regard is placed on the nature of the assets that a credit union holds.

2.1.1.2 In assessing “*nature*”, risk must be a critical consideration e.g. a credit union that is 30% lent, with the majority of its funds held in deposit based products is wholly different in *nature* to a credit union that is 70% lent with a more diversified investment base.

2.1.1.3 The application of a blanket 10% regulatory reserve requirement does not appear consistent with the principle that a credit union “*must maintain adequate reserves having regard to its nature, scale and complexity*” insofar as it does not take due regard of the nature of the assets held by credit unions.

2.1.1.4 The nature of assets held by credit unions has changed significantly over the last 5 years (since the introduction of the Regulatory Reserve Ratio in 2009). This is illustrated below, by reference to consolidated movement statistics of ILCU affiliated credit union in the Republic of Ireland:





Based on the above graphs, it is clear that the nature of assets (both in respect of risk profile and make up) has fundamentally changed since the introduction of the Regulatory Reserve Ratio as follows:

- i. Credit unions are significantly less lent now, have smaller loan books, larger provisions, falling arrears and therefore are exposed to lower levels of credit risk.
- ii. Credit unions have more concentration in deposits in authorised credit institutions (which are generally protected by the various interventions of EU governments) and therefore are exposed to lower levels of counterparty risk.
- iii. In these ways, the *nature* of credit union assets has changed significantly.
- iv. This is separate to qualitative factors which are also relevant in assessing the nature of assets (and the lower risk profile) such as:
 - a. More robust underwriting practices which better mitigate credit risk;
 - b. More robust investment governance practices which better mitigate counterparty risk; and

- c. A strengthened governance and risk management framework which promotes a broader culture of risk awareness.

2.1.1.5 While the League accepts the fundamental principle set out in the Regulatory Reserve Requirement¹ i.e. that “adequate reserves are the foundation on which the financial stability of a credit union rests”, we believe the 10% regulatory reserve requirement to be inflexible and lacking the required dynamism to adjust to the changing environment of credit unions and to reflect the changing nature of credit unions’ assets.

2.1.1.6 Currently, the average capital level in an ILCU affiliated credit union in the Republic of Ireland is 15.5%. In 2009, this was 12.3%. In absolute terms, the total capital of ILCU affiliated credit unions in the Republic of Ireland is currently €2bn. The excess capital over the Regulatory Reserve Ratio is €710m.

ILCU views the *efficient* use of capital as being a critical consideration for credit unions, at this point in the economic cycle. While reserves have a role in providing certain buffers, they are above all comprised of members’ wealth. Reserves should not just be commensurate to risk but should also be used efficiently, prudently and in the members’ best interests. As stated above, there is currently €710m of members’ funds held in the reserves of affiliated credit unions above the regulatory reserve requirement. The efficient use of reserves requires a more dynamic regulatory approach to reserving which would:

- i. Enable more flexible capital management policies and dividend policies to facilitate the appropriate investment of capital in the business model of credit unions to create more robust and sustainable credit unions with an enhanced ability to serve members’ needs.

¹ Regulatory Reserve Ratio for Credit Unions, 2009

- ii. Enable a more flexible regulatory approach in setting risk appetite/tolerances that are better correlated with capital levels.
- iii. Enable a more expanded reserve approach which would facilitate credit unions in benefitting the broader economy and contributing to the national economic recovery.

2.1.2 Suggestions

2.1.2.1 That CBI considers a more dynamic regulatory reserve requirement that better reflects the nature of risk in Irish credit unions, the environment to which credit unions are exposed, and the broader role of Irish credit unions in the Irish economy. A non-risk based 10% regulatory reserve requirement is inflexible and lacks the required dynamism to reflect to these considerations.

2.1.2.2 That CBI considers a more dynamic regulatory reserve requirement that promulgates a more *efficient* use of capital mindful of the vast levels of capital in credit unions.

2.1.2.3 Noting the importance of the principles of proportionality and efficiency in the maintenance of capital in Irish credit unions, the League has commissioned an external report on capital levels in credit unions in the Republic of Ireland and will be glad to engage further with CBI in this regard.

2.2 Issue 3 - Introduction of an initial reserve requirement.

2.2.1 Comments

We note the following:

- i. It is proposed to introduce an initial reserve requirement for newly registered credit unions.
- ii. The effect of this proposal would be that a newly registered credit union would have to meet:

a. *An Initial Reserve Requirement;*

And

b. *Any applicable Regulatory Reserve Requirement;*

And

c. *Any Operational Reserve* which the Bank may require that the credit union hold.

iii. We consider that such an approach would be prohibitive and would act as a barrier to entry which is entirely at odds with the philosophy and objectives of the credit union movement.

iv. The rationale for the proposed introduction of an *Initial Reserve Requirement* (articulated at page 15 of CP88) is:

“to support the credit union’s anticipated growth and take account of expected operating losses”.

v. It appears therefore that the approach being suggested is risk based. Such any approach would imply that a capital cushion would be commensurate with the level of risk on the balance sheet of a credit union and could be built up in an orderly and constructive manner as the risk profile of the newly formed credit union grows.

vi. A capital “glide-path” for a start-up credit union (i.e. where a newly formed credit union builds up capital in a time-bound manner) would be preferable to what appears to be proposed in CP88.

vii. New section 45 (3) (c) of the Act provides that:

(3) The Bank may prescribe the regulatory reserve requirement that a credit union shall maintain at a minimum and, in so prescribing, may include conditions on the application of the regulatory reserve requirement. For that purpose the Bank may also prescribe in respect of other matters related to the regulatory reserve requirement, including any of the following:

[...]

(c) the requirement for initial reserves to be held by a newly-registered credit union under section 6.

- viii. In proposing to “*prescribe*” the regulatory reserve requirement in line with its power to do so under Section 45 (3) of the Act, CBI has been specific in its proposal of 10%.
- ix. In proposing to “*prescribe*” an initial reserve requirement in line with its power to do so under Section 45 (3) (c) of the Act, CBI has not been at all specific in its proposal.
- x. Murdoch’s Dictionary of Irish Law² defines “*prescribe*” as:
- “To lay down with authority; to set out under a regulation.”*
- xi. We would question whether the provisions at draft Regulation 5 either set down with authority or set out what the obligation around an *Initial Reserve Requirement* would be if the draft Regulation were to come into effect.
- xii. **Capital Requirements Directive**

Credit unions in the Republic of Ireland are exempt from the Capital Requirements Directive.

A primary driver of that exemption was a recognition that, given the nature and ethos of credit unions, it would not be appropriate to impose an initial capital requirement on credit unions as to do so (absent a philanthropic contribution or similar) would effectively prohibit the development of new credit unions.

We do not believe that the lack of newly registered credit unions in the Republic of Ireland movement in recent time is relevant or somehow defeats the validity of the CRD argument. The movement has operated here for over 50 years. For the majority of that period, the registration of newly formed credit unions was very much a feature. The fact that this has not been the case in recent times is of limited relevance in the overall context of the past and future development of the movement in the Republic of Ireland.

You will be aware that discussions have been ongoing with the League for some time around the establishment of a new Dublin based credit union with a national common bond. It is hoped that this can be achieved during 2015.

² Murdoch’s *Dictionary of Irish Law*, 4th Edition, Page 850, Henry Murdoch, Lexis Nexis, 2004.

Clearly, the imposition of an *Initial Reserve Requirement* on this (or indeed any other such) initiative would almost certainly have a devastating impact on its success.

2.2.2 Suggestions

2.2.2.1 The CBI considers a more dynamic regulatory reserve requirement for newly formed credit unions that better considers the nature of risk in such entities.

3. Liquidity (Section 6 of CP88)

(ii) Do you have any comments on the draft liquidity regulations? If you have suggestions please provide them along with the supporting rationale.

Summary of Issues

1. Timing of the proposed introduction of a short term liquidity ratio.
2. Expanding the definition of liquid assets and the explicit written guarantee.

3.1 Issue 1 - Proposed introduction of a Short Term Liquidity Ratio of 10% within one year of commencement.

3.1.1 Comments

We note the following:

- i. It is proposed to introduce a short term liquidity ratio of at least 10% of unattached savings (where short term liquidity is defined as cash and investments with maturity of less than eight days).
- ii. The rationale provided for the proposed change (articulated at page 19 of CP88) is that:

“The Central Bank considers it prudent that credit unions should ensure that their liquid assets contain a mix of maturities, including a portion on call to ensure that the credit union can meet its obligations as they arise on an on-going basis as required under the 1997 Act. In particular, the on-demand nature of credit union savings is a consideration for credit unions in ensuring they maintain appropriate short term liquidity”.

- iii. An overriding statutory obligation on CBI (articulated at Section 84A of the Credit Union Act) is as follows:

In making regulations under this Act, the Bank shall have regard to the need to ensure that the requirements imposed by the regulations so made are effective and proportionate having regard to the nature, scale and complexity of credit unions, or the category or categories of credit unions, to which the regulations will apply

- iv. In our discussions with credit unions on this issue, a recurring theme was the severe difficulty credit unions are continuing to experience in making a return on investments. Numerous credit unions articulated the view that to impose further restrictions in what is already a very difficult area at this time would be problematic.

3.1.2 Suggestions

3.1.2.1 We suggest that the issue be revisited as part of an overall review of the new Regulations (see page 35 of this document).

3.2 Issue 2 – Expanding the definition of liquid assets and the explicit written guarantee.

3.2.1 Comments

We note that:

- i. It is proposed to expand the definition of liquid assets to include the amount of any investment with more than three months to maturity where the credit union has an explicit written guarantee that the funds can be accessed by them in less than three months (and that with a guarantee, the investments may be considered liquid assets to the value of the investments guaranteed, excluding penalties on interest or income).
- ii. The definition of short term liquid assets includes investments with a maturity of less than 8 days (excluding the minimum reserve deposit account and the deposit protection account).

3.2.2 We are concerned that the Regulation may be attempting to make the benefit of the expanded definition dependent on something which may be beyond the control of the credit union e.g. in circumstances where the counterparty refuses to provide an explicit written guarantee.

3.2.3 In the event that a particular type of investment or a particular counterparty transpires to be more willing than others to provide the required explicit written guarantee on the terms dictated by the Regulation, we are concerned that the Regulation could be interpreted as indirectly requiring credit unions to hold particular products with particular counterparties which would be highly undesirable.

3.2.4 **If a credit union cannot, for whatever reason, benefit from the expanded definition, they will effectively be limited to incredibly short term accounts (or equivalent) with little or no return.**

3.2.2 Suggestions

3.2.2.1 Revisit the proposal to impose a short term liquidity requirement.

3.2.2.2 The question of the suitability or otherwise of the proposal could be revisited as part of a review of the Liquidity Regulations (see page 35 of this document).

4. Lending (Section 7 of CP88)

(iii) Do you have any comments on the draft lending regulations? If you have suggestions please provide them along with the supporting rationale.

Summary of Issues

1. Relevant extracts from CP88 and related comments.
2. Creation of categories of credit union loans.
3. Retention of the existing Section 35 limits (>5 and 10 year percentages).
4. Maximum maturity limit on loans of 25 years.
5. Maximum loan – the greater of €39,000 or 10% of RR.
6. Lending Concentration Limits.
7. Lending to Related Parties.
8. Total large exposures limit.
9. Maturity of Lending

4.1 Issue 1 – Relevant extracts from CP88 and related comments.

4.1.1 Comments

4.1.1.1 The following extracts from CP88 refer:

- i. **At Page 13** in relation to the proposed new lending framework:

“These requirements are informed by regulatory actions taken by the Central Bank arising from lending practices in individual credit unions”.

And

- ii. **At Footnote 9 (page 13)** that:

“There are currently lending restrictions in place in c.58%³ of credit unions. These have been imposed on individual credit unions on a case by case basis arising from specific supervisory concerns”.

^{3 3} On 12 February 2015, the Minister for Finance confirmed that “about 56% of all credit unions are subject to lending restrictions”.

And

iii. At Page 14:

“Where credit unions can demonstrate improvements in their credit risk management practices in line with the strengthened regulatory framework, it is anticipated that the use of credit union specific restrictions as a regulatory tool will reduce over time.”

- 4.1.1.2 We are concerned that, taking the above extracts together, CP88 evidences an intention to create a regulatory environment for all credit unions that will ultimately result in CBI having to issue fewer individual Regulatory Directions.
- 4.1.1.3 It is not appropriate to propose to create a restrictive lending framework for all credit unions when, as appears from the above extracts, CBI’s basis for that restrictive framework is its experience in credit unions where it has found reason to take supervisory action.
- 4.1.1.4 To reign in the business/ability of all credit unions to earn income on the basis of CBI’s concern around some, is – in our opinion - not the correct approach for CBI to employ in making general Regulations for all credit unions.
- 4.1.1.5 Does CBI consider that this is a *“proportionate”* approach to Regulation making (in line with its statutory duty under Section 84A⁴ of the Act)?
- 4.1.1.6 CBI has made extensive use of its statutory powers to impose Regulatory Directions on individual credit unions in recent years. There is an IFSAT appeal against CBI’s decision to impose a Regulatory Direction on an individual credit union which is a vital component of natural justice. On the other hand, there is no statutory appeal against CBI when it makes general Regulations (such as those contained, in draft form, in CP88).

⁴ Section 84A states that *“In making regulations under this Act, the Bank shall have regard to the need to ensure that the requirements imposed by the regulations so made are effective and proportionate having regard to the nature, scale and complexity of credit unions, or the category or categories of credit unions, to which the regulations will apply”*.

4.1.2 Suggestions

4.1.2.1 In the interests of natural justice, the existing system of individual Regulatory Direction and statutory appeal must be maintained and not abandoned in favour of CBI using general Regulations to create an overly restrictive lending environment for *all* credit unions.

4.2 Issue 2 – Creation of categories of credit union loans.

4.2.1 Comments

4.2.1.1 We note:

- a. the proposed creation of a *House Loan* category (Category 4); and
- b. the requirement that a credit union must hold a first legal charge on property to make a *House Loan*; and
- c. the retention of existing Section 35 restrictions on lending (percentages); and
- d. the proposed introduction of a 25 year maximum on any loan.

4.2.1.2 Bearing (a) to (d) above in mind, we feel that the issue of credit unions providing this type of lending to members is deserving of a focused and thorough consideration with a view to making a *House Loan* specific Regulation at the end of that process.

4.2.2 Suggestions

4.2.2.1 In defining the various categories of loan, it may assist to align wording where possible e.g. the definition of “*personal loans*” refers to “*the purchase of property*” whereas the definition of “*house loans*” refers to “*buy[ing] a house that is already constructed on the property*” and also, having a house constructed on property.

4.2.2.2 ILCU calls for the creation of a **Working Group on CU House Loans** (to include movement stakeholders and, where necessary, external specialists) to expedite a dedicated consideration of the issue of *House Loans*. The establishment or operation of the Group should not negatively impact in any way on any credit unions currently operating successful first charge lending schemes.

4.2.2.3 Having noted the confirmation (at page 27 of CP88) that CBI will take “*decisions made on CP87 into account when finalising the lending regulations for credit unions, including consideration of loan to value requirements for house loans*”, we are concerned that the outcome of this could be the publication by CBI of a Lending Regulation (or portion thereof) which credit unions have not had prior sight of.

4.2.2.4 We believe this to be contrary to a commitment made by CBI in its 2012 *Consultation Protocol for Credit Unions* which states (at paragraph 4) that:

The Central Bank will consult on new regulations that will, in the view of the Central Bank, potentially impact on the business of credit unions.

4.2.2.5 Given that all issues related to lending go to the very core of “*the business of credit unions*”, we feel that these matters (together with all other considerations around the provision of house loans by credit unions) must be fully dealt with prior to regulations being made in the area of house loans and should be addressed in early course by a *Working Group on CU House Loans*.

4.2.2.6 Please define the *Loans to Other Credit Unions* category (Category 5).

4.2.2.7 Please confirm that credit unions can continue to make loans for home renovations and improvements (without having a first charge on property) under the *Personal Loan* category (Category 1).

4.3 Issue 3 – Retention of the existing Section 35 limits (over 5 and 10 year percentages).

4.3.1 Comments

4.3.1.1 The League’s views on the overly restrictive nature of the existing large exposure and lending limits stipulated at Section 35 have been well-rehearsed over the years. We are disappointed that the draft Regulations propose to retain those overly restrictive limits.

4.3.1.2 These limits are preventing some credit unions from lending to *good borrowers* and, in this way, they are effectively being prevented from generating income. We expect that more will fall into this category as loan demand increases alongside the national recovery.

4.3.2 Suggestions

4.3.2.1 In order to safeguard the continued existence of credit unions in the Republic of Ireland – their ability to generate income has to be protected.

4.3.2.2 With this in mind, we ask that CBI utilises the opportunity presented by this set of Regulations to revise the existing Section 35 percentages upwards.

4.4 Issue 4 – Maximum maturity limit on loans of 25 years.

4.4.1 Comments

Previous comments on the establishment of a *Working Group on CU House Loans* refer.

4.4.2 Suggestions

4.4.2.1 Please provide a rationale for the imposition of a 25 year maximum maturity limit as this has not been stated in CP88.

4.4.2.2 Defer further consideration of imposing any maximum maturity limit on loans until the *Working Group on CU House Loans* has had an opportunity to fully consider the issue of home loans before making its report.

4.5 Issue 5 – Maximum loan – the greater of €39,000 or 10% of RR.

4.5.1 Comments

4.5.1.1 Our understanding is that the relevant limit is 10% of whatever a credit union holds in its Regulatory Reserve and the following comments are made on that basis.

4.5.1.2 Why is CBI proposing to move from the current system (% of total assets) which has been used by credit unions for decades?

4.5.1.3 The limited rationale for the proposed change (articulated at page 28 of CP88) is:

“The large exposure limit set will now be calculated based on a credit union’s reserves rather than assets so that lending takes account of the credit union’s ability to absorb any losses that may arise from credit risk.”

4.5.1.4 **Our data indicates that, if introduced today, just over 40% of member credit unions would have a lower maximum loan limit than that which has been available to them since the introduction of the 1997 Act, a fact that is not immediately apparent from the text of CP88 (which omission, we would expect, will not be repeated in future RIAs conducted by CBI – see further comments on this issue at page 36 of this document).**

4.5.1.5 Our analysis shows that the largest impact would be on smaller credit unions with lower than average regulatory reserves. ILCU data indicates that, if implemented today, 8 member credit unions (2%) would breach the new requirement.

	Assets	RR	Old 1.5% Maximum	New Maximum
Small CU	€4m	16%	€58,700	€62,274
Medium CU	€44m	15%	€652,921	€660,589
Large CU	€103m	15%	€1,541,173	€1,581,710

4.5.1.6 Also omitted from consideration as part of CP88 is the issue of Value in Use. In the event that the proposal to link loan maximums to reserves rather than assets is implemented and a credit union is required to post an impairment on its premises (which, as you would expect since the collapse of the property market in the Republic of Ireland, is likely to be substantial), the result of that will be greatly reduced reserves and therefore a significant knock on effect on that credit union's ability to lend (more so than if it were to remain linked to total assets).

4.5.1.7 In this scenario therefore, a credit union with potentially excellent lending practices, policies and procedures would suffer a significant drop in its maximum loan on the basis of nothing at all to do with its lending function but instead, as a direct result of the collapse of the Irish property market.

4.5.2 Suggestions:

4.5.2.1 Please clarify:

- i. That the proposed limit is 10% of total realised reserves.
- ii. The rationale for moving from the current system which has been imbedded in credit unions for decades.
- iii. The rationale for proposing to restrict the maximum loan which can be granted by a credit union by reference to external factors over the credit union has no control e.g. the collapse/recovery of the Irish property market.

4.6 Issue 6 - Lending Concentration Limits

4.6.1 Comments

We note that:

- i. It is proposed to introduce the following lending concentration limits:
 - Commercial ↑ 50% of RR
 - Community ↑ 25% of RR
 - Other CUs ↑ 12.5% of RR
- ii. ILCU data indicates that introduction of the proposed new limits would result in the following maximums:

At Movement Level (ILCU Credit Unions)

Commercial	€1.003 billion
Community	€502 million
Inter Credit Union	€251 million

At Credit Union Level

	Asset Size	Commercial Maximum	Community Maximum	Inter CU Maximum
Small CU	€5m	€417,000	€208,000	€104,000
Medium CU	€30m	€2.3m	€1.2m	€574,000
Large CU	€103m	€8.0m	€4.0m	€2.1m
Total		€1,004m	€502m	€251m

- iii. The limited rationale for the proposed change (as articulated at page 27 of CP88) is that:

“The Central Bank is also introducing concentration limits and requirement for certain categories of lending to reflect the specific risks associated with these categories.”
- iv. The proposed concentration limits could be too restrictive if credit unions expand on this type of lending in the future.

4.6.2 Suggestions

- 4.6.2.1 We do not believe that it is appropriate for CBI to engage in the blanket application of lending concentration limits to every credit union irrespective of size or capacity to manage risk nor do we believe that CBI has adequately explained its rationale for proposing to do so.
- 4.6.2.2 Credit union boards and management are best placed to consider and agree on concentration limits within their own credit unions and we would suggest that they be left to do so.
- 4.6.2.3 CBI's willingness to restrict individual credit unions in these areas (where it has deemed that cause exists to do so) has been widely evidenced in recent years.
- 4.6.2.4 The current system of assessing credit unions on an individual basis and, where necessary, imposing Regulatory Directions in accordance with Section 87 of the Act (subject to any successful appeal to IFSAT) must be maintained.
- 4.6.2.5 The matter could be revisited as part of an overall review of the regulations (see page 35 of this document).

4.7 Issue 7 - Lending to Related Parties

4.7.1 Comments

We note that a:

- i. *Related Party* is a member of the board or management team or a member of their family or a business in which they have a significant shareholding; and
- ii. *Member of the Family* is a person's father, mother, spouse or civil partner, cohabitant, son, daughter, brother or sister.

4.7.1.1 Credit unions have expressed concern around the introduction the proposed system of lending to Related Parties and the likely impact it would have on their ability to attract and retain volunteers and therefore, would not want restrictions to go beyond those which are currently in place for loans to officers.

4.7.1.2 The limited rationale for the proposed change (as articulated at page 29 of CP88) is:

"The Central Bank is introducing requirements on the governance of related party lending to supplement these [loans to officers] requirements but is not proposing to introduce limits on related party lending at this time in recognition of the community based nature of the sector and the potential impact this may have on the implementation of such limits."

4.7.2 Suggestions

- 4.7.2.1 Anything that could mitigate against the successful recruitment and retention of credit union volunteers is a matter of huge concern that goes to the very core of the movement.
- 4.7.2.2 As such, it is critically important that this type of restriction does not impose further on the officers of credit unions and their families etc. than is entirely necessary and we would ask that CBI review the issue on that basis.
- 4.7.2.3 While the €2,000 threshold is noted, we would ask that it be revisited with a view to an upwards revision. Also there is no cognisance of the risk attaching to the loan e.g. where it is above the threshold but within savings.
- 4.7.2.4 The definition of “Cohabitant” in the 2012 Act refers. Is it intended that a person is deemed to be a *Member of the Family* for the purposes of related party lending immediately upon cohabitating or should the reference be to a “qualifying cohabitant” under the relevant Act⁵?

4.8 Issue 8 – Total large exposures limit

- 4.8.1 We note the following extract (page 28 of CP88):

“The draft lending regulations do not define a large exposure or include a total large exposures limit as provided for in the regulation making powers contained in section 35. However, the Central Bank intends to issue guidance defining a large exposure as any exposure greater than 5% of RR and indicating that the total large exposures (including contingent liabilities) of a credit union should not be greater than 500% of the RR of the credit union. Following commencement of the regulations, credit unions will be required to report on the number and amount of large exposures held by the credit union, which will facilitate analysis to inform a regulatory limit on total large exposures in the future.”

While we would query why this information was not sought from credit unions in advance so that it could be included along with all other matters in CP88, it is perhaps opportune in that it affords the *Working Group on CU House Loans* an opportunity to examine the appropriateness or otherwise of what is being proposed as part of its work.

⁵ Civil Partnership and Certain Rights and Obligations of Cohabitants Act 2010

4.9 Issue 9 – Maturity of Lending

4.9.1 We note the following (footnote 12 on page 29 of CP88):

“The Central Bank is reviewing the conditions that currently apply for credit unions to be approved to extend their longer term lending limits.”

4.9.2 We would appreciate detail around why that review is taking place and when it will be completed.

4.9.3 Again, outputs from the *Working Group on CU House Loans* will no doubt be of significant benefit to CBI in its review of these matters. As a general principle, we would say that any assessment as to whether credit unions can benefit from the increased percentages should be based on that credit union’s current ability to run an excellent lending function and should not be driven by historic arrears.

5. Investments (Section 8 of CP88)

(iv) Do you have any comments on the draft investments regulations? If you have suggestions please provide them along with the supporting rationale.

Summary of Issues

1. Removal of Equities.
2. Introduction of Concentration Limits for investments in other credit unions and Industrial & Provident Societies (12.5% of RR)
3. Applying maturity limits to the *Investment Portfolio* rather than *Individual Investment Classes*
4. *Irish and EMU State Securities* expanded to *Irish and EEA State Securities*
5. Restriction of Authorised Classes of Investment.
6. Proposed maturity limits for investments.

5.1 Issue 1 - Removal of Equities.

5.1.1 Comments

5.1.1.1 We understand that managed funds that include a portion of equities will not be impacted and that the new proposed rule relates only to credit unions investing directly in equities.

5.1.1.2 In our discussions with member credit unions, some have opposed the proposal to remove equities.

5.1.2 Suggestions

5.1.2.1 Please confirm that managed funds which include a portion of equities will not be impacted by the proposed change.

5.1.2.2 We would ask that the views of credit unions on this issue be given due consideration by CBI.

5.2 Issue 2 - Introduction of Concentration Limits for investments in other CUs and Industrial & Provident Societies (12.5% of RR)

5.2.1 Comments

5.2.1.1 Previous comments on the issue of lending concentration limits refer.

5.2.1.2 Credit union boards and managements are best placed to consider and decide on concentration limits within their own credit unions.

5.2.2 Suggestions

5.2.2.1 Encourage credit unions to carefully consider any concentration limits which may be appropriate (relative to factors in their own credit unions) as part of their overall Investment Policy.

5.2.2.2 We will be glad to do likewise and will undertake to circulate guidance to affiliated credit unions in this area.

5.3 Issue 3 - Applying maturity limits to the *Investment Portfolio* rather than *Individual Investment Classes*

We agree with this approach.

5.4 Issue 4 - *Irish and EMU State Securities* expanded to *Irish and EEA State Securities*

We agree with this approach.

5.5.1 Issue 5 - Restriction of Authorised Classes of Investment.

5.5.2 Comments

5.5.2.1 There have been ongoing discussions around credit unions playing a significant role in various social and economic initiatives in the State (as evidenced at page 33 of the *Social Housing Strategy 2020: Support, Supply and Reform*⁶ which was approved by Government in November 2014).

⁶ The Government, as part of Budget 2015, announced that €400m of public investment will be available, including the proceeds from the sale of Bord Gáis energy business, to capitalise this new vehicle and provide for at least 2,000 housing units. ***This investment can then leverage private sector finance which will be raised from a variety of sources which could include the EIB, ISIF, Pension Funds, Credit Unions and other financial institutions, both domestic and international.*** This funding will then be lent on to qualifying AHBs, giving them access to long term finance. The Government believes that this new source of funding will enable AHBs to better leverage their existing stock with the ultimate aim of delivering more housing from scarce exchequer resources. This funding solution will be part of an incentivised programme where AHBs will commit to deliver specific housing targets and AHBs that are the most active and capable of delivering new housing supply will receive a greater proportion of this funding.

5.5.2.2 CBI's power to prescribe the investments in which a credit union may invest derives from section 12 of the *Credit Union Act 2012* (inserting a new section 43). New section 43 (3) (a) provides that the Bank may also prescribe other matters in relation to prescribed investments including:

The classes of investments including, where appropriate, any investment project of a public nature the credit union may invest in.

5.5.2.3 **Given that the ability for CBI to prescribe such matters was in line with the wishes of the Commission on Credit Unions, it is regrettable that CBI now appears to have opted not to exercise its power to do so.**

5.5.2.4 We believe it is vital that the *Working Group on CU House Loans* be mandated to consider the issue of centralised mortgage lending by credit unions which will be a vital component of a holistic approach to the Working Group's consideration of the issue. Consideration of the operations of other credit union movements in the area will no doubt be of substantial benefit to the Working Group.

5.5.2.5 We note the omission of *Corporate Bonds* (which had featured in CP76) from CP88. We believe that the ability for credit unions to invest in corporate bonds is important in terms of their ability to diversify investment portfolios.

5.5.3 Suggestions

5.5.3.1 In the interests of credit unions playing a significant and worthwhile role in these areas, additions must be made to the proposed list of authorised classes of investments (at draft Regulation 25).

5.5.3.2 To that end (and in line with CBI's section 43 power to do so), we suggest that the existing list of authorised investment classes at paragraphs (a) to (f) be revisited with a view to including the following:

g. social housing;

h. State guaranteed projects;

i. centralised lending [e.g. mortgages, SMEs];

j. corporate bonds;

k. such other classes as may be approved by the Bank.

5.6 Issue 6 - Proposed maturity limits for investments.

5.6.1 Comments

The proposed 10 year maximum for investments is unlikely to be sufficient for all required investment activities e.g. social housing and centralised lending.

5.6.2 Suggestions

Revisit the 10 year maximum and in line with a review of the list of authorised investment classes.

6. Savings (Section 9 of CP88)

(v) Do you have any comments on the draft savings regulations? If you have suggestions please provide them along with the supporting rationale.

Summary of Issues

1. Proposed reduction of the statutory savings limit.
2. Retention of requirement that a credit union's total deposits cannot exceed total shares.

6.1 Issue 1 - Proposed reduction of the statutory savings limit.

6.1.1 Comments

6.1.1.1 We note the proposal to reduce the statutory savings maximum (shares plus deposits) per member from the greater of €200,000 or 1% of total assets (which could include deposits up to €100,000) to €100,000.

6.1.1.2 We are surprised that CBI has made this proposal given its statutory mandate under section 84 which requires that the Registrar "*administer the system of regulation and supervision of credit union with a view to [...] the maintenance of the financial stability and well-being of credit unions generally*".

6.1.1.3

[REDACTED]

7.

6.1.1.4 The limited rationale for the proposed change (as articulated at page 45 of CP88) is:

"This requirement seeks to ensure credit unions' funding is sufficiently diversified while also protecting members' savings."

6.1.1.5 In order to understand the impact of what is being proposed (which is not clear from the Regulatory Impact Analysis – see comments at page 36 of this document) and the extent of same, we conducted our own analysis which follows.

[REDACTED]

Analysis of Impact of Proposed New Savings Maximum

As of today's date:

- **54% of our member credit unions (200 in total) have at least one account with a balance in excess of €100,000.**
- **2,932 members of affiliated credit unions hold accounts with balances in excess of €100,000.**
- **Total savings in these accounts total €417 million which equates to 3.9% of total savings.**

	Number of CUs	% of CUs
50 accounts or more > €100,000	10	3%
20-50 accounts > €100,000	25	7%
10-20 accounts > €100,000	31	8%
5-10 accounts > €100,000	31	8%
Less than 5 accounts €100,000	103	28%

- **We would have to presume that a portion of these savings would be lost to the system. Depending on withdrawal patterns, the amounts could be significant.**
- **Savings fell in 2012 but rebounded and grew by 1.1% in 2013 and 1.7% in 2014.**
- **Withdrawal of a significant portion of the effected €417 million would effectively wipe out this recent growth.**

6.1.2 Suggestions

6.1.2.1 The rationale for the proposal to restrict credit unions in this manner is not clear.

6.1.2.2 What is the rationale for proposing to impose a savings limit on a movement with:

- €2.0 billion in capital;
- 216 credit unions with capital above 15%; and
- €670 million in loan provisions?

6.1.2.3 Please clarify the following:

- a. which other financial institutions/participants in the Deposit Guarantee Scheme/beneficiaries of the Government's blanket guarantee are subject to a similar limit;
- b. that CBI is satisfied that the proposal to impose such a limit on credit unions does not fall foul of competition law considerations;
- c. whether CBI accepts that it may not be possible to force a member to withdraw savings (within 6 months or any other timeframe) and so, CBI may be attempting to provide for something in Regulation which could be beyond the control of the credit union thereby placing it in breach of the new restriction through no fault of its own and that, in this way, what is being proposed is potentially unworkable; and
- d. the process CBI would expect a credit union to follow in order to pay a dividend to members who have already reached the proposed maximum of €100,000.

6.1.2.4 We suggest that CBI retains the existing limits and, if it is deemed to be necessary, encourages credit unions to consider any appropriate limits (specific to the circumstances of that particular credit union) within the statutory maximum as part of its overall ALM and business considerations.

6.1.2.5 We will be glad to do likewise and will undertake to circulate guidance in this area.

6.2 Issue 2 - Retention of requirement that a credit union's total deposits cannot exceed total shares.

6.2.1 Comments

6.2.1.1 The rationale for retaining the provision is not evident from CP88.

6.2.1.2 Where a credit union is offering fixed rate loans of any descriptions (including home loans) it should have the ability to match this asset with a fixed rate liability. The only way to achieve this within the credit union itself i.e. without having to resort to external sources of funding, is by way of deposit taking.

6.2.1.3 We are unconvinced of the continued advisability of the provision given the overarching necessity for cohesive ALM by credit unions. This is particularly so in circumstances where a credit union may wish to move more towards a primarily deposit based savings model.

6.2.2 Suggestions

6.2.2.1 Please clarify the rationale for retaining this provision.

6.2.2.2 CBI to revisit the issue having regard to the requirement for deposit taking to support certain lending and the overarching necessity for cohesive ALM by credit unions.

6.2.2.3 The necessity for credit unions to be able to match fixed rate loans (such as home loans) to fixed rate liabilities without having to use external sources of funding should be examined in detail by the *Working Group on CU House Loans*.

7. **Borrowing (Section 10 of CP88)**

(vi) Do you have any comments on the draft borrowing regulations? If you have suggestions please provide them along with the supporting rationale.

Summary of Issues

1. Proposed reduction of the maximum a credit union can borrow.

7.1 Issue 1 - Reduction of the maximum a credit union can borrow.

7.1.1 Comments

7.1.1.1 We note the proposal to reduce the maximum a credit union can borrow from 50% of aggregate savings to 25% of aggregate savings.

7.1.1.2 Our analysis of the impact of the proposed change illustrates that borrowing activity is currently low but we have some concern that this reduction could cause future problems where inter CU lending/borrowing may become more commonplace.

7.1.1.3 No clear rationale for the change is provided other than to state that only a small number of credit unions commented on it in CP76 submissions and that less than 5% of credit unions have borrowings (the totality of which represents less than 6% of aggregate savings). We would be concerned if this is an indication of any future approach to regulation making by CBI i.e. that unless existing limits are used to the full, they will be lost.

7.1.2 Suggestions

7.1.2.1 Given that it is not anticipated that the reduction would cause any immediate problems for credit unions, we would suggest that its operation be noted for consideration as part of an overall review of the Regulations (see page 35 of this document).

8. Systems, Controls and Reporting Arrangements (Section 11 of CP88)

(vii) Do you have any comments on the draft regulations on systems, controls and reporting arrangements? If you have suggestions please provide them along with the supporting rationale.

Summary of Issues

1. Performance of the loan book and other disclosures.

8.1 Issue 1 - Performance of the loan book and other disclosures.

8.1.1 Comments

8.1.1.1 The rationale for the proposed change (as articulated at page 52) is:

“The draft regulations also contain a number of reporting and disclosure requirements in relation to reserves, lending and investments which will provide increased transparency to credit union members in credit unions’ annual accounts” (at page 52).

8.1.1.2 Given the wide availability of credit unions’ AGM booklets and annual accounts e.g. on public sections of websites, it is unlikely that the transparency referenced above will be provided only to members.

8.1.1.3 What is the perceived benefit of circulating detail on the performance of the loan book and related party lending outside the credit union?

8.1.2 Suggestions

8.1.2.1 Please clarify:

- i. The precise form any such disclosures would take.
- ii. Whether CBI has any concerns around that level of information being widely available.

9. Services Exempt from Additional Services Requirement (Section 12 of CP88)

(viii) Do you have any suggestions on additions, amendments or deletions to the services and related conditions that are included in the draft regulations? If you have suggestions please provide them along with the supporting rationale. It should be noted that any further services proposed to be included in the regulations must not involve undue risk to members' savings, the financial stability of the credit union or the operational capability of the credit union.

9.1 Existing Regulations

Our files around the process of engagement which led up to the making of the *Credit Union Act 1997 (Exemption from Additional Services Requirements) Regulations 2004* illustrate that it took some 18 months and ongoing meetings to complete and agree wording for inclusion. As such, it has not been possible to progress to that point within the timeframe provided for responses to CP88.

9.2 Process of Review

We will be glad however to engage in a process with CBI of reviewing the existing Regulations with a view to their enhancement. In our recent engagement with them on this issue, member credit unions have raised Safety Deposit Boxes and Event Tickets as items for further discussion.

9.3 Necessary Amendments

We would highlight the following areas as requiring particular review and discussion at this time:

- 1. Transactional/Current Accounts; and**
- 2. Debit Cards (both Pre Paid and Full Service).**

These items will be vital in enabling credit unions adapt to far reaching developments in financial services technologies so that they meet members requirements in those areas.

In addition, it would assist Government in progressing its financial inclusion agenda if credit unions were authorised to offer suitable accounts under the Government's *National Payments Strategy*.

10. Timelines (Section 13 of CP88)

(ix) Do you agree with the proposed timelines for the introduction of the draft regulations set out in this consultation paper, in particular the transition period proposed between the publication and commencement of the regulations? If you have other suggestions please provide them, along with the supporting rationale.

10.1 It will be necessary to see CBI's responses to the significant issues raised in this submission (and those from all other contributors) before we can reasonably be expected to provide a view as to whether we agree with the proposed timelines.

10.2 In this regard, we do not agree that the final regulations should be published alongside CBI's feedback statement in June 2015 as appears to be proposed by CP88 (at page 64) which states:

June 2015 Publish feedback statement and final regulations

10.3 Paragraphs 13 and 14 of CBI's *Consultation Protocol for Credit Unions* provide the following:

13. *The Central Bank will publish a feedback statement outlining how significant comments from the consultation process have been dealt with.*

14. *The Central Bank will issue final regulation to all credit unions and will advise them of the commencement date of such regulations. All final regulations will be published on the Central Bank website.*

10.4 CP88 appears to suggest that these separate steps will be taken simultaneously – please confirm if that is CBI's intention.

11. Further Issues for Consideration

11.1 Review Clause

11.1.1 Comments

We note the following provision of the *Personal Insolvency Act 2012*:

141. – (1) The Minister shall, in consultation with the Minister for Finance, not later than 3 years after the commencement of this Part, commence a review of its operation.

(2) A review under subsection (1) shall be completed not later than one year after its commencement.

(3) Having completed the review the Minister in consultation with the Minister for Finance shall prepare a report setting out the assessment arrived at and the reasons for that assessment.

(4) The Minister shall lay a copy of a report prepared under subsection (3) before each House of the Oireachtas as soon as reasonably practicable after it has been completed.

11.1.2 In circumstances where the financial services system in the Republic of Ireland continues to operate with ongoing uncertainty and concern, it is vitally important that the Regulations make clear provision for review within a designated period.

11.2 Suggestions

11.2.1 To that end, we believe that it is wholly in line with its statutory mandate in respect of credit unions that CBI include the following provision in these Regulations:

(1) The Bank shall, in consultation with the credit union sector, not later than 2 years after the commencement of these Regulations, commence a review of their operation.

(2) A review under subsection (1) shall be completed not later than six months after its commencement.

(3) Having completed the review the Bank shall prepare a report setting out the assessment arrived at and the reasons for that assessment.

- (4) *A copy of a report prepared under subsection(3) shall be provided to each credit union registered in the State and to such other bodies as appear to the Bank to be expert or knowledgeable in matters relating to credit unions as soon as reasonably practicable after it has been completed.*

11.2 Regulatory Impact Analysis

11.2.1 Comments

- 11.2.1.1 Our understanding of an RIA is that it, in part, *“helps to identify any possible side effects or hidden costs associated with regulation and to quantify the likely cost of compliance on the individual citizens or the business”*⁸.
- 11.2.1.2 In this regard, the Regulatory Impact Analysis provided as part of CP88 has not been helpful in assisting our understanding of what the possible side effects, the costs (either hidden or obvious) and the actual impact of the proposed new Regulations on our member credit unions would be if brought into effect.
- 11.2.1.3 In the absence of such an analysis from CBI, we have had to conduct our own. One of a number of unsatisfactory elements of this is that we cannot present our members with a movement wide picture (given that our available data relates only to affiliated credit unions). This work should be conducted by CBI and not left to a representative body to carry out in respect only of its own membership.
- 11.2.1.4 We note the following extract from the Final Report of the Commission on Credit Unions:

“When setting out new Regulations, the Commission recommends that the Central Bank undertakes a Regulatory Impact Analysis (RIA) in line with existing requirements and having regard to international best practice”.

We are disappointed that CBI has not seen fit to comply with the Commission’s clear recommendation around RIAs. This is particularly so in circumstances where CBI has operated to the letter of the Commission report in other areas.

11.2.2 Suggestions

- 11.2.2.1 We have provided the following documents along with this submission in order to illustrate our understanding of the Commission’s reference to *“international best practice”* in the context of regulation making for credit unions:

⁸ Page 3, *Revised RIA Guidelines : How to Conduct a Regulatory Impact Analysis*, Roinn an Taoiseach, June 2009

i. Strengthening Accountability in Banking: A New Regulatory Framework for Individuals (FCA CP 14/13, PRA CP 28/14).

The purpose of this consultation paper was to put forward proposals relating to a new regime for Approved Persons in regulated firms and includes a cost benefit analysis at pages 62-69.

As part of the analysis the issue of compliance costs (both once off and ongoing) were addressed as well as the indirect costs and wider impacts on the firms affected by the proposals.

Crucially, the FCA commissioned *Europe Economics* (an independent specialist economics consultancy) to assist in assessing the likely impacts arising from the proposals (their report is also provided).

ii. CP 11/17 FSA Regulation of Credit Unions in Northern Ireland

The purpose of this CP was to set out regulations for credit unions in Northern Ireland in light of the transfer of responsibility for their regulation from the Department of Enterprise, Trade and Investment (Northern Ireland) to the Financial Services Authority (FSA).

See in particular Annex 3 (pages 77- 101) which again includes extensive detail relating to the potential costs and impacts on credit unions as a result of the proposals.

iii. Integrated Mortgage Disclosures Under the Real Estate Settlement Procedures Act (Regulation X) and the Truth In Lending Act (Regulation Z); Proposed Rule

This consultation document issued by the US Bureau of Consumer Financial Protection sets out proposed rules relating to mortgage disclosures. The CP is interspersed with analysis of the costs of the proposals including once off and annual burdens (see for example pages 185-188).

The document is available at:

<http://www.gpo.gov/fdsys/pkg/FR-2012-08-23/pdf/2012-17663.pdf>

- 11.3 **We would emphasise the importance of CBI providing all relevant detail to credit unions when exercising its regulation making power into the future and providing a clear analysis of the potential cost impact on credit unions and the possible impact on the future of the credit union movement which would result from implementation proposals.**

12. Conclusion

- 12.1 Given the complexity and wide range of issues covered by these draft Regulations, we would again caution against the publication of the final regulations alongside the Feedback Statement.
- 12.2 At a minimum, credit unions and stakeholders should have an opportunity to consider the likely contents of the Final Regulations (as illustrated by the Feedback Statement) prior to being asked to confirm whether or not the timeframes being suggested are sufficient to enable them alter systems, policies, and procedures to ensure compliance. Credit unions will have to know precisely what they will be expected to be compliant with before they can reasonably be expected to answer those questions.
- 12.3 We look forward to the publication of all submissions received and CBI's feedback on same which we will consider and analyse carefully.
- 12.4 In the interim, a League delegation will be available to meet to discuss any of the matters raised in this submission.