Banc Ceannais na hÉireann
Central Bank of Ireland
Eurosystem

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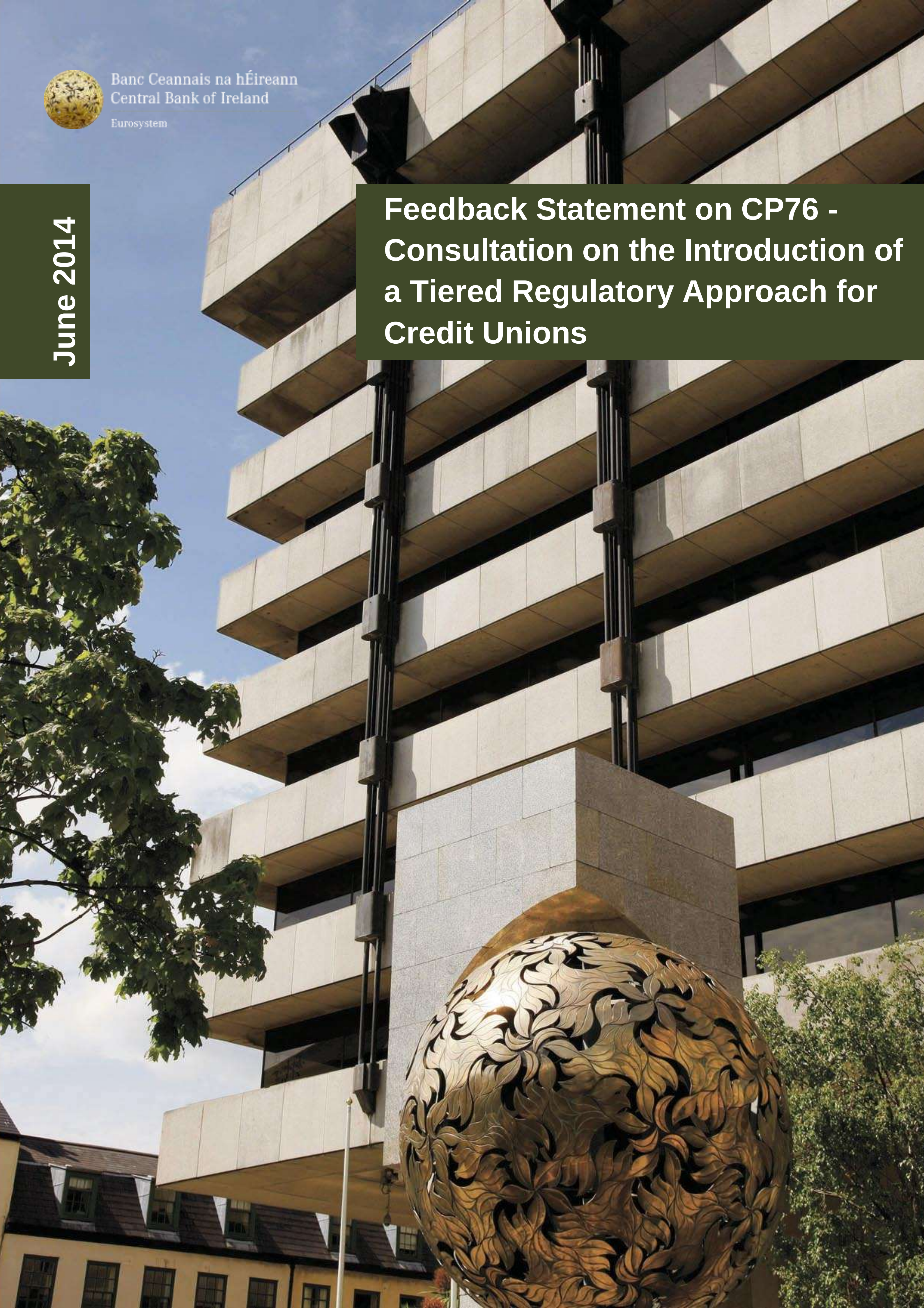
Feedback Statement on CP76 - Consultation on the Introduction of a Tiered Regulatory Approach for Credit Unions



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1. Introduction

On 23 December 2013 the Central Bank of Ireland ("the Central Bank") published Consultation Paper 76 - Consultation on the Introduction of a Tiered Regulatory Approach for Credit Unions ("CP76").

CP76 set out the Central Bank's proposed approach to tiered regulation arising from the recommendations contained in the Report of the Commission on Credit Unions[1], which included a recommendation that regulation should be proportionate to the nature, scale and complexity of the credit union.

CP76 posed six specific questions for respondents to address. The original closing date for submissions was 28 February 2014. Following a request from a sector stakeholder this closing date was extended by one month to 31 March 2014. 164 submissions were received in response to CP76. The Central Bank would like to thank all parties who took the time to make a submission on CP76 to inform the policy development process. The submissions received can be broken down as follows:

- 140 from 143 credit unions[2]
- Five from credit union chapters
- Five from credit union bodies
- 14 from others (including professional bodies and individuals)

All submissions received are available on the Central Bank website at the following link.

This paper summarises the feedback received on CP76 and sets out the Central Bank's considered decisions. It is intended to be read in conjunction with CP76 and makes reference to proposals and terms used in the original consultation document which can be found on the Central Bank's website at the following link.

Section 2 of this feedback statement provides an overview of the key messages from the submissions received, a summary of the Central Bank's responses to these messages and an outline of the proposed next steps. Section 3 of this feedback statement provides details on the individual questions posed in CP76 and the proposals in CP76, together with a summary of the responses received to each question and the Central Bank's response.

This feedback statement is published to promote understanding of the policy formation process within the Central Bank and is for information purposes only. This document does not alter legal or regulatory requirements for credit unions. This document does not constitute legal advice and should not be used as a substitute for such advice. It is the

[1] Report of the Commission on Credit Unions (March 2012), available at the following link.
[2] A number of joint submissions were received from credit unions.

responsibility of all credit unions to ensure their compliance with legal and regulatory requirements.

2. Key Messages and Summary of Central Bank Response

2.1 Purpose of Consultation

Following on from the introduction of the strengthened regulatory framework for credit unions, the Central Bank is seeking to facilitate the prudent development of the credit union sector within an appropriate regulatory framework.

Arising from the recommendations of the Commission on Credit Unions regarding a tiered regulatory approach, the Central Bank undertook an initial consultation to seek views from credit unions and sector stakeholders on the proposals for a tiered regulatory approach for credit unions, including the services and activities to be undertaken in each tier.

CP76 proposed a tiered regulatory approach that would allow credit unions to:

- continue to undertake services and activities comparable to those that credit unions are currently undertaking within the strengthened regulatory framework; and
- allow credit unions that are capable of and wish to undertake a wider range of services and activities to do so, subject to additional regulatory requirements.

Views were sought in the following areas:

- the tiered regulatory approach proposed for credit unions;
- the introduction and on-going operation of the proposed tiered regulatory approach;
- the activities, services and related requirements proposed for each tier;
- the development of a provisioning framework for the credit union sector; and
- the timelines, including the most appropriate time for the introduction of a tiered regulatory approach.

2.2 Key Messages

A number of the key messages that emerge from the feedback provided on CP76 are set out below.

Timing

CP76 proposed that the timing of the introduction of a tiered regulatory approach would need to be considered in light of the significant changes required in credit unions to implement the strengthened regulatory framework and the voluntary restructuring of the sector that is currently underway. Overall, the feedback received on CP76 on timing indicates that a majority of respondents are of the view that a tiered regulatory approach should not be introduced at this time given the amount of change the credit union sector is currently undergoing.

Number of Tiers

CP76 proposed a two category approach to the introduction of a tiered regulatory approach for the credit union sector. A small number of respondents agree with the proposals set out in CP76. However, a large number of respondents do not agree with two tiers as proposed in CP76. Of these, a number suggest that there should be three or more tiers. However, respondents do not set out the activities and services that should be provided by credit unions in each tier or put forward views on how the sector should develop. A limited number of respondents are of the view that no tiering is required.

Operation of Tiers

The proposals for the operation of tiers within a tiered regulatory approach set out in CP76 took account of the proposals set out in the Report of the Commission on Credit Unions and the services and activities that credit unions currently undertake. Proposals for smaller credit unions were less restrictive than proposed by the Commission on Credit Unions.

A substantial number of respondents indicate that the proposals set out in CP76 were too restrictive with a significant number indicating that these proposals are an attempt by the Central Bank to micromanage the sector, mainly in the areas of lending, investments and savings. In addition, some submissions make reference to an expectation that smaller credit unions would be subject to reduced requirements under a tiered regulatory approach which they indicate is not reflected in the proposals contained in CP76.

Additional Services[3]

CP76 asked what new additional services credit unions wish to offer their members. While some respondents provide feedback on new additional services that credit unions would wish to offer, the majority of respondents do not. The services that are most frequently referred to, such as debit cards and Electronic Funds Transfers (EFT) are services that credit unions can already undertake[4]. A small number of further additional services are also referred to in a limited number of submissions.

Provisioning

Comments provided on provisioning are mixed. The majority of respondents who comment on the proposed provisioning framework are of the view that there is a need for a provisioning framework to provide clarity and consistency in the manner in which credit unions calculate provisions, while others indicate that the existing provisioning framework is adequate.

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[3] This includes services provided to members beyond the core services of lending and savings.
[4] Schedule items 2 and 3 of S.I. No 223 of 2004 permit credit unions to offer EFT services to facilitate transfers to or from a member’s account and ATM services to facilitate withdrawals from a member’s account.

2.3 Central Bank Response

The Central Bank has given detailed consideration to the submissions received and the feedback has influenced the proposed approach in areas such as:

- the timing of the introduction of a tiered regulatory approach;
- limits on investments and limits on lending to restricted persons;
- proposals on additional services; and
- further engagement with the credit union sector on the development of the regulatory framework for credit unions.

Timing

The Central Bank notes the feedback received on the proposed timing of the introduction of a tiered regulatory approach and acknowledges the amount of change in the credit union sector at this time, arising from the introduction of the strengthened regulatory framework and the voluntary restructuring of the sector. Having considered the feedback received on timing, while the Central Bank is not proposing to introduce a two tiered regulatory approach for credit unions at this stage, the Central Bank is proposing to take a number of steps in relation to the development of the regulatory framework for credit unions. The proposed next steps are set out below in Section 2.4.

Number of Tiers/Operation of Tiers

Submissions received suggest that there is a wide range of views among respondents on the specific scope and purpose of a tiered regulatory approach, in particular on the number and operation of tiers.

A substantial number of respondents are of the view that the limits proposed in CP76 for the two tiers are restrictive. However, this contrasts with the number of submissions that suggest that there should be three or more tiers as the introduction of additional tiers would involve the introduction of specific limits and requirements for each tier resulting in a more prescriptive and restrictive regulatory framework for credit unions.

It is also important to recognise that an element of tiering has already been introduced in the existing regulatory framework as a number of requirements of the strengthened regulatory framework apply in proportion to the nature, scale and complexity of the business being undertaken by the credit union. Additionally, key limits in the regulatory framework, such as large exposure limits for lending and savings, are related to asset size and tier in accordance with the scale of the credit union.

Some submissions indicate that there should be reduced requirements for smaller credit unions. However, submissions from smaller credit unions do not indicate that they wish to operate a simpler model as proposed for Type 1 credit unions in the Report of the

Commission on Credit Unions. The proposals contained in CP76 for the operation of category 1 credit unions do not introduce any significant new requirements for smaller credit unions and allow smaller credit unions to undertake a wider range of services and activities than was proposed in the Report of the Commission on Credit Unions[5]. In addition, while the requirements of the strengthened regulatory framework for credit unions are set out in legislation and cannot be removed for smaller credit unions, a number of these requirements are effectively reduced where a smaller credit union operates a simpler business model as these requirements apply in proportion to the nature, scale and complexity of the business being undertaken by the credit union.

Having regard to the new strengthened regulatory framework introduced by the Credit Union and Co-operation with Overseas Regulators Act 2012 ("the 2012 Act"), the Central Bank considers a two tier approach is consistent with the recommendations of the Commission on Credit Unions.

Additional Services

Some submissions make suggestions on additional services for credit unions. The majority of services referred to in the submissions received can currently be provided under the existing regulatory framework. Submissions that make reference to additional services do not provide detailed proposals on how such additional services would be developed and implemented.

While the Central Bank is not proposing to introduce a tiered regulatory approach at this time, the Central Bank is, in principle, supportive of credit unions developing additional services. The Central Bank will consider proposals from credit unions on new additional services they wish to provide to members where the credit union can demonstrate that:

- the proposed additional service is supported by a robust business case;
- the proposed additional service is not contrary to financial services legislation;
- the board of directors has a sound appreciation of the nature of the additional service proposed and is fully informed of the strategic, governance, risk management, operational, financial and legal implications involved; and
- systems and controls are in place to ensure any risks involved in the provision of the additional service are managed and mitigated.

Provisioning

In relation to provisioning, as set out in CP76 the Central Bank is proposing to develop a provisioning framework for all credit unions in order to ensure consistency and clarity in the manner in which credit unions calculate provisions.

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[5] E.g. the Report of the Commission on Credit Unions proposed that savings for Type 1 credit unions would be limited to the lower of a specified % of assets and €50,000 while CP76 proposed a savings limit of €100,000.

2.4 Proposed Next Steps

The next steps proposed in CP76 were the publication in June 2014[6] of a feedback statement and a second consultation paper, including regulations and a Regulatory Impact Analysis ("RIA"), on the details of the tiered regulatory approach.

In light of the feedback received, the Central Bank does not propose to introduce a tiered regulatory framework for credit unions at this time. The Central Bank is of the view that it is appropriate to undertake a process of further communication, engagement, clarification and consultation with the credit union sector prior to taking a decision to introduce a tiered regulatory approach for credit unions.

This engagement will help inform the Central Bank in developing the regulatory framework for credit unions to facilitate the prudent development of the credit union sector.

In order to maintain momentum in the development of the regulatory framework for credit unions a number of steps, set out below, are proposed. The steps take account of the recommendations of the Commission on Credit Unions, the enactment of the 2012 Act and on-going engagement with the credit union sector.

- Complete the introduction of the strengthened regulatory framework applicable to all credit unions by **developing regulations** for the sector under the regulation making powers contained in the 2012 Act. These regulations will contain a set of requirements that will apply to all credit unions including regulations on lending, savings, investments, borrowings, liquidity and reserves, and will take account of the existing regulatory framework and feedback received on CP76. Further details are provided in Section 3.
- **Publish a consultation paper**, including a Regulatory Impact Assessment ("RIA"), on the draft regulations.
- **Undertake a programme of nationwide information seminars** to inform and engage with credit unions on the proposed new regulations and the next steps in developing the regulatory framework for credit unions.
- **On-going engagement** and consultation with credit unions and other sector stakeholders on the prudent development of the credit union sector and the regulatory framework for credit unions.

In relation to provisioning, the Central Bank proposes to develop the provisioning framework for credit unions as a separate work stream. This framework will apply to all credit unions and will be based around developing the high level proposals contained in CP76. It is intended that draft guidance on provisioning for credit unions will be published

[6] Takes account of one month extension to the consultation period.

by end December 2014. The publication of draft guidance on provisioning will provide credit unions and other sector stakeholders with an opportunity to provide comments and feedback on this guidance prior to final publication.

The table below provides a summary of the proposed next steps and timelines.

New Regulations	
Date	**Step**
End September 2014	Publish Consultation Paper including draft regulations and RIA
October 2014	Conduct Information Seminars
End December 2014	Consultation period closes
February 2015	Publish feedback statement and final regulations
February - August 2015	Transition period
August 2015	Regulations come into force
On-going	On-going engagement and consultation with the credit union sector on the development of the regulatory framework

Provisioning	
Date	**Step**
December 2014	Publish draft guidance on provisioning
December 2014 – March 2015	Feedback period
June 2015	Publish final guidance on provisioning

3. Responses to Questions Posed in CP76

3.1 Proposed Tiered Regulatory Approach for Credit Unions

Question (i)

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.

3.1.1 Proposals set out in CP76

In CP76 the Central Bank proposed a two category approach to the introduction of a tiered regulatory approach for the credit union sector. The proposed approach took account of the recommendations of the Report of the Commission on Credit Unions and the recently introduced strengthened regulatory framework that applies to all credit unions. This approach allows for the prudent development of the sector within an appropriate regulatory framework.

Category 1

Under the proposed approach, category 1 credit unions could offer services comparable to those currently being offered by the majority of credit unions. Given that the requirements of the strengthened regulatory framework take account of nature, scale and complexity, where a credit union operates a more limited business model (e.g. the business model proposed for Type 1[7] credit unions in the Report of the Commission on Credit Unions), these requirements will automatically apply in a proportionate manner.

Category 2

Credit unions that are capable of and wish to undertake a wider range of activities and services could apply to become a category 2 credit union. Category 2 credit unions would be subject to additional regulatory requirements to take account of the additional level of risk.

3.1.2 Submissions

Number of Tiers

A small number of respondents agree with the proposals set out in CP76. However, a large number of respondents do not agree with two tiers as proposed in CP76, with a number of respondents proposing three or more tiers, while a limited number of respondents are of the view that no tiering is required. A limited number of credit unions suggest that tiers should cater for specific business models within the credit union sector. Where submissions propose three tiers, many make reference to the proposals of the Report of the Commission on Credit Unions but do not provide details on the activities

[7] The Report of the Commission on Credit Unions proposed that credit unions with assets of less than €10m would be Type 1 credit unions.

and services that should be provided in each tier. In addition, some submissions make reference to an expectation that smaller credit unions would be subject to reduced requirements under a tiered regulatory approach which they feel was not reflected in the proposals contained in CP76.

Asset Size

Some respondents disagree with the use of asset size as proposed in CP76 to categorise credit unions. It is suggested that using €100m as a cut-off point would prevent some credit unions with the capability to operate as a category 2 credit union from doing so. However, other submissions acknowledge that asset size should be one of the factors in determining categorisation. Some submissions suggest that the asset bands proposed by the Commission on Credit Unions should be used while a limited number of other submissions propose alternative asset bands.

Application Process

A small number of submissions comment on the application process, with a limited number suggesting that categorisation should be automatic, based on asset size and/or other information available to the Central Bank (e.g. through Probability Risk and Impact System ("PRISM") engagements). A limited number of submissions also suggest that PRISM should be used to categorise credit unions for the purposes of tiering.

3.1.3 Central Bank Response

Number of Tiers

Submissions received suggest that there is a wide range of views among respondents on the specific scope and purpose of a tiered regulatory approach, in particular on the number and operation of tiers. A number of submissions suggest that there should be three or more tiers. However, the introduction of additional tiers would involve the introduction of specific limits and requirements for each tier resulting in a more prescriptive and restrictive regulatory framework for credit unions. This is not consistent with the view expressed in a substantial number of submissions that the limits proposed in CP76 for the two tiers are restrictive (more detail on the feedback received in relation to the operation of the tiers is set out in Section 3.2).

Tiering within the existing regulatory framework

The strengthened regulatory framework contains a comprehensive set of governance and prudential requirements that apply to all credit unions. However, within this regulatory framework the requirements provide that the arrangements put in place in each credit union should take account of the nature, scale and complexity of the business being undertaken. In addition, key limits in the existing regulatory framework, such as large exposure limits for lending and savings, are related to asset size thereby facilitating a degree of tiering within the strengthened regulatory framework.

Business Models

A limited number of respondents indicate that tiers should reflect the specific business models undertaken by credit unions. The Central Bank considers that a regulatory framework should set out prudential and governance requirements that have the flexibility to facilitate a number of business models from which each credit union can choose, rather than prescribing a separate regulatory framework for each business model.

Smaller Credit Unions

The proposals contained in CP76 for the operation of category 1 credit unions did not introduce any significant new requirements for smaller credit unions and allowed smaller credit unions to undertake a wider range of services and activities than was proposed in the Report of the Commission on Credit Unions. For example, the Commission on Credit unions proposed that Type 1 credit union investments be limited to bank deposits with a maximum maturity of one year and Type 1 credit union lending be limited to a maximum term of five years. The wider range of services proposed in CP76 is considered appropriate in light of the comprehensive set of requirements, including detailed governance and risk management requirements, which now apply to all credit unions under the strengthened regulatory framework. Additionally the Central Bank notes that submissions from smaller credit unions do not indicate that they wish to operate a simpler model as proposed for Type 1 credit unions in the Report of the Commission on Credit Unions.

While the regulatory framework takes account of nature, scale and complexity it does not facilitate the removal of certain requirements for smaller credit unions. Where smaller credit unions wish to operate a more restricted business model, as proposed by the Commission on Credit Unions for Type 1 credit unions, they can do so as the governance and prudential requirements of the new strengthened regulatory framework apply in a manner proportionate to the business being undertaken, taking account of nature, scale and complexity. Therefore these requirements would effectively be reduced for smaller credit unions operating such a model.

Summary

As envisaged by the Commission on Credit Unions, under proposals contained in CP76 larger credit unions that are capable of and wish to operate on a more sophisticated basis would be permitted to do so. Under the proposals set out in CP76, category 1 supported the Type 1 and Type 2 credit unions proposed in the report and category 2 is comparable to Type 3. Having regard to the introduction of the new strengthened regulatory framework introduced by the 2012 Act, the Central Bank considers that a two tier approach is consistent with the recommendations of the Commission on Credit Unions.

Asset Size

The Central Bank notes the variety of comments on the use of asset size to categorise credit unions for the purposes of a tiered regulatory approach. The Central Bank considers that a certain scale is necessary to undertake a more complex business model and therefore asset size should be an important element in categorising credit unions for the purpose of tiered regulation. CP76 indicated that in general, credit unions that apply to become category 2 credit unions would have assets close to or above €100m.

Application Process

Credit unions should have the flexibility to determine the tier in which they wish to operate. Where a credit union wishes to operate in a higher tier, and is capable of doing so, they should make an application to the Central Bank, rather than it being a matter for the Central Bank to decide on which credit unions should be categorised as category 2.

PRISM is a risk-based framework for the supervision of regulated firms under which entities with the ability to have the greatest impact on financial stability and the consumer receive a higher level of supervision. The assessment as to which tier a credit union should be permitted to operate within should ultimately be linked to their ability to conduct more complex business and meet the additional regulatory requirements associated with undertaking that business, as opposed to being linked to their impact category in PRISM. There is no direct correlation between the impact category assigned through PRISM and the ability of a credit union to conduct more/less complex business in a manner which protects members' interests.

Summary

As set out in Section 2, in light of the feedback received on the timing of the introduction of a tiered regulatory framework, the Central Bank does not propose to introduce a two tiered regulatory approach for credit unions at this stage of the process. This will facilitate further discussion and consultation with the sector on the scope, purpose and operation of a tiered regulatory approach.

3.2 Operation of the Tiers

Question (ii)

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.

3.2.1 Proposals set out in CP76

The table below provides a high level summary of the activities, services and requirements that were proposed for category 1 and category 2 credit unions in CP76. Further details on the specific proposals are contained in section 5 of CP76.

	Category 1 Credit Unions (Type 1 / Type 2)	Category 2 Credit Unions (Type 3)
Lending	• Personal lending, limited commercial lending, community lending and lending to other credit unions. • Existing maturity limits – maximum loan term 15 years. • Other lending limits based on reserves. • Large exposure limits / restricted persons limits.	• Personal lending, less restrictive commercial lending, limited community lending and lending to other credit unions. • Existing maturity limits with existing longer term lending limits and consideration of a specific class of home loan. • Other lending limits based on reserves. • Large exposure limits / restricted persons limits.
Investments	• Bank deposits, Irish and EEA State Securities and shares / deposits of other credit unions. • Concentration and counterparty limits related to reserves. • Maximum maturity five years. • Investment committee.	• Bank deposits, Irish and EEA State Securities, shares / deposits of other credit unions, bank bonds and corporate bonds. • Concentration and counterparty limits related to reserves. • Maximum maturity 7 / 10 years, depending on type of investment. • Investment committee.
Savings	• Limited to lower of €100k and 1% of assets. • Total deposits to total savings ratio.	• Limited to €100k. • Total deposits to total savings ratio.
Borrowings	• Total borrowings cannot exceed 25% of total savings.	• Total borrowings cannot exceed 25% of total savings.
Additional services	• Able to provide the additional services currently available under the exemption from additional service requirements regulations. • Further additional services depending on proposals and level of complexity.	• Able to provide the additional services currently available under the exemption from additional service requirements regulations. • Further additional services depending on proposals and level of complexity.
Governance	• New governance framework in the 1997 Act.	• New governance framework in the 1997 Act. • Audit Committee, Risk Committee, Remuneration Committee and Asset and Liability Committee. • Dedicated risk management officer, compliance officer and internal audit function. • External review of the board of directors every three years.
Fitness and Probity	• As introduced from 1 August 2013[8].	• As introduced from 1 August 2013.

[8] Fitness and Probity will come into effect for credit unions with total assets less than €10m on 1 August 2015.

Reserves	• Existing approach to apply. • Assess additional reserves required for operational risk.	• Existing approach to apply. • Risk weighted approach may be considered following restructuring. • Minimum operational risk reserve requirement.
Liquidity	• Existing requirements with additional short term liquidity requirements. • Amended definition of liquid assets.	• Existing requirements with additional short term liquidity requirements. • Amended definition of liquid assets. • Consideration of additional requirements on stress tests and maturity mismatches.

3.2.2 Submissions and Central Bank Response

Overview

A substantial number of submissions view the limits in certain prudential areas (primarily lending, investments and savings limits) as restrictive, with a number of these suggesting that the Central Bank is attempting to micromanage credit unions.

Central Bank Response

The limits proposed in CP76 for the two tiered approach took account of the proposals set out in the Report of the Commission on Credit Unions and the services and activities currently undertaken by the majority of credit unions. The proposed limits were less restrictive limits than those proposed by the Commission on Credit Unions for smaller credit unions in a number of areas. The introduction of additional tiers would involve the introduction of specific limits and additional requirements for each tier resulting in a more prescriptive and restrictive regulatory framework for credit unions. The sections below set out feedback received on specific proposals contained in CP76 and the Central Bank's response to this feedback.

Lending

Classes of lending

Some submissions comment on the classes of lending in CP76 with the majority of these commenting on the definition of commercial lending. Comments suggest that the definition should be revised with a number suggesting that a distinction be made between small loans for sole traders and loans to larger commercial enterprises. There are also a limited number of comments on the requirement for a credible business plan for commercial loans with the suggestion that this would be unworkable in relation to loans for small traders.

Central Bank Response

The proposals on classes of lending contained in CP76 took account of the proposals set out in the Report of the Commission on Credit Unions and the type of lending currently undertaken by credit unions. The Commission on Credit Unions' proposals included prohibiting Type 1 credit unions from undertaking business lending and restricting Type 2 credit unions to limited business lending.

The Central Bank is proposing to define the range of classes of lending, as set out in CP76, for all credit unions. However, based on the feedback provided on the definition of commercial lending, the Central Bank is considering revising the definition of commercial lending to provide clarity to credit unions on the types of loans that should fall within the definition of commercial lending.

Concentration limits for lending

Some submissions comment on the restrictive nature of the concentration limits proposed in CP76 and suggest that the proposed limits would hinder a credit union's capacity to undertake commercial and community lending. Submissions also indicate that the imposition of concentration limits represent micromanagement of the sector and that in light of new governance and risk requirements, credit unions should be responsible for determining limits. A limited number of respondents suggest that the introduction of concentration limits would add to the complexity of managing loan books making it more difficult to monitor them on an on-going basis. A limited number of submissions query whether the application of lending limits would replace lending restrictions.

Central Bank Response

The concentration limits proposed for lending in CP76 are reflective of the lending that credit unions are currently undertaking and the Commission on Credit Unions' proposals on business lending. As set out above, in light of the feedback received it is now proposed that concentration limits will apply to commercial lending only, at this stage.

In relation to lending restrictions, such restrictions are imposed due to prudential concerns regarding a credit union's credit risk management standards and practices. The introduction of the strengthened regulatory framework should support credit unions in ensuring that they put appropriate risk and governance frameworks in place to manage and mitigate risks, including credit risk.

Maturity limits for lending

Some submissions comment on the restrictive nature of the maturity limits proposed in CP76. A limited number of respondents indicate that category 1 credit unions should be able to undertake mortgage lending while a limited number of submissions note the impact of maturity limits on the capacity to undertake mortgages and question whether it is viable for a credit union to undertake a small number of mortgages given the systems and expertise required to undertake the business. A limited number of submissions suggest that limits proposed in CP76, including maturity limits, may impact on the ability of credit unions to compete with other credit institutions. As with concentration limits, a limited number of submissions indicate that maturity limits should be a policy matter for credit unions. While a small number disagree with the proposed 15 year maximum term for personal loans, one submission indicates that a 10 year personal loan maturity is too long and not aligned with industry best practice and notes that personal loan terms should reflect the natural life of the asset.

Central Bank Response

The maturity limits proposed in CP76 took account of the proposals set out in the Report of the Commission on Credit Unions to maintain existing maturity limits for Type 2 and Type 3 credit unions. The maturity limits also reflect the lending currently being undertaken by credit unions which is well within the existing limits set out in section 35 of the Credit Union Act, 1997 ("the 1997 Act"). The maturity limits proposed in CP76 are less restrictive than those proposed by the Commission on Credit Unions for smaller credit unions.

In relation to mortgage lending, the Central Bank considers that credit unions must have appropriate systems, controls and expertise to undertake such lending and is of the view that scale is an important factor in determining whether a credit union can put these in place and offer mortgages as a viable business line.

The lending maturity limits contained in the regulatory framework are an important tool in assisting credit unions to manage the asset and liability mismatch that is inherent in the credit union model, whereby the majority of members' savings are available on demand. Therefore, the Central Bank considers it prudent to maintain the existing maturity limits contained in the 1997 Act for all credit unions (i.e. up to 30% of the loan book can be outstanding for more than five years and up to 10% of the loan book can be outstanding for more than 10 years).

Restricted person limits for lending

A large number of submissions refer to the proposed restricted person limits. Submissions indicate that these proposals are inappropriate given the community based nature of the sector. It is also suggested that these proposals could be seen as disadvantaging volunteers. Submissions suggest that creditworthiness should be the primary consideration in assessing all loans, including loans to restricted persons. A limited number of submissions, including two of the credit union bodies, suggest that governance and risk management requirements rather than limits should be used for lending to restricted persons.

Central Bank Response

The Central Bank acknowledges the community based nature of the sector and the potential impact this may have on the implementation of restricted person limits. In light of the feedback received, the Central Bank is proposing, at this stage, to set requirements on the governance (including reporting and monitoring) of lending to restricted persons rather than imposing limits on the level of lending to restricted persons.

Large exposure limits for lending

The majority of submissions do not comment on the large exposure limit for individual loans of the greater of €39,000 or 10% of the Regulatory Reserves of the credit union as proposed in CP76. However, a limited number of submissions indicate that this limit is considered to be too high.

Central Bank Response

The proposal set out in CP76 was to amend the existing large exposure limit to be based on reserves rather than total assets, thus reflecting a risk-based approach. In most cases the new proposed large exposure limit will result in a lower maximum exposure amount for credit unions than applies under the current regulatory framework. The Central Bank proposes to apply the large exposure limit as set out in CP76 and keep this limit under review.

Investments

Classes of investments

Overall, respondents indicate that the classes of investments available to both category 1 and category 2 credit unions would be too limited, with over half of the submissions commenting on the restrictive nature of the investment classes as outlined in CP76. There are a number of comments on the exclusion of collective investment schemes with many of these raising objections to the removal of collective investment schemes as a class of investment. A limited number of submissions note the potential use of collective investment schemes for investment in state projects. There were a small number of comments on the exclusion of bank bonds for category 1 credit unions. A limited number of respondents refer to the 2006 Guidance Note on Investments by Credit Unions and indicate that it should be retained as it is working well.

Central Bank Response

The classes of investments proposed in CP76 took account of the proposals set out in the Report of the Commission on Credit Unions and reflect the investments currently being undertaken by credit unions. However, the classes of investments proposed were less restrictive than those proposed by the Commission on Credit Unions.

In light of the feedback received, and taking account of the new strengthened regulatory framework now in place for credit unions, the Central Bank is proposing to set out authorised classes of investments in regulations based on the current list of authorised classes of investments as set out in the 2006 Guidance Note on Investments by Credit Unions with the exception of class 4 - investments in equities. In relation to state projects, while the Central Bank is willing to consider proposals on such projects, specific proposals have not been received to date.

Maturity limits for investments

In general, submissions indicate that maturity limits for investments proposed in CP76 are too restrictive with a significant number of submissions commenting on this. There are a small number of comments on the restrictions on investments in longer term government paper with a few of these making specific reference to 10 year Irish Government Bonds.

Central Bank Response

The maturity limits set out in CP76 took account of the proposals set out in the Report of the Commission on Credit Unions, with less restrictive limits than those proposed by the Commission on Credit Unions for smaller credit unions. The maturity limits also reflected the maturity profile of existing credit union investments.

In light of the feedback received, the Central Bank is proposing to introduce limits in regulations based on the maturity limits contained in the 2006 Guidance Note on Investments by Credit Unions, which sets a maximum maturity of 10 years for investments. However, while certain maturity limits are currently applied to specific classes of investments, consideration will be given to applying maturity limits to the full investment portfolio.

Impact on income

Over half of the submissions comment on the potential impact on income arising from the limits proposed in CP76.

Central Bank Response

Some of the concerns respondents raise in relation to income generated from investments seem to stem from credit unions' current reliance on investment income. This arises from the current make-up of credit union balance sheets which are generally weighted towards investments rather than loans. The approach to classes of investments and maturity limits the Central Bank proposes to adopt, as outlined above, is broadly in line with the existing investment framework for credit unions and therefore should address concerns raised about the impact on investment income arising from the investment limits proposed in CP76.

Counterparty Limits

Some submissions do not agree with the proposal on counterparty limits based on reserves set out in CP76. Concerns include the increased complexity involved with managing an investment portfolio on this basis given the increased number of counterparties some credit unions will need to have. A significant number of submissions comment on the impact this would have on credit union investments in domestic counterparties.

Central Bank Response

The Central Bank considers counterparty diversification an important means of managing risk. In light of feedback received, it is proposed that the existing 25% counterparty limit contained in the 2006 Guidance Note on Investments by Credit Unions will be reflected in investment regulations.

Savings

Over half of the submissions are of the opinion that a €100,000 limit on savings is too restrictive.

Central Bank Response

The savings limit proposed in CP76 took account of the proposals set out in the Report of the Commission on Credit Unions for a savings limit of the lesser of a specified percentage of assets or €50,000 for Type 1 credit unions and the lesser of a specified percentage of assets or €100,000 for Type 2 credit unions. The proposed savings limits also took account of the current savings profile of the sector.

The Central Bank is proposing to review the current savings limits for credit unions taking account of the recommendations of the Commission on Credit Unions, the feedback received on CP76 and the current savings profile of the sector.

Liquidity

A limited number of submissions, including a submission from a credit union body, comment on and welcome the new definition of liquid assets proposed in CP76. A number of submissions do not agree with the proposed additional liquidity limits set out in CP76. These submissions indicate that the limits are too prescriptive and too complex, with a number commenting on the impact the proposed limits would have on income.

Central Bank Response

The Central Bank considers it prudent that credit unions should ensure that their liquid assets contain a mix of maturities including a portion available 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 unions savings is a consideration for credit unions in ensuring they maintain appropriate short term liquidity.

In light of the feedback received, consideration will be given to reviewing the additional liquidity limits proposed in CP76.

Borrowings

There are a small number of comments on borrowings, most of which acknowledge that credit unions do not generally use borrowing as a source of funding.

Central Bank Response

The Central Bank proposes to introduce the proposals contained in CP76 in relation to borrowing.

Governance and Fitness and Probity

Submissions raise no issues in relation to Fitness and Probity. However, a small number of submissions disagree with the proposal to have a dedicated risk management officer, compliance officer and internal auditor for category 2 credit unions.

Central Bank Response

The requirement to have a dedicated risk management officer, compliance officer and internal audit function was developed in line with the proposals contained in the Report of the Commission on Credit Unions.

As required under the 1997 Act, all credit unions will continue to be required to have a risk management officer, a compliance officer and an internal audit function. In light of the feedback received, the requirement to have a dedicated risk management officer, compliance officer and internal audit function will not be introduced as a regulatory requirement at this time.

The Central Bank considers that where a credit union is undertaking more complex business it may be appropriate to have a dedicated risk management officer, compliance officer and internal audit function.

It will be a matter for individual credit unions to determine whether they should have a dedicated risk management officer, compliance officer and internal audit function taking account of the nature, scale, complexity and risk profile of the credit union. In determining appropriate resourcing arrangements credit unions should ensure that:

- all functions of the role can be effectively carried out by the proposed resourcing arrangements;
- any potential conflicts are identified and managed;

- where independence of functions is required that this is maintained; and
- all legal and regulatory requirements such as those relating to outsourcing are met.

Reserves

The majority of respondents do not comment on reserves. A small number of submissions suggest a risk weighted approach to reserves. While a limited number of respondents agree with the proposals in relation to an operational risk reserve some submissions do not agree with the proposal. A limited number of credit unions query whether existing additional reserves, in excess of the minimum reserve requirement, could be used for an operational risk reserve.

Central Bank Response

CP76 indicated that consideration will be given to a risk weighted asset approach for category 2 credit unions following restructuring of the credit union sector. This proposal will be kept under review.

On commencement of section 13 of the 2012 Act, credit unions will be required to maintain additional reserves which they have assessed as being required in respect of operational risk having regard to the nature, scale, complexity and risk profile of their business. The Central Bank is not proposing to prescribe limits in relation to the operational risk reserve in regulations at this stage. Where credit unions have existing additional regulatory reserves in excess of the minimum regulatory reserves they have assessed they are required to hold in line with regulatory requirements, these may be used to provide an operational risk reserve.

3.3 Additional Services

Question (iii)

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.

3.3.1 Proposals set out in CP76

CP76 proposed that both category 1 and category 2 credit unions would be able to provide the additional services currently available under the Exemption from Additional Service Requirements Regulations[9] which include:

- account access by phone;
- account access by internet;
- third party payments (including EFT);
- ATM services;
- bureau de change;
- certain insurance services on an agency basis;
- group health insurance;
- bill payment;
- money transfers;
- standing orders;
- direct debits;
- financial counselling; and
- PRSAs on an introduction basis.

In addition, some credit unions have been approved under section 48 of the 1997 Act to provide other services, including mortgages on a tied agency basis and some additional insurance services on a referral basis.

CP76 sought feedback on any further additional services that credit unions wish to provide to their members.

3.3.2 Submissions

While some respondents provide feedback on additional services that credit unions would wish to offer, the majority of respondents do not. The services that are most frequently referred to, such as debit cards and EFT, are services that credit unions can already

[9] S.I. 223 of 2004 - Credit Union Act 1997 (Exemption From Additional Services Requirements) Regulations 2004; S.I. 107 of 2007 - Credit Union Act 1997 (Exemption from Additional Services Requirements) Regulations 2007.

undertake within the existing framework. A few further additional services are also referred to in a small number of submissions, including revolving credit and overdraft facilities.

3.3.3 Central Bank Response

The Central Bank notes the limited feedback received on additional services and that the majority of services referred to in the submissions received can currently be provided under the existing additional services framework[10].

Where respondents provide feedback on additional services they tend to refer to additional services but do not provide detailed proposals on how additional services would be developed and implemented.

Where credit unions wish to provide services not provided for under the existing framework, the Central Bank is open to considering such proposals. The Central Bank is, in principle, supportive of credit unions developing additional services. The Central Bank will consider proposals from credit unions on new additional services they wish to provide to members where the credit union can demonstrate that:

- the proposed additional service is supported by a robust business case;
- the proposed additional service is not contrary to financial services legislation;
- the board of directors has a sound appreciation of the nature of the additional service proposed and are fully informed of the strategic, governance, risk management, operational, financial and legal implications involved; and
- systems and controls are in place to ensure any risks involved in the provision of the additional service are managed and mitigated.

[10] Subject to certain provisions, a credit union may provide, as principal or agent, additional services of a description that appears to the Registrar of Credit Unions to be of mutual benefit to its members. The Minister for Finance has enacted legislation which provides credit unions with exemptions from additional services requirements for a number of additional services subject to certain conditions.

3.4 Provisioning

Question (iv)

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.

3.4.1 Proposals set out in CP76

In line with the powers that will be available to the Central Bank, and to ensure consistency and clarity in the manner in which credit unions calculate their provisions, CP76 proposed to develop a provisioning framework for all credit unions, to reflect the following objectives:

- recognition of loan losses as early as possible within the context of accounting standards;
- adoption of a sufficiently conservative and comparable approach to the measurement and making of impairment provisions in their loan book; and
- disclosures to support members' understanding of the performance of the loan book and the credit union's credit risk management practices.

CP76 also proposed the steps to be taken by credit unions in assessing their loan books for losses and determining the appropriate provisions. It also considered setting a requirement for credit unions to provide in full for a loan that has been delinquent for a specified period. CP76 also proposed that all credit unions will be required to have a provisioning policy.

3.4.2 Submissions

A significant number of submissions provide comments on the proposals on provisioning set out in CP76. The feedback in relation to provisioning is mixed. While the majority of submissions that comment on the proposed provisioning framework welcome a revised methodology to provide clarity and consistency, a smaller number state that Resolution 49 and existing approaches are adequate. A limited number of the submissions that comment on provisioning state that more defined information is needed before an appropriate response can be made. A small number of submissions make reference to a desire for the sector to have input into the development of provisioning guidelines and that it should be developed separately to the tiered regulatory approach.

3.4.3 Central Bank Response

In light of feedback received in relation to provisioning, the Central Bank proposes to develop the provisioning framework for credit unions as a separate work stream. This framework will apply to all credit unions and will be based around developing the high level proposals contained in CP76. It is intended that draft guidance on provisioning for credit unions will be published before the end of the year. The publication of draft guidance on provisioning will provide credit unions and stakeholders with an opportunity to provide comments and feedback on this guidance prior to final publication.

The table below sets out the high level proposed timeline for the implementation of a provisioning framework for credit unions.

Provisioning	
Date	**Step**
December 2014	Publish draft guidance note on provisioning
December 2014 – March 2015	Feedback period
June 2015	Publish final guidance note on provisioning

3.5 Timing

Question (v)

Do you agree that the tiered regulatory approach should be introduced at this time? If you consider that alternative timing is more appropriate, please provide suggestions, along with the supporting rationale.

Question (vi)

If it is considered that the tiered regulatory approach should be introduced at this time, do you agree with the proposed timelines for the introduction of the tiered regulatory approach set out in section 7.1, in particular the transitional period proposed between the publication and commencement of the regulations? If you have other suggestions please provide them, along with the supporting rationale.

3.5.1 Proposals set out in CP76

CP76 noted that the timing of the introduction of the tiered regulatory approach would need to be considered in light of the significant changes required in credit unions to implement the strengthened regulatory framework and the voluntary restructuring sector that is currently under way. CP76 posed two specific questions on timing of a tiered regulatory approach.

3.5.2 Submissions

Of the many submissions that comment on timing, the majority indicate that they believe that now is not the appropriate time for a tiered regulatory approach to be introduced. The comments made include the following:

- there is a need for additional time to allow the new requirements to be fully embedded prior to the introduction of tiering;
- a tiered approach should be delayed until after ReBo has completed its work[11]; and
- the introduction of a tiered regulatory approach should be delayed by two years.

Of the submissions that comment on the timelines proposed in CP76, almost all indicate that more time would be required for the implementation of a tiered regulatory approach. The comments mainly focus on a need for an extended transitional period, along with the need for a RIA and face to face engagement with sector stakeholders.

[11] The Commission Report contains an indicative timeline that proposes the restructuring process would be completed by end Q4 2015. The legislation that established ReBo requires the Minister to carry out a review by 1 January 2016 to establish whether ReBo has completed the performance of its functions and to make an Order dissolving ReBo where this is the case.

3.5.3 Central Bank Response

Based on the submissions received in relation to timelines, the Central Bank does not propose to introduce a two tiered regulatory approach for credit unions at this stage. In light of feedback, the Central Bank is of the view that it is appropriate to undertake a process of further communication, engagement, consultation and evaluation prior to taking a decision to introduce a tiered regulatory approach for credit unions.

This will facilitate further discussion and consultation with credit unions on their proposals for the prudent development of the credit union sector. Arising from the wide range of views received in submissions on CP76, this will also provide an opportunity for the Central Bank to outline to credit unions the purpose, scope and operation of the regulatory framework and engage with credit unions on how this can support the prudent development of the credit union sector.

In order to maintain momentum in terms of the implementation of the Commission on Credit Unions' recommendations and commencement of the provisions of the 2012 Act, the Central Bank proposes the following:

- Complete the introduction of the strengthened regulatory framework applicable to all credit unions by **developing regulations** for the sector under the regulation making powers contained in the 2012 Act. These regulations will contain a set of requirements that will apply to all credit unions including regulations on lending, savings, investments, borrowings, liquidity and reserves, and will take account of the existing regulatory framework and feedback received on CP76. Further details are provided in Section 3.
- **Publish a consultation paper**, including a RIA, on the draft regulations.
- **Undertake a programme of nationwide information seminars** to inform and engage with credit unions on the proposed new regulations and the next steps in developing the regulatory framework for credit unions.
- **On-going engagement** and consultation with credit unions and other sector stakeholders on the prudent development of the credit union sector and the regulatory framework for credit unions.

Throughout these stages the Central Bank intends to engage with the credit union sector on an on-going basis to inform the development of the regulatory framework for credit unions.

The table below provides a summary of the proposed next steps and timelines.

New Regulations	
Date	**Step**
End September 2014	Publish Consultation Paper including draft regulations and RIA
October 2014	Conduct Information Seminars
End December 2014	Consultation period closes
February 2015	Publish feedback statement and final regulations
February - August 2015	Transition period
August 2015	Regulations come into force
On-going	On-going engagement and consultation with the credit union sector on the development of the regulatory framework

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