Comhar Linn
INTO CREDIT UNION

33 Parnell Square, Dublin 1.
Tel: 1850 277 377 – Fax: (01) 873 3253
Email: info@intocreditunion.ie
Web: www.comharlinnintocu.ie

Registry of Credit Unions
Central Bank of Ireland
PO Box 559
Dublin 2

31st March 2014.

RE: CP 76 *"Consultation Paper on the Introduction of a Tiered Regulatory Approach for Credit Unions"*

Dear Registrar,

On behalf of Comhar Linn INTO Credit Union Limited (CLINTO), I enclose the Credit Union's response to the recently issued Consultation Paper CP 76: *'Consultation on the Introduction of a Tiered Regulatory Approach for Credit Unions'*. The comments expressed in this letter represent the views of CLINTO and their detailed views and comments are set out in the Enclosure. At a high level, these views could be summarised as follows:

- The document is very welcome and represents a significant step forward in the necessary work of strengthening and re-vitalising the credit union sector which continues to play such a pivotal role in Irish society.
- The additional flexibility and wider risk parameters available to Category 2 credit unions, as specified in the document, are somewhat limited and, in this context, the additional governance, risk management, compliance, liquidity and reserve requirements seem disproportionate.
- There may be a case for introducing a third category of credit unions, with similar governance, risk management, compliance, liquidity and reserve requirements as Category 2, but with a higher total asset entry threshold.
- The Report of the Commission on credit unions points out that, according to the World Council of Credit Unions, Ireland is in the "Transitional" stage of development of the credit union sector due to many factors including "limited product development".
  The proposals set out in CP-76, where they are specific, appear to discourage and mitigate against the development of additional products and services for delivery to credit union members.
- There is a general lack of specificity in the document which makes it difficult to draw conclusions about many of the proposals set out.

We are grateful for your consideration of our views and are happy to meet to discuss these further should that be appropriate.

Yours sincerely,

John Carr

John Carr
Chairman

Enclosure - Detailed Responses of Comhar Linn INTO Credit Union Limited to CP 76

Number	Areas where Central Bank is Seeking Views	Detailed CLINTO Responses
(i)	Do you agree with the proposed tiered regulatory approach for credit unions?	In principle, CLINTO is not opposed to a Tiered Regulatory system. The Report of the Commission on Credit Unions includes a well-reasoned recommendation for a three-tier system which would take account of the current variations in the nature, scale and complexity of credit unions. We would question the rationale of a two tier system which would impose the same governance requirements on all Category 1 credit unions – irrespective of size. This seems to be at odds with the principle of *"regulatory requirements"* being *"proportionate to the nature, scale and complexity of the business being undertaken by the credit union"* There is no rationale for a two-tier system set out in the document.
(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?	In general, when comparing Categories 1 and 2, there appears to be significant up-front and on-going cost associated with a migration to Category 2 in terms of governance, risk control, reserves and liquidity requirements. However, the additional services which are available to Category 2 credit unions– as explicitly set out in the document – are relatively limited. Further, the criteria and approval process(es) for the provision of other additional services are not outlined. This limited additional business opportunity available to Category 2 credit unions could actively discourage credit unions from applying for approval to migrate to that category and has the potential to increase financial risk for credit unions who achieve Category 2 status but are unable to recoup the additional associated cost. We set out below comments on specific sections: **<u>5.2 Lending</u>** Additional Category 2 lending capacity set out in the document is limited and there is limited potential for

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		additional risk and, therefore, limited opportunity to increase income. We note that PPR home lending is still under "*consideration*" for Category 2 credit unions. The proposed prescribed loan-to-value and maximum maturity limits would place credit unions at a competitive disadvantage vis-à-vis other mortgage providers, despite the additional systems and controls (as yet undefined) which will be required if Category 2 credit unions are permitted to provide this specific class of home-loan. **5.3 Investments** In principle, the framework for Investments for both Category 1 and Category 2 seems appropriate. However, with the exception of bank and corporate bonds, which are only available to Category 2, there is no differentiation of concentration risk limits based on credit rating. Indeed, there is not even a minimum applicable credit rating criteria for bank deposits or Irish and EEA State Securities. The concentration limit for investments in these asset classes is the same, irrespective of the credit rating of the counterpart. Therefore, under the framework as proposed, the credit concentration risk limit would be the same for a 3 month German state security, as for a 2 year deposit with a sub investment-grade bank. This would seem to be contradictory to market best practice and has the potential to increase the level of risk inherent in credit union investment portfolios. There have been significant enhancements to governance and risk management and control practices of credit unions in the recent past. The proposals set out do not seem to take account of these enhancements and represent a retrograde step despite their introduction. This is particularly the case for Category 1 credit unions.

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		We note again the requirement for significantly increased governance and risk management structures required for Category 2 certification along with the associated cost, and the limited additional availability of investment asset classes and maturities. **<u>5.4 Savings</u>** The proposed maximum savings value of €100,000 is overly restrictive and should be reconsidered. This is particularly the case for Category 2 credit unions. Any limit that might be imposed should be dependent on an appropriate balance sheet parameter or ratio. In this regard we note that it is proposed that there will be additional liquidity risk parameters imposed on all Category 2 credit unions. We also note that this restriction will place Category 2 credit unions at a competitive disadvantage vis-à-vis banks – potentially banks of similar balance sheet size. **<u>5.7 Governance</u>** The additional Governance requirements for Category 2 would, at significant extra cost, ensure that all credit unions in this category have extremely robust governance and risk control structures in place. However, these structures seems disproportionate given the limited additional activities and risks allowed to Category 2 credit unions. For Category 2 credit unions, the document sets out the requirement for a "dedicated" risk management officer, a compliance officer and an internal audit function. It is not clear what the word "dedicated" means in this context. Nor is it clear if this single standard is suitable for all credit unions in this category, irrespective of size or complexity.

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		<u>5.9 Reserves</u> CLINTO has no objection in principle to providing additional operational risk reserves, either as a Category 1 or Category 2 credit union. However, the reserve requirement needs to be proportionate to the risks involved. We have no details of the risk weighted approach to reserves which is being considered and so we can not comment on that. However, in general, we would have two concerns should there be changes to the level of reserves credit unions are required to hold: 1. Any amendment to the regulations governing the holding of reserves should not put credit unions at a competitive disadvantage vis-à-vis its competitors. 2. Any amendment to the regulations governing the holding of reserves which causes a general increase in the level of reserves to be held, should be implemented on a phased basis to avoid undue pressure on the sector. **<u>5.10 Liquidity</u>** The document mentions “consideration” of certain further unspecified requirements in relation to Liquidity. CLINTO is fully supportive of measures to improve and maintain the financial stability of individual credit unions and of the sector as a whole. However, it is difficult to make any comment here given the lack of detail. **<u>5.11 Other Prudential Requirements</u>** The document speaks of “consideration” of possible requirements for holding interim audits and additional requirements in relation to business continuity testing. Again, in the absence of specifics, it is difficult to comment.

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		<u>Other</u> There may be a case for introducing a third category of credit unions, with similar governance, risk management, compliance, liquidity and reserve requirements as Category 2, but with a higher total asset entry threshold. Eligible credit unions would necessarily be of a size to facilitate appropriate granularity and dilution of risk across a portfolio of, for instance, home-loans. The existence of such a category, and an unambiguous potential to expand the range of products, would have the effect of further driving consolidation in the sector and ensuring that particular higher-risk products were available via the credit union sector while at the same time ensuring that these products were only available via credit unions of an appropriate size.
(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?	There are a minimum of 3 categories of additional service that credit unions must be able to provide to their members: 1. Home loans where the credit union is the lender 2. Car leasing 3. Debit cards These service offerings should be available to both Category 1 and Category 2 credit unions with appropriate limitations for credit unions is each category. Credit unions aspire to be the main supplier of financial services to their members. A home and a car are generally the two largest purchases a person may make; both are generally financed. Credit unions must be in a position to provide this finance to its members. It is noted that the criteria and the approval processes associated with securing approval for the provision of other additional services are not defined in the document.

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(iv)	Do you agree that a provisioning framework should be developed for credit unions as proposed in section 6.2?	In principle, we agree that an appropriate provisioning framework should be implemented for all credit unions. However, there is little detail in the document regarding the proposed metrics to be used and the potential impact on provisions required. It is therefore difficult comment further.
(v)	Do you agree that the tiered regulatory approach should be introduced at this time?	In the absence of so much of the specifics of the proposed tiering structure, it is difficult to comment.
(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?	In the absence of so much of the specifics of the proposed tiering structure, it is difficult to comment. However, it should be noted that the credit union sector has undergone significant regulatory change in recent times. This change has incurred additional cost. Further, this change has taken place during the worst recession in the history of the country while credit union income has been under significant pressure. It is imperative that the introduction of any further and potentially costly, regulatory changes must take place in a manner that does not increase the general level of financial risk in the sector. Despite the introduction of enhanced governance and risk control and management structures and process as required by regulation in the recent past, credit unions are to be further restricted with regard to investment choices. The resulting negative impact on income will increase risk to the solvency of many credit unions and potentially put members' savings at risk.