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Deputy John McGuinness
Chairman
Public Accounts Committee
Leinster House
Dublin 2

23 December 2014

Dear Deputy McGuiness

Further to the meeting of the Committee of Public Accounts on Thursday 11 December 2014 please find attached information, prepared by the Registry of Credit Unions, on a number of points that were raised during the meeting. These relate to the following matters:

- Lending restrictions;
- Holding of AGMs;
- Social Housing;
- An Post Proposal;
- Investments in IBRC;
- Consultation on a Tiered Regulatory Approach; and
- Lending to small business.

I hope the information as attached is helpful to the Committee.

Yours sincerely

Elaine Byrne

Elaine Byrne
Deputy Registrar of Credit Unions

Response of the Central Bank of Ireland to Issues Raised in the meeting of the Committee on Public Accounts, 11 December 2014

LENDING RESTRICTIONS

Text from PAC transcript (pg. 17): ***Deputy Robert Dowds:*** *Will Mr. Casey or Mr. Power outline the sorts of restrictions that have been placed on credit unions? Why are they there? Can they be made more flexible?*

Background

While the important role of credit unions within their communities and, of course, that many members have a demand for credit is fully accepted, the need for credit unions to be prudent in how they lend money cannot be emphasised enough. It is the money of the saving members of credit unions that is ultimately lent to borrowing members. Ensuring that those borrowers can repay is paramount in the protection of those savings. Accordingly, we expect credit unions to apply prudent lending standards to the granting of all new loans or top-ups of existing loans and to have systems in place to ensure that such applications are fully assessed to confirm the member's ability to repay the loan. Lending restrictions are imposed in the context of on-going matters of supervisory concern arising in individual credit unions. On many of our on-site supervisory engagements, we have found an absence of credit policies, inadequate processes surrounding income verification and credit worthiness as well as significant failings in relation to credit control and following up on arrears.

Further information on findings from on-site engagements is set out in "Credit Union Prism Risk Assessments – Supervisory Commentary" and the associated press release available at the following links:

- http://www.centralbank.ie/press-area/press-releases/Pages/CentralBankpublishesreviewofthecreditunionsector.aspx
- http://www.centralbank.ie/press-area/press-releases/Documents/Credit%20Union%20PRISM%20Risk%20Assessments%20Supervisory%20Commentary%20May%202014.pdf

Lending Restrictions

It has been necessary to put lending restrictions in place in credit unions where there are regulatory concerns about the operation of these individual credit unions and the resultant risk to members' savings. The number of lending restrictions is a reflection of concerns about lending practices in the sector.

Currently about 56% of all credit unions are subject to lending restrictions. Where lending restrictions are imposed they tend to take the form of a restriction on individual loan size or on commercial lending activity and in some cases, a limit on the total lending permitted each month. Less than 10 per cent of all credit unions have a restriction which limits the total amount of lending within the month. This means that the vast majority of credit unions are not restricted in how much they lend in aggregate per month.

For those credit unions with an individual loan size restriction, the level at which the limit is imposed ensures that the vast majority of these credit unions can continue to make loans significantly more than the average value for gross loans outstanding for the sector of just above €6,000 – with the majority of restrictions enabling credit unions to lend amounts of between €10,000 and €30,000. This supports the approach adopted whereby we have carefully calibrated our use of this regulatory tool to mitigate risk while recognising the core business of credit unions to lend to their members.

38% of credit unions have a commercial lending restriction. Commercial lending is a specialist form of lending that requires specific skills and expertise. In general we view this type of lending as high risk and not appropriate for the majority of credit unions particularly in light of the current issues that have been identified in relation to lending standards and practices.

Based on analysis of returns submitted to the Central Bank by credit unions, there is no material difference between the average loan-to-asset ratio of credit unions with and without restrictions. Furthermore, where individual lending restrictions are imposed, the evidence suggests that the majority of credit unions are not lending up to the lending restriction amount with the majority of loans granted being at lower loan levels.

Review of lending restrictions

Individual credit union lending restrictions currently in place are reviewed on a regular basis to determine whether there is a necessity for the restrictions to remain in place.

Lending restrictions are, in most cases, intended to be short-term in nature and kept in place until the credit union has addressed the issues giving rise to the particular concerns advised to the credit union and until we can evidence that the weaknesses in governance and systems and controls are properly remediated and solutions fully embedded by the credit union. Credit unions that address our regulatory concerns and engage with us proactively in relation to mitigating identified risks will find that we are open to reviewing and, where appropriate, easing lending restrictions. Reviews of lending restrictions in credit unions are included within the planned 2015 supervisory work programme of the Registry.

Changes proposed to the lending framework for credit unions

The Central Bank published a consultation paper, "CP 88 Consultation on Regulations for Credit Unions on the commencement of the remaining sections of the 2012 Act", on 27 November 2014. This consultation paper includes proposals on regulations for credit unions in the area of lending, which are informed by regulatory actions taken by the Central Bank arising from lending practices in individual credit unions. It is considered that the introduction of these regulations, along with the governance and risk management framework introduced in October 2013, will provide a strengthened regulatory framework for credit unions in the area of lending. As referred to in CP88, 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 lending restrictions as a regulatory tool will reduce over time.

Holding of AGMs

Text from PAC transcript (pg. 14): ***Deputy Áine Collins****: I am aware of a credit union that has not had an AGM for three years and has been told by the Central Bank that it cannot hold an AGM. (pg. 15) Members are concerned when AGMs are not held. I appreciate the argument about destabilisation. When an AGM is not held, it gets around pretty quickly among the members that there is a problem. It is not open and transparent. We do not want to go back to where we all were a number of years ago, when people did not know what was going on. It is a serious issue.*

The provisions in relation to the Annual General meeting (AGM) are set out in Section 78 of the Credit Union Act, 1997. Currently less than 10 per cent of credit unions have not yet held AGMs in relation to pre-2014 financial year-ends. The primary reasons for this include matters of supervisory concern which have yet to be addressed by credit unions, as well as some cases where the annual accounts now have to be finalised by the credit union.

Actions taken by the Registry of Credit Unions in relation to the holding of AGM's seek to ensure protection of the interests of members of individual credit unions. The Registry continues to work with each such credit union on a case by case basis in order to resolve all outstanding issues to enable the AGM's proceed as soon as possible. This pro-active follow-up will continue and is included within the planned 2015 supervisory work programme of the Registry.

Social Housing

Text from PAC transcript: ***Deputy Robert Dowds*** *(pg 20) The ICLU reckons the credit union movement could provide between €500 million and €1 billion for social housing. I would be interested to know the Central Bank's reaction to this and whether it sees it as a viable proposition. (pg 21) I was rather surprised by this suggestion in the sense that it is not an area in which I would expect credit unions to be involved, although if they have sufficient funds and are able to be, that is all well and good. Could I ask Mr. Casey for a written response from the Central Bank on this question?*

When the remaining sections of the Credit Union and Co-operation with Overseas Regulators Act 2012 ("2012 Act") are commenced, the Central Bank will be provided with new regulation making powers in the areas of investments. These regulation making powers will include the power to prescribe:

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

The Central Bank is open to considering any proposals from credit unions or their representative bodies on investments for credit unions in public projects, including in relation to social housing. To date, no such proposals have been received. Any proposals received would be assessed in light of the new legislative requirements for credit unions with regard to the following:

- ensuring that any investment does not involve undue risk to members' savings; and
- assessing the potential impact of any investment on the credit union, including the liquidity and financial position of the credit union.

An Post Proposal

Text from PAC transcript: (pg 31) ***Deputy Paul J. Connaughton****: There is a proposal with the Department of Finance - I think it has come from Limerick - with regard to a possible amalgamation between the credit union movement and An Post. I will not go into this as An Post is not represented here and I imagine it would have to be consulted on this as well. From a rural perspective, in terms of ensuring the viability of credit unions and post offices, do the delegates see a possible synergy between those two entities in the future? I imagine it would need a change in legislation or regulation from the Central Bank. I accept it is not something that is going to happen overnight but* ***where does the proposal stand at the moment?***

The Central Bank is supportive of credit unions developing additional services and will consider proposals from credit unions on new additional services they wish to provide to members where the proposed additional service is supported by a robust business case, not contrary to financial services legislation, and the credit union can ensure risks are understood, managed and mitigated.

The Central Bank met with credit union representatives involved in the proposal for a pilot project between An Post and certain credit unions in October 2014. The Central Bank has provided feedback on the proposal including areas of financial services legislation that apply to credit unions which would need to be considered in the context of such a proposal. We have also indicated that we are available to have further meetings with the relevant parties as appropriate.

INVESTMENTS IN IBRC

Text from PAC transcript: ***Deputy Joe Costello:*** *(pg.39) Is Mr. McCarter able to give us an idea of the quantity of money owed to the 16 credit unions that are unsecured creditors?_(pg. 41)* ***Mr. Seamus McCarthy:*** *My understanding is that the original amount of the bonds will be known in each case. It should not be impossible to total the amounts. What we do not know is how much of it will come back. What one can know is how much of it has been impaired at this stage. There are three points - there is the face value of the bonds, the impairment that has been processed by this date and, to be decided and determined in the future, the amount the liquidator will be able to surrender.* ***Deputy Joe Costello:*** *The Comptroller and Auditor General has put it much better than I could. That is precisely what I am looking for. Can we obtain a note on that matter?* ***Chairman:*** *Will the information be supplied to the committee?* ***Mr. Seamus McCarthy:*** *The first two columns could be provided by the Central Bank, subject to any disclosure measure that needs to be taken. It may be an aggregate figure. I presume it will not be supplied on a individual basis.* ***Chairman:*** *Who can provide the rest of it?* ***Mr. Seamus McCarthy:*** *The IBRC liquidator.* ***Chairman:*** *Will the Central Bank give us as much information as it can in response to Deputy Joe Costello's question?*

Based on information provided to the Central Bank by IBRC 16 credit unions held a deposit with IBRC (not covered by the Eligible Liability Guarantee scheme) at the date of the liquidation. We understand the total amount is c.€15.2m (which represented c0.20% of total investments held by credit unions at end - 2012[1]). Based on information provided to the Registry of Credit Unions by the individual credit unions, all 16 credit unions have written - off the value of this investment in their accounts. (We understand that in relation to these deposits each of these credit unions received compensation of an amount of €100,000 from the Deposit Guarantee Scheme.)

[1] Based on December 2012 Prudential Return

CONSULTATION ON A TIERED REGULATORY APPROACH

Text from PAC transcript: (pg. 46) ***Chairman:*** *Would it be possible for us to see the consultation paper or the results of the process relating to it in order that we might obtain an idea of how the Central Bank approached the matter?*

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.

Consultation Paper 76 – "Consultation on the Introduction of a Tiered Regulatory Approach for Credit Unions" ("CP76") was published on 23 December 2013.

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.

The consultation closed on 31 March 2014 and 164 submissions were received in response to CP76.

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 indicated 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.

Following review of the submissions received, on 30 June 2014 the Central Bank published a Feedback Statement on CP76 which set out the Central Bank's detailed consideration of the submissions and proposed next steps which include that:

- in light of the feedback received, the Central Bank does not propose to introduce a tiered regulatory framework for credit unions at this time;

- further communication, engagement, clarification and consultation with the credit union sector is required prior to taking a decision to introduce a tiered regulatory approach for credit unions; and
- the Central Bank would publish a consultation paper on regulations for all credit unions to complete the introduction of the strengthened regulatory framework under the regulation making powers contained in the 2012 Act.

On 27 November 2014, the Central Bank published Consultation Paper 88 – "Consultation on Regulations for Credit Unions on commencement of the remaining sections of the 2012 Act" ("CP88"). The consultation on CP88 is open until 27 February 2015.

Further information on the consultation papers is available at the following links:

- CP76, the submissions received on CP76 and the Feedback Statement on CP76: http://www.centralbank.ie/regulation/poldocs/consultation-papers/Pages/closed.aspx.
- CP88:http://www.centralbank.ie/regulation/poldocs/consultation-papers/Pages/default.aspx.

LENDING TO SMALL BUSINESS

Text from PAC transcript (pg. 50) ***Deputy Áine Collins:*** *Are credit unions allowed to lend money to small businesses? We know it is happening, but are they legally entitled to do it?*

Credit unions are permitted to lend to members within the requirements of the Credit Union Act, 1997. This includes providing loans to members with small businesses. Currently the majority of credit union sector lending is personal lending[2]. Business lending is a specialist form of lending that requires specific skills and expertise. The Report of the Commission on Credit Unions proposed that the level of business lending that credit unions are permitted to undertake should be subject to limits, with higher limits for larger credit unions. The recently published consultation paper on new regulations for credit unions ("CP 88") proposes that credit unions should be permitted to undertake commercial lending up to 50% of their regulatory reserve. Certain other requirements are also proposed for commercial loans. Small business loans (less than €25,000) are excluded from this proposed limit and would not be subject to additional regulatory requirements proposed for commercial loans.

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[2] Based on reported information.

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[redacted]

[illegible] (FF) [illegible] Credit unions would welcome [illegible] to small businesses [illegible] they are largely confined to [illegible]

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