

Public Accounts Committee

Thursday, 14th December 2017

Opening Statement by Mr Des Carville, Head of the Shareholding and Financial Advisory Division, Department of Finance

Introduction

I would like to thank the Chairman and his Committee for the opportunity to address you this morning.

With me this morning are Mr Gary Tobin, Assistant Secretary, Banking Division in the Department of Finance, Mr Scott Rankin, Deputy Head of the Shareholding and Financial Advisory Division, Mr Gary Hynds, Senior Banking Specialist in the Shareholding and Financial Advisory Division, Mr Eoin Dorgan, Principal Officer, Banking Division and Mr David Tuohy, Banking Specialist in the Shareholding and Financial Advisory Division.

I will focus on chapter 3 of the Comptroller and Auditor General's Report on the Accounts of the Public Service 2016. Chapter 3 of this report deals with the Cost of the Banking Stabilisation Measures as at end-2016. From your invitation to the Department of Finance, I do understand that the Committee particularly wished to discuss the

Special Liquidation of IBRC and specifically the costs incurred as part of the liquidation, however, as per my letter to you dated 12th December 2017, having consulted with the Attorney General's Office, unfortunately we are not in a position to respond to queries concerning the costs associated with the Special Liquidation given that these matters are now the subject of dispute in the High Court awaiting determination. This is as a result of the Department of Finance being served with a Plenary Summons on the 8th December 2017 seeking declaratory reliefs against the Minister for Finance with regard to a number of matters pertaining to the terms and conditions of remuneration and expenses of the Special Liquidators, and their oversight by the Department. We have shared the plenary summons with the Committee so you will appreciate its scope. While the Special Liquidators were due to attend with us today, their legal advice is that it would not be appropriate for them to be present. We have shared the correspondence between the Department and the Special Liquidators in this regard with you for full transparency.

I have to say that we are very disappointed and frustrated that we are not able to discuss the costs of the liquidation as this is a topic in which we invest considerable efforts to ensure that the taxpayer is getting value for money. We warmly welcome the Committee's interest in this topic as we recognise that the absolute quantum of

fees are, on the face of it, large. It was for this reason in 2014 that the first of four detailed reports were published to provide transparency on the workstreams associated with the special liquidation and the associated costs of each of these workstreams. Please be assured that the Department and the Special Liquidators will appear before the Committee as soon as the litigation is resolved.

Returning to the Comptroller and Auditor General's Report on the Accounts of the Public Service 2016, chapter 3 of this report sets out an estimate of the net outturn of the banking stabilisation measures taken by the State as at end 2016. The gross cost of recapitalising the banking system during the period 2009 - 2011 stands at €66.8bn, which was funded through a combination of Exchequer and National Pension Reserve Funding. Taking into account the cost of servicing the debt to end 2016 of €14.8bn and the income earned on our investments to end 2016 of €25.1bn, the net cost estimated by the Comptroller and Auditor General was €56.5bn as at end 2016.

When the estimated value at that date of the State's remaining shareholdings in AIB, Bank of Ireland and Permanent TSB (a combined €13.6bn), and NAMA's projected surplus (€3bn) are taken into account, the estimated net outturn as at end-2016 is a cost of

around €39.9bn. This shows a reduction of approximately €3bn since this analysis was last conducted at the end of 2014 which reflects additional receipts of €5bn and the recognition of the estimated €3bn surplus now expected when NAMA winds down in 2020. This was offset by the increase in the cost of debt servicing associated with these investments by €6.1bn over the period.

At the end of 2016 the value in the State's shareholdings in the three quoted banks was €13.6bn. Since then the State realised €3.4bn from the IPO of AIB in June this year leaving it with a 71% remaining shareholding in that bank. The IPO of AIB was managed by the Department and was the second largest IPO globally in 2017, the largest in Europe in 2017 and the largest on the London Stock Exchange since 2011 as measured by the level of funds raised. By any measure this was a very successful transaction which was made possible by the recovery of the bank, the economy and the dedication and professionalism of all those who worked on the transaction. As of the close of business on 12th December 2017 the market value of our remaining investments in these banks stood at €12.4bn indicating a net increase in the value of our shareholdings since the end of 2016 of almost €2.2bn when the proceeds from the AIB IPO are taken into consideration.

In relation to banking stabilisation related Central Bank income, for the years 2009 to 2016, the examination by the Comptroller and Auditor General has estimated that in the region of €7.7bn of the Central Bank's surplus income of €12.5bn was attributable to financial instruments held as a result of banking stabilisation measures taken by the State. These financial instruments were in the form of exceptional liquidity assistance and Government bonds held by the Central bank. The report estimates that 97% of the €7.7bn portion of the Central Bank's surplus income for the years 2009 to 2016 is attributable to transactions between the Central Bank and IBRC.

Subsequent to the liquidation of IBRC in February 2013 the Central Bank acquired €25.034bn of Floating Rate Notes (FRNs) and €3.46bn of the fixed rate 5.4% Treasury Bond 2025. Between 2013 and 2016, the Central Bank earned net interest of €2.7bn from the bonds and realised gains of €3.2bn from the disposal of some of these bonds. The Central Bank stated in its 2016 annual report that it intends to sell the remaining floating rate bonds as soon as possible, provided conditions of financial stability permit.

As at 13th December 2017, the Bank has so far disposed of €9.5 billion nominal of the Floating Rate Notes, significantly exceeding its minimum targets outlined in 2013. While the pace of these disposals

is significantly ahead of the minimum schedule, it is positive that the NTMA is locking in current low market interest rates now rather than some time in the future at which point rates could be higher.

Furthermore, the cancellation of these bonds will also increase the amount of Irish debt that the ECB can purchase in the sovereign debt markets which should help in further reducing the cost of the State's borrowing. Notwithstanding these positives clearly this acceleration needs to balance the negative consequences of the purchase and cancellation which includes the potential creation of excess supply in the market and the foregoing to the State of ongoing Central Bank profits related to these bonds.

The debt-related cost to the State associated with the investments in the bank was in the region of €14.8bn over the period 2009 to 2016. These costs are estimated by the C&AG and reflect the additional annual debt servicing costs and other related costs incurred by the State as a result of the borrowings used to invest in the banks.

The C&AG highlights that the Exchequer continues to incur the cost of servicing the debt associated with the net €56.5bn cost of the investments in the banks and the report estimates that this cost is likely to be in the region of €1.7bn for 2017 with over €1bn of this in respect of IBRC and a further €0.6bn in respect of AIB. The ongoing annual cost of servicing the debt associated with Permanent TSB is

estimated at around €50m per annum. The State has recouped its investment in Bank of Ireland and, therefore, incurs no ongoing debt servicing costs in relation to Bank of Ireland.

The long-term cost of servicing the debt associated with the bank investments will depend on a number of factors including:

- The amount the State realises from its remaining investments
- The period for which the Central Bank continues to hold government bonds.
- The cost of funding for the State as it refinances existing debt when it matures.

The State guaranteed certain bank liabilities under three main schemes - The Deposit Guarantee Scheme, the Credit Institutions (Financial Support) Scheme, and the Eligible Liabilities Guarantee Scheme. By the end of 2016, the State had received net income in the region of €3.7bn under the schemes with the majority of this relating to the Eligible Liabilities Guarantee Scheme. Included in this figure is €280m received as an interim dividend from the Special Liquidators of IBRC and it is expected a second interim dividend of €280m will be received in the next few weeks following the

announcement last week of a further 25% payment to admitted unsecured creditors of IBRC.

Finally, in relation to NAMA, their Board has approved a projected terminal surplus of up to €3bn over the course of its life, which is dependent on favourable market conditions being maintained when realising remaining assets. This surplus will be paid to the Exchequer to reduce the overall cost of banking stabilising measures.

I would like to thank the Chairman and Committee for your attention. I hope you appreciate that the stance adopted by the Department today is in the interests of protecting the position of the State in the proceedings brought. I would welcome any follow-on questions.

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