Joint Committee on Regional Development, Rural Affairs, Arts and the Gaeltacht

'Maintaining an effective service and presence in rural communities'

Wednesday, 9th November 2016

Credit Unions - At The Heart of Communities

Lending to SMEs and Agri Business

Personal Micro Credit Scheme

Social Housing Strategy

WE LOOK AT THINGS DIFFERENTLY

Credit Union

WHAT CREDIT UNIONS CAN DELIVER

The Irish League of Credit Unions represents over 300 credit unions with over 3 million members across the country. These credit unions have total assets of over €14 billion. Credit unions are self-help financial co-operatives owned and run by their members. Our aim as a movement is to help members who group together in communities of place and interest, such as their employment, pool their savings and give access to credit.

The credit union model remains not merely relevant but is an essential support for local communities. In an age when globalisation of financial institutions and deployment of technology as a barrier, as distinct from a worthwhile assistance, between ordinary people and decision makers who make extraordinarily important financial judgement calls affecting their lives, credit unions are open and local.

In many communities, especially rural communities, the credit union is not just a local source of credit it is the only physically present, face-to-face interaction available for people with the decision makers they need to interact with.

The policy platform of the League is set out in its Six Strategic Steps. Three of those key proposals dealing with micro-lending, lending to for SMEs and agri-loans and lending for Social Housing are set out more fully in this submission to the Joint Committee.

Late last year a Personal Micro Credit (PMC) pilot initiative was launched in 30 credit unions across the country. Branded the 'It Makes Sense Loan', its aim was to prove that credit unions could offer a loan product that matched the convenience and ease of moneylenders' offerings, address the exorbitant rates charged by them and yet was within prudential lending guidelines.

The pilot was an undoubted success and the scheme is now being rolled out to as many credit unions as possible. Already over 80 credit unions are offering PMC loans with more to come on board in the coming months.

On lending for social housing, the League's proposal is in response to Government policy, set out in Social Housing Strategy 2020. The Joint Committee on Housing, Planning and Local Government in its recent report supported the initiative as a priority action. The Programme for a Partnership Government further reflected positively on the initiative. Numerous meetings have taken place, however, to date no substantive progress has been made. This is a matter of considerable frustration to the League and credit unions.

On lending to SMEs and agri-lending, traditionally lending was for personal purposes e.g. family events, education, cars and home improvements. The lending types our proposal seeks to address includes workshops, vans, tools, farm buildings, tractors, machinery and livestock.

The League understands that these loans are different due to cyclical and seasonal factors which affect cash flow. This needs to be appreciated by all stakeholders including the Central Bank (CBI). It is essential to consider our proposal within its context of ensuring that all applications are expertly assessed so that that lending decisions are prudent and members' savings are fully protected.

The Irish League of Credit Unions (ILCU) is giving leadership in responding to community need and government policy. We look to the Oireachtas and government to deliver commitments made to credit unions before the election. Particularly we look to the Joint Committee for practical help in ensuring delivery on commitments made in the Programme for Partnership Government, which are attached with this submission.

LENDING TO SMES AND AGRI BUSINESS

Introduction

Credit unions have a significant footprint in Ireland, with a total membership of 3.1m people. At 30 September 2015, there were 355 registered credit unions in Ireland with total assets of €14.8bn. At 30 September 2015, the total capital level of credit unions was 16% of assets.

Currently, the movement has circa €9bn held in investment related products earning a low yield and put to an unproductive purpose. In 2015, the Irish League of Credit Unions (ILCU) agreed a strategy document entitled "Six Strategic Steps". This is our policy programme. It is a plan to better serve our members, to invest our resources to meet the needs of society, to ensure better regulation and deliver on the social objectives we were founded to serve, for the future. Since the release of this document, the Irish League of Credit Unions has made significant progress on one such Strategic Step; the development of a proposal whereby the Irish credit union movement could create a dedicated funding vehicle to provide finance for social housing in line with Government Policy. The participation of credit unions in a fund for SMEs including family farms is another of our stated Six Strategic Steps. The purpose of this paper is to outline our SME proposal, which is intended to encompass all business types which represent prudent lending propositions.

SMEs, including family farms play a vital role in the Irish economy. SMEs create employment, generate taxes, stimulate economic activity, and participate in the orderly supply of goods and services for the betterment of the wider population, both domestically and internationally. It therefore follows that providing the SME sector with necessary supports to foster a culture of growth orientation and dynamism is a key matter of national policy.

In line with its operating principles, the credit union movement has an interest in improving the economic and social well-being of 3.1m Irish people, and a vibrant and well-funded SME sector has a special relevance to Irish credit unions in this regard. The economic strength of the Irish economy is highly relevant to Irish credit unions, as the vast majority of the economically active Irish population, are members. Given the economic importance of SMEs to the overall well-being of the wider economy and family farms in the rural economy, the Irish credit union movement has a strategic interest in supporting the sector.

Outline of Proposal

Our proposition is broadly as follows; Irish credit unions would participate in a State backed vehicle that would:

- Enable Irish credit unions to act as an efficient distribution network to originate SME loan applications
- Enable Irish credit unions to invest in a funding facility that will lend to SMEs in Ireland

Our proposition is that this structure is formed on a collective basis. Our proposition is that this would be piloted with a small pool of well capitalised and large credit unions at the outset.

BENEFITS

Benefits for Irish Credit Unions from the Proposal

The key benefit arising for the credit union movement from the Proposal would be that it would enable the movement to put a portion of the members' funds of €9bn (currently held in short term investments) to a more productive and economically rewarding purpose. It would also enable the movement to offer its members a more diversified and dynamic product offering. If an SME or family farm approached a credit union for a commercial loan while the credit union itself would not offer the loan nor take direct risk on the loan, it could direct the application to a credit union associated entity (the vehicle) who could consider the credit and potentially offer the loan to the SME or farm borrower.

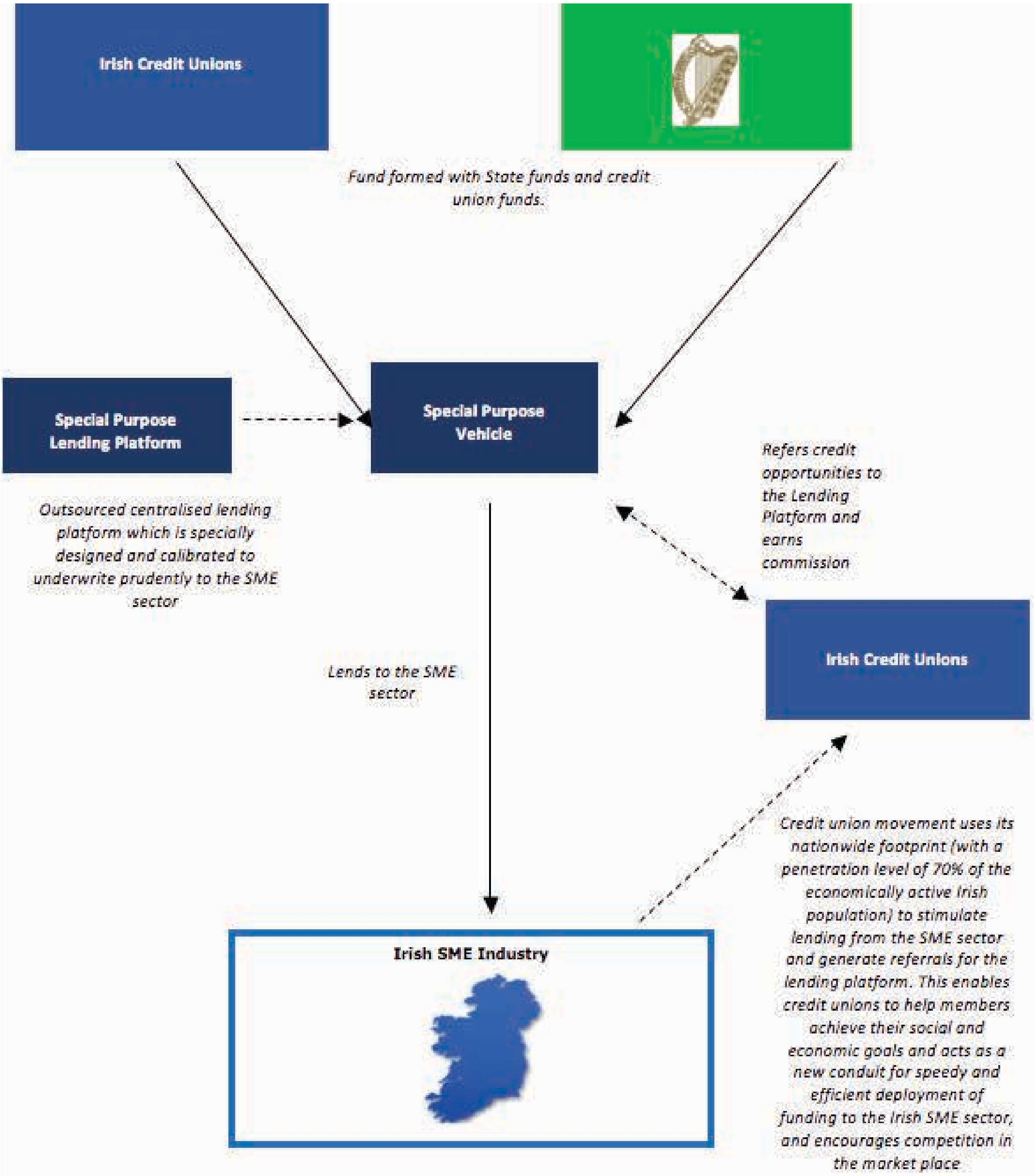
Credit unions by definition exist to assist their members to attain their economic and social goals. On a wider economic level, the Irish credit union movement is, similar to other elements of the financial services landscape, highly sensitive to external economic factors. In times of economic disruption, lending demand typically falls and arrears typically grow. In times of economic stability, lending demand typically grows and arrears typically fall. Given the economic importance of SMEs to the overall well-being of the wider economy, the Irish credit union movement has a strategic interest in supporting the SME sector as this should lead to a strengthening of the economic environment to which our 3.1m members are exposed. Finally, commercial lending is by nature, more risky than personal lending. The formation of a centralised vehicle to lend to the SME sector would enable a stronger centralised risk management capability whereby the vehicle, managed by an independent third party, would have dedicated and skilled resources to identify, assess, measure, and manage credit and operational risks. This would facilitate credit unions supporting the commercial loans market, but in a manner that would provide robust mitigants to manage risk, and above all, protect member funds.

Benefits for the State from the Proposal

Providing the SME and farm sectors with necessary supports to foster a culture of growth orientation and dynamism is a key matter of national economic policy. This proposal would enable these enterprises to access a strong, sustainable, well-capitalised and domestically managed funding source. In addition, this proposal would open up the credit union infrastructure as a key SME loan distributor. Credit unions are located throughout the country and interface with a significant portion of the economically active population of Ireland. Credit unions are different in structure, nature and ethos to retail banks. The credit union model could act as a new conduit for the State to stimulate borrowing in the SME and farm market and support it with competitive loans in a speedy and effective manner, using the Credit Unions' pre-existing and mature infrastructure. The credit union movement has a wide socio-economic and political reach. Thousands of civic minded volunteers committed to furthering the social and economic goals of 3.1m people within the Irish State, are active in local communities and could provide a key link to the SME sector in communicating the availability of funding at grass-roots level. The proposal would also enhance competition in the market place.

Infographic of Proposal

An infographic setting out an outline of the proposal is shown below:



PERSONAL MICRO CREDIT SCHEME

Background

Credit unions are a social movement, delivering financial services, in communities across the country. One community that that is central to the concerns of the movement are the financially excluded. In the best of times ours was a country where people who fell on hard times either had no access to credit, or fell into the hands of moneylenders. After the worst recession in decades, many more fell into dire straits.

The Personal Micro Credit (PMC) project is a practical example of how Government Departments and Agencies, the Irish League of Credit Unions (ILCU), Credit Unions and the Not for Profit sector can work together to achieve real impact. PMC is operated by individual credit unions and promotes financial inclusion by offering the most vulnerable in Irish society a low cost credit alternative to moneylending organisations.

Besides providing much needed credit, the PMC loan is designed to incentivise individuals to join a credit union, gain a credit history and build a long-term mutually beneficial relationship as a conventional member. It's about immediate help now and help for people to help themselves, longer term.

The origins of the PMC project date back to 2013. A draft report was produced and sent to the then Minister for Social Protection recommending the introduction of a PMC initiative operated by the credit unions as an alternative to the moneylending industry. The ILCU stepped forward and have worked closely with Citizens Information Board (CIB), Money Advice and Budgeting Service (MABS) and Social Finance Foundation (SFF) to lobby politicians and departmental officials to support such a scheme.

Simultaneously, a research project, funded by SFF and the Central Bank of Ireland, examined the experience of PMC schemes internationally. It concluded that such schemes worked, with low rates of default and recommended that a PMC-type initiative should be undertaken in Ireland.

In March 2015 the endeavour kicked off in earnest, gaining stakeholder support for the trial of a PMC pilot program. The initial focus was social welfare recipients who were willing to use the Household Budget Account (HHB) as the repayment method for the loan.

The stakeholders in the initiative are numerous and committed:

- Department of Social Protection
- Department of Finance
- Central Bank: Registry of Credit Unions
- Irish League of Credit Unions
- Credit Union Managers' Assoc.
- Credit Union Development Association
- Individual credit unions
- An Post
- Social Finance Foundation
- Citizens Information Board
- MABS
- St Vincent de Paul (representing NGOs)

The Pilot

Branded the 'It Makes Sense Loan', a pilot program ran from November 2015 to May 2016 in 30 credit unions across the country. The aim was to prove that credit unions could offer a loan product that matched the convenience and ease of moneylender products, whilst undercutting the exorbitant rates charged by moneylenders and yet remained consistent with prudential lending guidelines.

The pilot was a significant success and more than

1,200 loans were written over the six month pilot period. Loan amounts were typically €500 with a repayment schedule of less than a year.

The scheme was designed so that borrowers did not need to be existing credit union members, did not need to have savings built up and were not disqualified as a result of previous indebtedness / credit default. The default rates at 4% were consistent with international levels. The effect on many of the borrowers was transformative and overall satisfaction levels were a remarkable 97%. 94% of borrowers stated that they would borrow again. Some relevant data from the pilot are shown in the table.

Average APR	% of Loans between 7-12 months	% of Female Borrowers	% of Borrowers who are single	% of Borrowers who are lone parents	No. of loans with poor credit history
11.69%	72%	55%	49%	30%	84

National Rollout

As a result of the successful pilot, a national rollout of the initiative was agreed by all stakeholders. Significantly the initiative was also included in the 2016 Programme for Partnership Government i.e. "Specifically we support…the rollout and extension of the Personal Microcredit Scheme, which is providing simple microloans to members and helping to combat the use of moneylenders." In July 2016, the Minister for Social Protection announced the national rollout, which was welcomed by all political parties and by prospective borrowers.

As part of the national roll-out the initiative has been extended to both cash and EFT social welfare recipients. This means that the number of individuals and families who can be helped under this initiative has been greatly increased, including those on the Family Income Supplement (FIS) payments.

To date 80+ credit unions are signed up to offer It Makes Sense loans. These credit unions represent over 40% of eligible credit union assets across twenty-one of the twenty-six counties. Credit unions continue to sign up to the PMC initiative and early 2017 will see a further recruitment drive. Information on where loans are available can be found at www.itmakessenseloan.ie

It is planned to shortly introduce a facility whereby a small amount of money can be added to the loan repayment as a means of promoting a savings habit with the individual.

The key features of the 'It Makes Sense' offering are:

- Social welfare recipients
- Fast track membership (for non-members)
- No savings needed
- Default history does not necessarily rule individuals out – an ICB check is not mandatory
- Separate credit policy drafted with and acknowledged by the Registry of Credit Unions in the Central Bank
- Repayment via An Post's Household Budget Scheme or by standing order or direct debit
- Encouragement for individuals to save
- Path for individuals to graduate to standard lending
- Final credit decision rests with the credit union

The Social Injustice

There is a real social injustice in Ireland when those that can least afford it pay the highest rates of interest for credit. And not just the highest rates but exorbitant ones. Take the typical example below where a credit union interest rate of 12.68% (APR) is contrasted with that of one well-known moneylending organisation of 187.2% (APR).

€500 loan repaid over 26 weeks

	Interest	Weekly Payment
Credit Union	€16	€20
Money lenders	€150	€25
Diff	€134	€5

Long Term Strategy

The ILCU recognises the importance of individuals and families having access to affordable credit and has therefore enthusiastically supported the PMC initiative. It has provided funding for the initiative, has delivered much of the operational infrastructure to roll out PMC and continues to deliver vital support to ensure its success.

ILCU also views the initiative as a very important bridgehead in the quest to address financial exclusion in Ireland, thus improving the lives of hundreds of thousands of individuals and families.

Finally, with the credit union movement fully on board by end 2017, there will be a strong case to be made then to the authorities for much more stringent regulation of the money lending industry, including restricting the level of interest rates they may charge. This would represent a substantial victory, consistent with the original intent and ethos of the founders of the credit union movement and have a very beneficial effect on the most vulnerable in Irish society.

CREDIT UNION SOCIAL HOUSING STRATEGY

Introduction

Following is a summary of our proposal for the provision of funding for social housing by credit unions. It is aligned with our overarching policy document, Credit Unions – Six Strategic Steps. Social housing refers to the provision by the Irish Government of housing supports for those unable to provide for accommodation from within their own resources. It is a key social policy and it impacts a significant proportion of the population in a profound way. During the recession there were successive years of reduction in the social housing budget. In November 2014, the Minister for the Environment, Community and Local Government published the Social Housing Strategy 2020 ("SHS") which included a number of key themes:

- The State adopts a central role in the direct provision of social housing through a resumption of building on "a significant scale".

- The funding of this programme will require the development of innovative funding mechanisms that do not increase the General Government Debt i.e. financial sustainability.

Credit unions are self-help co-operative financial organisations geared to attaining the economic and social goals of members and wider local communities. Credit unions have been part of the Irish financial services landscape since the 1960's when enabling legislation was passed. Irish credit unions, like other Irish financial institutions, are currently strategically challenged due to low lending demand. Loan to asset levels have fallen at movement wide level from 44% in 2010 to 27% in 2015. During this period, the movement has maintained its funding base, and as a result, has significant levels of member funds held in investment related products earning a low yield and put to an unproductive purpose. This also exposes significant levels of members' funds to market risk as income yields are under increased margin pressure due to the prolonged low interest rate environment. Currently, the movement has circa €8.5bn held in investments.

Proposition

Our proposition is broadly as follows: the ILCU movement credit unions would form a special purpose vehicle that would either:

1. Invest in a state owned "financial vehicle" which would on-lend to Approved Housing Bodies to fund the development of social housing.

2. Invest and on-lend directly to Approved Housing Bodies to fund the development of social housing.

The key benefit arising for the credit union movement from this proposition would be that it would enable the movement to put a significant portion of the members' funds of €8.5bn (currently held in short term investments) to a more productive and economically rewarding purpose, while at the same time, addressing a key social issue that deeply affects the communities which credit unions serve. This would represent an initiative that would be very closely aligned to the core values of the credit union movement; economic democracy, inclusiveness, human and social development, community focus etc. The key benefit for the State from this proposition would be that this would enable the Government Strategy of "Off-Balance Sheet" sustainability to be fulfilled over short, medium and long term time-horizons. Credit unions could become the leading funder of the social housing strategy (via AHBs) and reduce the financial commitments of the State to the Social Housing Agenda, while, enabling the Government to retain complete control over Social Housing Policy. This would also have a wider economic impact. The initiation of Social Housing Projects would create employment, generate taxes, provide stimulus to the construction sector etc. The key benefits for the population as a whole are obvious; the creation of a sustainable supply of social housing opportunities for those in need.

The Mechanism – Approved Housing Bodies

Approved Housing Bodies ("AHBs") will play an increased role in the provision of social housing strategy over the coming years, in line with the national strategy to move to "off balance sheet" finance. The proposed mechanism developed in this paper sets out a structure by which the Irish credit union movement could fund AHBs to provide social housing. AHBs provide and manage social rented housing. They are private, non for profit organisations formed for the purpose of relieving housing need. There are approximately 520 Approved Housing Bodies in Ireland with a stock size of over 27,000 units. It is estimated that approximately 17% of the current stock is supplied by AHBs. Approximately 10% of AHBs provide 80% of the housing supply. Therefore, there are a small number of well-established and financially sound AHBs who provide the vast majority of the social housing needs. The 2011 National Housing Policy Statement introduced a Voluntary Regulation Code, which was designed to provide a framework through which the standards and operating practices of AHBs may be more effectively regulated. In February 2014, the Minister for the Environment, Community and Local Government established an Interim Regulatory Committee under the Board of the Housing Agency. It is worthwhile to note that one of the primary stated regulatory objectives is to "facilitate investment". The regulatory focus with regard to the AHBs is to ensure that AHBs meet certain objectives in relation to "governance, financial viability and performance management".

Risks to the Irish Credit Union Movement

The nature of the risks that the proposal would present to credit unions' funds could be summarised into two core risk types, as follows:

- Counterparty Risk – risk that an AHB defaults and credit unions have to impair the investment in the Credit Union SPV as the AHB is unable to repay the SPV.

- Liquidity Risk – risk that credit union funds are unduly tied up for excessively long periods of time and the Credit Union SPV is unable to meet liquidity calls from credit unions.

It is important at the outset to note that credit unions are constantly exposed to counterparty risks. Every loan that a credit union grants and every investment that a credit union makes, exposes the credit union to risk; risk that the member defaults on a loan, or risk that a counterparty fails to redeem an investment. The fact that a social housing scheme presents counterparty risk should not of itself be a concern. What is relevant is the level of risk, the nature of risk, and the mitigants that can be put in place to manage the risk. The key mitigant in underwriting loans that are part of a social housing scheme is that the State is ultimately the counterparty to the loan repayments. In addition, the fact that over 80% of the housing needs are provided by a small pool of well established, financial sound, and regulated entities is a key aspect of reducing the risk profile of the proposition. A social housing scheme would undoubtedly impact liquidity levels in the credit union movement. However, the relativity of liquidity is the key consideration in the context of credit unions at this stage of the economic cycle of recovery.

Currently, the Irish credit union movement has reached highs in liquidity levels. Therefore, the Irish League of Credit Unions would view that a social housing scheme could redress a liquidity imbalance, rather than expose the movement to excessive liquidity risk, provided the scale of the scheme is measured, proportionate and regulated.

The Proposed Structure

Two proposed structures are set out overleaf. In order for a credit union social housing scheme to fit within the current regulatory framework, a change in regulatory guidance would be needed to expand the definition of collective investment schemes to include social housing projects. Class 5 Collective Investment Scheme would need to be expanded, along the following lines (see underline):

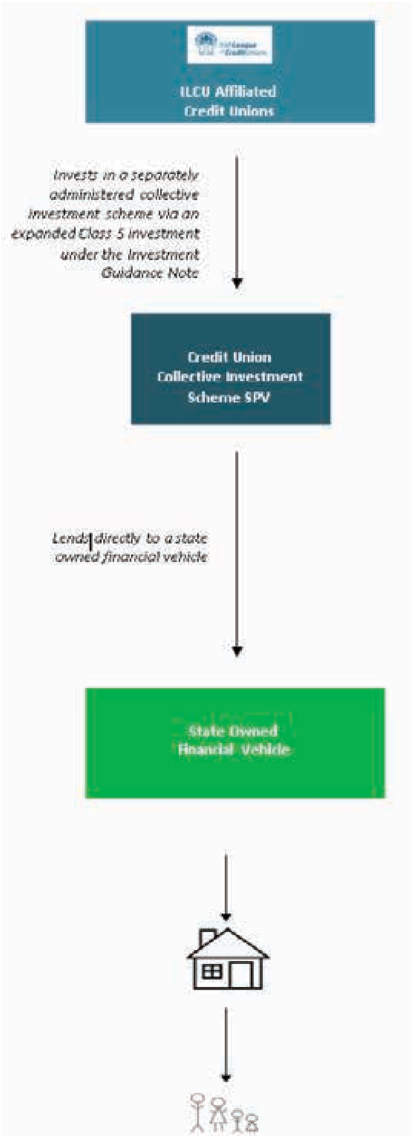
"Units or shares in open-ended retail collective investment schemes, <u>including Approved Housing Body property schemes, but excluding all</u> other property schemes, authorised by the Financial Regulator".

Benefits for the State from the Proposal

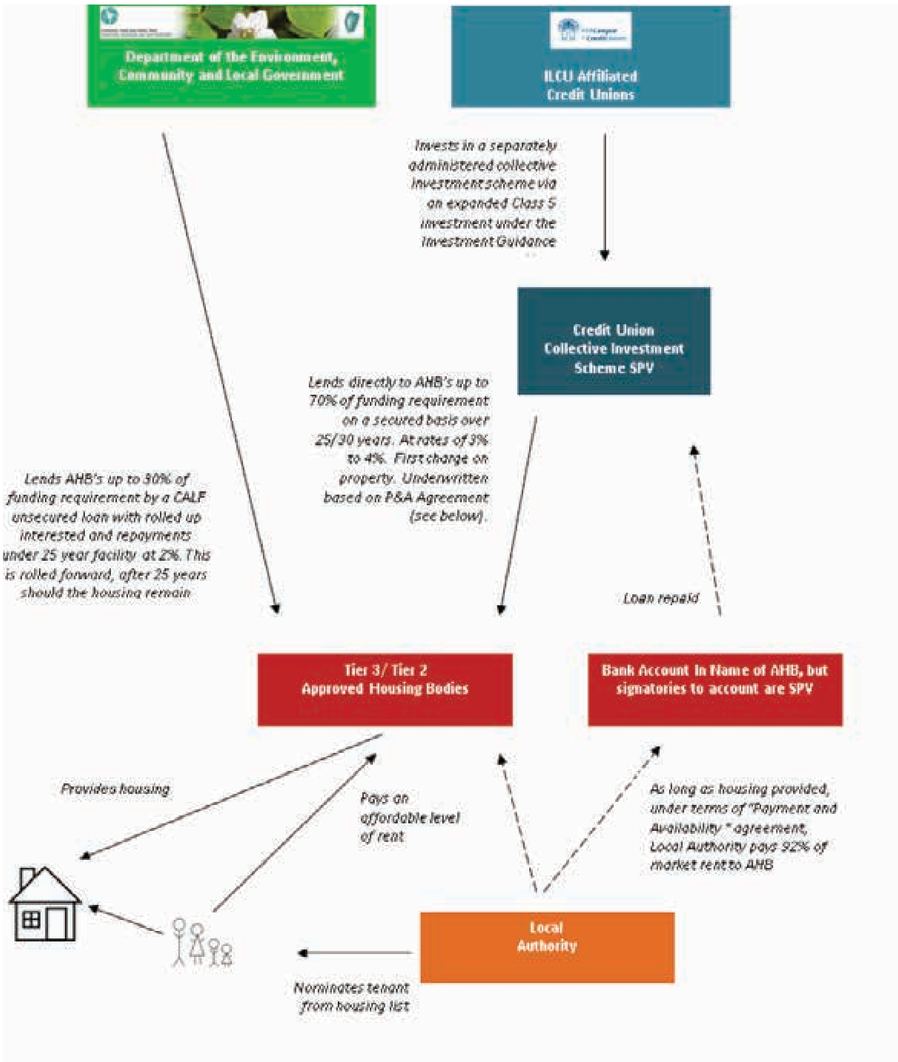
Providing the SME sector with necessary supports to foster a culture of growth orientation and dynamism is a key matter of national economic policy. This proposal would enable the SME sector to access a strong, sustainable, well-capitalised and domestically managed funding source. In addition, this proposal would open up the credit union infrastructure as a key SME loan distributor. Credit unions are located throughout the country and interface with a significant portion of the economically active population of Ireland. Credit unions are different in structure, nature and ethos to retail banks.

The credit union model could act as a new conduit for the State to stimulate borrowing in the SME market and support it with competitive loans in a speedy and effective manner, using the Credit Unions' pre-existing and mature infrastructure. The credit union movement has a wide socio-economic and political reach. Thousands of civic minded volunteers committed to furthering the social and economic goals of 3.1m people within the Irish State, are active in local communities and could provide a key link to the SME sector in communicating the availability of funding at grass-roots level. The proposal would also enhance competition in the market place.

Direct Model



Indirect Model



2016, THE POLITICAL COMMITMENTS WHICH REQUIRE TO TO BE DELIVERED ON

Credit unions are self-help co-operative financial organisations geared to attaining the economic and social goals of members and wider local communities.

The Government is proceeding on the basis of both the Programme for Partnership Government and the Confidence and Supply Arrangement between the Government and Fianna Fáil.

The Confidence and Supply Arrangement provides to:

- Develop a strategy for the growth and development of the credit union sector.

And the Programme for Partnership Government to:

- ...investigate with all stakeholders how Credit Unions can support social housing through Voluntary Housing Services (Year 1 Action).

- To investigate what role the Credit Union movement can play in the development of new housing, the Department of Finance will engage with the League of Credit Unions to help them develop their housing proposals. (First 100 Days Action).

- Requesting An Post and the League of Credit Unions, as well as any other interested stakeholders, to investigate and propose a new model of community banking.

The Programme for Partnership Government also promises:

"We are also committed to ensuring that credit unions benefit from regulatory support, in order to respond to the needs of a changing economy. Specifically we support:

- The rollout and extension of the Personal Microcredit Scheme, which is providing simple microloans to members and helping to combat the use of moneylenders.

- Assisting credit unions in making successful applications to retain members' savings in excess of €100,000 (CP88), recognising the independence of the Registrar of Credit Unions.

- Asking the Central Bank of Ireland to instigate a review of the continued appropriateness of the savings limit within a year of the formation of the new Partnership Government.

- Working with the Registrar of Credit Unions at the Central Bank to gradually lift current lending restrictions as appropriate, including for housing.

- Credit unions' move towards more electronic and online services, including the rollout of debit cards and enhanced online banking service.

- Asking the Credit Union Advisory Committee (CUAC) to conduct a review, and report by the of June 2016, on the implementation of the recommendations outlined in the Report of the Commission on Credit Unions.