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Consultation on Potential Changes to the Lending Framework for Credit Unions

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1. Introduction

The Central Bank of Ireland is publishing this consultation paper to consult on potential changes to the lending framework for credit unions. These proposed changes have been informed by the Central Bank's statutory mandate in relation to credit unions as set out in section 84 of the Credit Union Act, 1997 (the 1997 Act) which requires that the Central Bank shall administer the system of regulation and supervision of credit unions with a view to (i) the protection by each credit union of the funds of its members, and (ii) the maintenance of the financial stability and well-being of credit unions generally.

The Central Bank's goal is for a resilient and trustworthy financial system, which sustainably serves the needs of the economy and its customers, in which firms and individuals adhere to a culture of fairness and high standards. From a prudential supervision perspective the Central Bank considers that regulated firms, including credit unions, should:

i. Have sufficient financial resources including under a plausible but severe stress scenario.
ii. Have sustainable business models.
iii. Be well governed, with appropriate cultures, effective risk management and control arrangements in place.
iv. Be able to recover if they get into difficulty, and if they cannot, they should be resolvable in an orderly manner without significant externalities or taxpayer costs.

Prudential requirements and limits, set out in regulations, play an important role in driving the adequacy of financial resources, building strong governance and effective risk management frameworks, and providing parameters to contain risks within acceptable levels. In this way the regulatory framework prescribes the minimum standards that industry must meet (with higher standards expected of those who undertake more complex activities) while requiring firms take ownership of their own risk frameworks.

In reviewing the lending framework for credit unions our overarching goal is to ensure that the scope and parameters of the lending framework are clear and are calibrated appropriately and reflect the competence and capability of credit unions. An appropriate lending framework should:

- Effectively manage duration risk and consider broader issues such as asset and liability management;
- Effectively manage concentration risk, both at a loan category and an individual borrower level;
- Facilitate credit risk diversification within loan portfolios; and
- Clearly define the scope and parameters of credit union lending categories.

A significant body of work has been undertaken over the past five years on developing and implementing a strengthened regulatory framework for credit unions. The strengthened regulatory framework for credit unions, which has been in place since late 2013, introduced detailed governance and risk management requirements for credit unions. Over this period credit unions have built their capital reserves with average sector reserves increasing from 14.5% in March 2013 to 16.5% in March 2018. Maintenance of capital strength, strong governance culture and the identification and mitigation of risks are core to ensuring the protection by each credit union of the funds of its members and the maintenance of the financial stability and well-being of the sector. The Central Bank is of the view that strong core foundations, evidenced by well governed credit unions with effective risk management and controls, are a necessary pre-requisite to facilitating changes to the regulatory framework. While some credit unions have demonstrated improvements in their governance and risk management frameworks, there are a significant number of credit unions where improvements are still required. The Central Bank is supportive of credit unions prudently developing their business model where they can demonstrate a clear vision and the capability to successfully implement that vision. An earned flexibility approach is being adopted by the Central Bank which supports such credit unions in delivering a broader range of products and services on a regulatory approval basis.

Lending Framework for Credit Unions

On 1 January 2016, section 11 of the Credit Union and Co-operation with Overseas Regulators Act 2012 (the 2012 Act) was commenced which substituted a new section 35 in the 1997 Act and provided regulation making powers to the Central Bank in relation to lending. The Credit Union Act 1997 (Regulatory Requirements) Regulations 2016 (as amended) (the 2016 Regulations) also commenced on 1 January 2016 with Part 4 of the 2016 Regulations setting out lending regulations for credit unions.

The 2016 Regulations outline the categories of lending which a credit union can undertake and contains certain concentration and a large exposure limit for lending. They also contain specific requirements in relation to lending practices. Loan maturity limits relating to the proportion of total loans which can be outstanding for periods exceeding 5 and 10 years, which were previously contained within the 1997 Act, are now contained within Regulation 14 of the 2016 Regulations. These limits are currently 30% and 10% of gross loans outstanding for 5 and 10 year maturities respectively but may be increased to 40% and 15% where a credit union is approved by the Central Bank to avail of increased limits. 15 credit unions have been granted approval for the increased lending maturity limits[1].

There has been significant engagement with the sector in relation to the existing lending framework with a particular focus on the impact of existing limits on the capacity for credit unions to undertake longer term lending including house loans. In November 2017, the Central Bank received a formal request from the Credit Union Advisory Committee (CUAC) Implementation Group[2] to review the section 35 lending limits. The Joint Committee on Finance, Public Expenditure and Reform, and Taoiseach (the Committee) also recommended[3] that a review of the section 35 limits be undertaken.

The Central Bank has previously expressed concerns at the sector's loan to assets (LTA) ratio and has cited it as one of the key sustainability challenges facing the sector given the negative impact on return on assets. Discussion by a number of credit unions has turned to the provision of mortgages. The Central Bank is supportive of credit unions increasing lending on a prudent basis, including engaging in new areas of lending and increasing exposure to longer term lending as part of a balanced loan portfolio. The Central Bank is of the view that a balanced loan portfolio, supported by strong risk management capability can increase diversification in loan books and help to manage credit concentration risks to which credit unions may be exposed. The Central Bank would caution however that all lending should be prudently undertaken, well-managed and in line with the credit union's strategy, capabilities and risk appetite. Credit unions should be aware of the risks and related considerations for new categories of lending including increased longer term lending. In this context in December 2017, the Central Bank published a paper entitled 'Longer

[1] As of 30th September 2018.
[2] This group consists of representatives from the Department of Finance, the credit union representative bodies and the Central Bank and is chaired by the Department of Finance.
[3] In November 2017 the Joint Committee on Finance, Public Expenditure and Reform and Taoiseach published a report on the Review of the Credit Union Sector with specific reference to the Credit Union Advisory Committee Review of Implementation of the Recommendations in the Commission on Credit Unions Report.

Term Lending- Guidance for Credit Unions'. This paper set out the Central Bank's guidance on what credit union boards seeking to increase longer term lending and provide house loans are expected to consider and address.

Changing Credit Landscape

Total household debt stood at c.€140.2bn at end Q1 2018, representing a 31% drop since its peak of c.€204.2bn at the end of Q3 2008[4].

The regulatory response to the financial crisis has seen the introduction of strengthened prudential requirements. Levels of required capital have been increased dramatically since the crisis while the ability of banks to absorb losses (and be recapitalised) has also been materially enhanced under the requirements of the Capital Requirement Directive and Capital Requirements Regulation, as well as the Bank Recovery and Resolution Directive. For liquidity, EU requirements for prudent liquidity management have also significantly increased since the crisis with banks required to hold significant levels of liquid assets (under the Liquidity Coverage Ratio) and to comply with stable funding requirements (under the Net Stable Funding Ratio). In February 2015, the Central Bank introduced mortgage measures aimed at enhancing the resilience of both borrowers and the banking sector. The measures set limits on the size of mortgages that consumers can borrow through the use of loan to value (LTV) and loan to income (LTI) limits. These regulatory changes have been accompanied by greater requirements relating to governance and risk management as well as staff remuneration. In addition, significant enhancements have been made to consumer protection requirements including the introduction of the Mortgage Credit Directive.

Competition in certain segments of the household credit market has intensified in recent years. A number of specialist lenders have entered the mortgage market targeting specific areas. Since 2015 growth in bank-related lending to Irish households for non-mortgage purposes has been driven by the growth in car-related debt, and in particular Personal Contract Plans (PCP)[5]. The presence of non-bank entities also offering PCPs for car purchase has added to competition in this segment of the credit market. Additionally, the rise of fintech is driving product and service innovation by established market players, with new market entrants attracted by lower cost operating models.

Taken together, all these factors have resulted in a dramatically changed landscape for those providing credit in Ireland, and credit unions should be aware of the potential impacts on their business.

Review of the Lending Framework

The Central Bank is of the view that proposals to increase long term lending should be considered by credit union boards in the context of the issues and requirements set out in our Longer Term Lending Guidance for Credit Unions. Any associated balance sheet transformation should consider maturity transformation and liquidity requirements and asset and liability management (ALM).

In order to ensure that the lending regulations remain appropriate for credit unions, the Central Bank initiated a review of the lending maturity limits in 2018. This review was undertaken in the context of:

[4]https://www.centralbank.ie/docs/default-source/statistics/data-and-analysis/financial-accounts/financial-accounts-data/financial-accounts-for-ireland-q1-2002-to-present---esa-2010.xlsx?sfvrsn=53
[5] Sherman, Martina; Heffernan, Tiernan and Cullen, Bryan, "An Overview of the Irish PCP Market", Central Bank Economic Letter Vol 2018, No. 2 pg.5.

- The Central Bank's statutory mandate to regulate and supervise credit unions with a view to ensuring the protection by each credit union of the funds of its members and the maintenance of the financial stability and well-being of credit unions generally;
- Sector engagements on business model development and longer term lending;
- Recent lending sector data and trends including data received from a questionnaire issued to the sector;
- The current lending framework; and
- Broader balance sheet considerations including ALM.

In April 2018, as part of pre-consultation for this review, the Central Bank requested that credit unions complete and submit a longer term lending questionnaire (the questionnaire). The questionnaire sought detailed information from credit unions on current and projected lending and savings. 181 credit unions completed and submitted this questionnaire. Submissions were collated and analysed and have informed the proposals contained in this consultation paper. Further information on the data collected via the questionnaire is contained in Section 3 of this paper.

Following this review the Central Bank is now consulting on potential changes to the lending framework contained in the 2016 Regulations which include a removal of maturity limits based on a percentage of outstanding loans and the introduction of tiered concentration limits for house and commercial lending. These changes reflect what the Central Bank views to be an appropriate prudent lending framework for credit unions taking account of their risk management and operational capabilities. The changes would provide all credit unions with some additional capacity to undertake personal lending and provide larger credit unions, who can demonstrate that they have the required financial strength and resilience, expertise, capability and risk management systems, additional capacity to undertake house and commercial lending. However, while credit unions have called for increased capacity to engage in longer term lending, the Central Bank is of the view that this is not the sole solution to the low LTA ratio and associated sustainability challenges facing the sector. This consultation paper sets out the potential changes to the lending regulations for credit unions, along with a Regulatory Impact Analysis (RIA), and seeks views from credit unions and other sector stakeholders on the potential changes outlined. This consultation paper also sets out areas for consideration by credit unions considering increasing longer term lending and/or longer term investments from an ALM and liquidity perspective.

The Central Bank will consider the feedback received as part of this consultation prior to finalising changes to the lending framework for credit unions and publishing a statutory instrument amending the lending regulations for credit unions. In addition, as part of the post implementation review, the Central Bank will perform and publish an analysis on credit union sector lending three years post commencement of new lending regulations for credit unions to assess and analyse the actual impact that the regulations have had.

The consultation paper is structured as follows:

- Section 2 sets out the purpose of this consultation;
- Section 3 provides an overview of the review undertaken;
- Section 4 provides an overview of the potential changes to the lending regulations that the Central Bank is considering following its review;
- Section 5 provides an overview of ALM and liquidity considerations;

- Section 6 provides commentary on a number of other considerations for credit unions seeking to engage in increased longer term lending;
- Section 7 provides an overview of the RIA undertaken;
- Section 8 outlines next steps in relation to the consultation;
- Section 9 summarises the areas where the Central Bank is seeking views;
- Section 10 sets out how to make submissions to the Central Bank;
- Appendix A sets out the lending requirements contained in the 2016 Regulations;
- Appendix B contains a table which compares the current lending framework to the proposals contained in the consultation paper;
- Appendix C contains the questionnaire on longer term lending which was issued to credit unions in April 2018; and
- Appendix D contains the full RIA.

2. Purpose of the Consultation

Following a review of the lending framework for credit unions, the Central Bank is considering a number of potential changes to the lending regulations for credit unions.

Views are sought in this consultation paper on:

- Potential changes to the lending framework for credit unions along with associated risk and ALM considerations – sections 4 and 5 of this consultation paper set out the potential changes and seek views on these.

The specific questions that credit unions and stakeholders are asked to respond to are set out throughout sections 4 and 5. These questions are summarised in section 9.

Detail on the RIA, that assesses the likely impact of potential changes to the lending framework, is set out in section 7. The full RIA is contained in Appendix D. Credit unions and other sector stakeholders may also wish to provide additional information or analysis they may have on the likely impact of the potential changes to the lending framework. This can be included in submissions to this consultation process.

3. Review

In order to ensure that the lending framework remains appropriate for credit unions taking account of the risk management capabilities, expertise and financial resilience of credit unions, a number of areas were considered as part of this review and have, in combination, informed the proposals contained in this consultation paper. These include:

- The Central Bank's statutory mandate to regulate and supervise credit unions with a view to ensuring the protection by each credit union of the funds of its members and the maintenance of the financial stability and well-being of credit unions generally;
- Sector engagements on business model development and longer term lending;
- Recent lending sector data and trends including data received from a questionnaire issued to the sector;
- The current lending framework; and
- Broader balance sheet considerations including in relation to ALM.

3.1 Sector Engagement

There has been significant engagement with the sector in relation to the existing lending framework with a particular focus on the impact of existing limits on the capacity for credit unions to undertake longer term lending. A number of stakeholders have expressed views that the current calibration of the limits is constraining the ability of credit unions to develop longer term lending business including the provision of house loans as credit unions do not have sufficient capacity to build a viable business line given the costs associated with putting appropriate systems and staff in place to support such a business line.

The CUAC Implementation Group submitted a paper to the Registrar of Credit Unions on 3 November 2017, noting the recommendation contained in CUAC's report on the Review of the Implementation of the Recommendations in the Commission on Credit Unions Report[6] published in July 2016, for a full review of lending limits and concentration limits, including the basis of the calculation of the limits together with the liquidity requirements attaching to same.

3.2 Current Sector Lending and Trends Over the past 5 years

As part of the review of the lending framework the Central Bank considered current credit union financial data and observed lending trends over the past five years from March 2013 to March 2018. Analysis of this data identified a number of key trends:

- **Sector Assets Growth:** Total sector assets have grown year on year during this period and are up from €13.8bn in 2013 to €17.2bn at March 2018.
- **Declining Loan to Assets Ratio:** The sector average loan to assets ratio in March 2013 was 35%. This has declined year on year and now stands at 27%.
- **Loan Category:** At March 2018, 96% of the average sector gross loans outstanding were personal loans and 1.7% average sector gross loans outstanding were house loans.
- **Loan Maturity:** The years 2014 to 2016 saw a decline in the average percentage of sector loans outstanding for greater than 5 and 10 years. However, since 2017 the average loan maturity has increased and surpassed levels reached in 2013. The average percentage of gross loans outstanding for more than 5 and 10 years is now 12.9%

[6] https://www.finance.gov.ie/wp-content/uploads/2017/05/CUAC-Review-of-Implementation-of-the-Recommendations-in-the-Commission-on-Credit-Unions-Report.pdf

and 2.1% respectively. Larger credit unions have a higher proportion of their total loans outstanding for periods of greater than 5 and 10 years.

- **Average Loan Size**: The average loan size in March 2018 was c.€6.6K. This has not changed significantly since March 2013 when it was c.€6.4K.
- **Loan Arrears:** The loan arrears profile has improved significantly across the sector and has reduced by over 65% in the past 5 years, from 20% at end of March 2013 to 7% at the end of March 2018.

Further detail on this analysis is set out in section 2 of the RIA which is appended to this consultation paper.

3.3 Regulatory Framework for Lending

Section 35 of the 1997 Act sets out provisions in relation to credit union lending and provides the Central Bank with regulation making powers in relation to lending. The lending section of the 2016 Regulations sets out:

- the types of loans that a credit union may provide;
  - personal loans;
  - commercial loans;
  - community loans;
  - house loans; and
  - loans to other credit unions.
- concentration limits for certain types of lending;
  - outstanding commercial loans cannot exceed 50% of regulatory reserves;
  - outstanding community loans cannot exceed 25% of regulatory reserves; and
  - outstanding loans to other credit unions cannot exceed 12.5% of regulatory reserves.
- a large exposure limit – maximum exposure to a borrower or group of borrowers who are connected of €39,000 or 10% of the regulatory reserve of the credit union, whichever is greater;
- a maximum maturity limit of 25 years for all lending; and
- specified limits for loans over 5 years and 10 years maturity.

3.3.1 Maturity Limits

Background

As outlined in Appendix A, Regulation 14 of the 2016 Regulations provides that a credit union may have up to 30% and 10% of total gross loans outstanding for a period of greater than 5 and 10 years respectively. Where a credit union engages in the maximum permitted lending over 10 years, the lending capacity within the 5 to 10 year maturity category is reduced. For example if a credit union has 5% of total gross loans outstanding for a period of more than 10 years, it may have 25% of gross loans outstanding for a period of between 5 and 10 years.

Regulation 14 also provides that where the Central Bank so approves in writing, these limits may be increased to 40% and 15% for lending greater than 5 and 10 years respectively.

The Section 35 Regulatory Requirements for Credit Unions (October 2013) set out additional liquidity requirements (to those contained in the 2016 Regulations) for any credit union that wishes to increase its lending outstanding for greater than 5 years above 20% of total gross loans outstanding. The additional liquidity requirements are set out in table 1 below and these requirements must be met before the credit union may increase its lending over five years.

Table 1 | Additional Liquidity Requirements for Credit Union Lending Over 5 Years

Lending Over 5 Years as a % Gross Loans Outstanding	Minimum Liquidity Ratio
> 20% and < 25%	At least 25%
≥ 25% and < 29%	Over 25%
≥ 29%	At least 30%

Source: Section 35 Regulatory Requirements for Credit Unions

Current Permitted Lending > 5 and > 10 Years

Based on March 2018 Prudential Return data submitted by credit unions and based on lending at that date, the current lending maturity limits (30% lending > 5 years and 10% of lending > 10 years) provide, at a maximum, for €1.36bn and €0.45bn of sector loans to have a maturity of greater than 5 and 10 years respectively. If all credit unions applied for and were approved to avail of the increased lending maturity limits provided under Regulation 14 of the 2016 Regulations, this would increase capacity for loans with a maturity of > 5 years and > 10 years to c.€1.8bn and c.€0.68bn respectively.

Longer term lending maturity limits are currently linked to the amount of shorter term lending outstanding. It is recognised that the current low LTA ratio of 27% limits the scope for credit unions to undertake longer term lending. A higher LTA ratio would result in increased scope for credit unions to engage in lending greater than 5 and 10 years and would increase their scope for engaging in increased house and commercial lending, which traditionally has a longer duration. Table 2 illustrates what the 5 and 10 year maturity limits would translate to based on an illustrative sector LTA ratio of 50% and compares this to the amount permitted for longer term lending based on the current sector LTA ratio. This illustrates that if the sector LTA was on average 50% then credit unions would have capacity to engage in close to €2.6bn of lending for periods of greater than 5 years and close to €0.9bn for a period of greater than 10 years. This analysis highlights the consequence of the calibration of the current maturity limits as a percentage of total loans that result in the level of longer term lending permitted being dependent on the total level of lending which can vary depending on the demand for credit. This scenario could have pro-cyclical impacts on the sector depending on overall credit flows.

Table 2 | Permitted Maximum Lending > 5 and > 10 Years based on Different Loan to Assets Ratio and Total Assets at 31 March 2018

	Current Loan to Assets Ratio 27% permits:	Illustrative Loan to Assets Ratio 50% would permit:	% Increase in Capacity with a Higher Loan to Assets Ratio
Lending > 5 Years (30% of total loans)	€1.36bn	€2.59bn	90.4%
Lending > 10 Years (10% of total loans)	€0.45bn	€0.86bn	91.1%
If approval granted to avail of increased maturity limits:			
Lending > 5 Years (40% of total loans)	€1.8bn	€3.45bn	91.6%
Lending > 10 Years (15% of total loans)	€0.68bn	€1.29bn	89.7%

Source: Credit Union Prudential Returns and Central Bank Analysis

Current Utilisation of Lending Maturity Limits

Based on March 2018 Prudential Return data submitted by individual credit unions, €725m or 12.9% on average of sector loans are outstanding for a period of greater than 5 years. The data also shows that €163m or 2.1% on average of sector loans are outstanding for a period of greater than 10 years. This data highlights that at a sector level there is significant scope available to increase lending above 5 and 10 years, although there are a small number of credit unions whose total lending above 5 and 10 years is at or close to the limits permitted under the 2016 Regulations. The Central Bank recognises that for some credit unions the headroom provided may not be sufficient to warrant the significant investment required to increase longer term lending.

The following table summarises the maturity profile of credit union sector lending > 5 and > 10 years.

Table 3 | % of Credit Union Lending > 5 and> 10 Years based on March 2018 Prudential Return

Lending > 5 Years		Lending > 10 Years	
Lending > 5 Years as a % Total Loans	No. of Credit Unions	Lending > 10 Years as a % Total Loans	No. of Credit Unions
< 5%	52	< 5%	222
≥ 5% and < 10%	57	≥ 5% and < 10%	36
≥ 10% and < 15%	49	≥ 10% and < 15%	4
≥ 15% and < 20%	48	≥ 15%	1
≥ 20% and < 25%	35		
≥ 25% and < 30%	18		
≥ 30% and < 35%	3		
≥ 35% and < 40%	1		
Total	**263**	**Total**	**263**

Source: Credit Union Prudential Returns

The additional capacity available at a sector wide level for increased lending above 5 and 10 years (based on the existing framework and additional approvals granted therein and on the current LTA ratio) is illustrated in table 4 below for credit unions by asset category:

Table 4 | Additional Lending Capacity for Lending > 5 Years and > 10 Years (under the existing framework)

	Lending > 5 Years	Lending > 10 Years
Credit Unions Total Assets ≥€100 million	€0.359bn	€0.157bn
Credit Unions Total Assets ≥€40 million and < €100 million	€0.216bn	€0.108bn
Credit Unions Total Assets <€40 million	€0.134bn	€0.062bn
Total	**€0.709bn**	**€0.327bn**

Source: Credit Union Prudential Returns and Central Bank Analysis

3.3.2 Concentration Limits

The 2016 Regulations prescribe concentration limits for certain categories of lending namely commercial loans, community loans and loans to other credit unions. There is no concentration limit contained in the regulatory framework for house loans.

The current concentration limit for commercial lending is 50% of regulatory reserves. Any commercial loan issued with a value of less than €25,000 does not currently utilise this concentration limit. There are specific underwriting and reporting requirements also contained in the 2016 Regulations for commercial loans granted for greater than €25,000. At a sector level this concentration limit provides scope for commercial lending in the region of €946m, for all commercial loans granted in excess of €25,000. Based on March 2018 Prudential Return data, at an overall sector level there is €84m outstanding in commercial loans, €46m of which relates to commercial loans granted for more than €25,000.

3.3.3 Large Exposure Limit

The 2016 Regulations place a limit on the maximum exposure to an individual borrower or a group of borrowers which are connected. This is currently limited to 10% of regulatory reserves or €39,000 whichever is the greater. This is aimed at ensuring that a credit union does not have an undue concentration in terms of an exposure to an individual borrower or a group of borrowers who are connected.

3.4 Longer Term Lending Questionnaire

To help inform the review of the credit union lending framework and to get individual credit union input, the Central Bank issued a longer term lending questionnaire to credit unions on 11 April 2018 and advised that responses received to the questionnaire would be analysed and would help inform the proposals contained in this consultation paper. The responses were considered and reviewed in the context of what is considered prudentially appropriate for credit union lending.

The questionnaire sought additional information on current lending and savings in credit unions (to supplement the information available from the Prudential Returns which credit unions submit to the Central Bank on a quarterly basis). In addition, the questionnaire sought views on whether the existing maturity limits are sufficient to meet forecasted loan activity of the credit union for future periods out to 30 September 2022. Where a credit union did not view that the limits are sufficient they were requested to provide further information on forecasted lending and savings activity for year ends to 30 September 2022 including the forecasted split of loans between loan categories and maturity buckets. These forecasted figures were requested to be provided on the assumption that no lending maturity limits applied. In addition, credit unions were afforded an opportunity to provide any commentary which they have on credit union lending. A template of the questionnaire which was issued is contained for information at Appendix C.

The Central Bank would like to thank all credit unions who provided a response to the questionnaire. There was a high response rate to the questionnaire with 181 responses received. The Central Bank liaised with a number of credit unions on a bilateral basis to clarify certain matters in the questionnaires which had been submitted in order to ensure data quality and consistency. Following this engagement it was necessary for nine questionnaires to be omitted from the sample as either the credit unions did not respond to requests for resubmission of the questionnaire on a timely basis or data inconsistencies remained in resubmitted questionnaires. The remaining 172 credit unions formed the data set which was used for analysis of credit union questionnaire responses (the data set). This analysis is summarised below. More detailed presentation of the results of the questionnaire is presented in the RIA accompanying this consultation paper.

Table 5 provides a breakdown of the number of credit union responses within each category of credit union by asset size. The response rate to the questionnaire represents c.65% of total credit unions by number and c.81% of credit union sector assets. The category of credit unions which provided the highest response rate to the questionnaire were those credit unions with total assets of greater than €100 million.

Table 5 | Profile of credit unions responding to the questionnaire

Credit Union By Asset Size	No of Credit Unions who submitted questionnaire	% Response Rate	% Coverage of Credit Union by Asset Size
Credit Unions Total Assets ≥€100 million	47	88.7%	91.5%
Credit Unions Total Assets ≥€40 million and < €100 million	58	72.5%	72.3%
Credit Unions Total Assets <€40 million	67	51.5%	56.8%
Total	**172**	**65.4%**	**80.5%**

Source: Credit Union Longer Term Lending Questionnaire

Questions 1 to 5 of the questionnaire sought additional information on credit union lending including the types of lending which fall within personal lending, more granular information on loan maturities than that which is provided in the Prudential Return, information on secured/unsecured lending split for personal and commercial loans and data on the interest rates charged on loans. In addition, information on the age profile of credit union savers and borrowers was requested. A high level overview of the questionnaire responses is summarised below (all data provided is for the period 31 March 2018):

<u>**Personal Loans**</u>

- On average 30% of personal loans are car loans and 28% are home improvement loans.
- c.50% of personal loans have a maturity of between 3 and 5 years with only 1% of personal loans having a maturity of > 10 years.

<u>**House Loans**</u>

- Close to 44% of questionnaire respondents currently engage in house loans with a total amount outstanding of €148 million provided through c.2,200 house loans.
- On average, 53% of house loans are outstanding for a period of greater than 10 years.

<u>**Commercial Loans**</u>

- Just over 54% of survey respondents engage in commercial lending with a total amount outstanding of €64 million provided through c.3,950 loans.
- Over 60% of commercial loans have a maturity of less than 5 years and 93% have a maturity of less than 10 years.

<u>**Age Profile of Savers and Borrowers**</u>

- Over 50% of savings of questionnaire respondents are held by members aged 55 years and over.
- Approximately 72% of loans outstanding are outstanding to borrowers who are aged below 55.

In responding to question 6 of the questionnaire, which asked if respondents felt that the current lending limits are sufficient to meet forecasted loan demand over the next 5 years, 63 credit unions indicated that the current lending maturity limits are not sufficient for them to meet forecasted loan demand out to 30 September 2022. This represented approximately 36% of the 172 credit unions included within the data set. Table 6 displays the number of credit unions within each category who indicated that a change in the maturity limits is necessary in order for them to meet lending demand out to 30 September 2022 - as can be seen, a higher proportion of credit unions with total assets of at least €100 million indicated this than any other category of credit union.

Table 6 | Profile of credit unions indicating that lending maturity limits are not sufficient to meet loan demand

Credit Union By Asset Size	No of Credit Unions	No of Credit Unions included in overall sample	% of Respondents
Credit Unions Total Assets ≥€100 million	37	47	78.7%
Credit Unions Total Assets ≥€40 million and < €100 million	13	58	22.4%
Credit Unions Total Assets <€40 million	13	67	19.4%
Total	**63**	**172**	**36.6%**

Source: Credit Union Longer Term Lending Questionnaire

These 63 credit unions provided further information on forecasted loan and savings activity in their credit union out to 30 September 2022. Data analysis on this information can be summarised as follows:

- These credit unions have a current loan to asset ratio broadly in line with the sector average of 27.4%. This is forecast to grow to 34.2% by 2022 for these credit unions.
- These credit unions have a higher proportion on average of gross loans outstanding for more than 5 and more than 10 years. They have 19.2% of total loans outstanding for a period of greater than 5 years and 4.6% outstanding for a period of greater than 10 years.
- The maturity profile of loans is forecast to increase on a gradual basis year on year in both the greater than 5 year and greater than 10 year maturity categories where it is forecast to represent 31.6% and 11.4% of gross loans outstanding by 2022. Expressed as a percentage of total assets this equates to 11.1% and 4.1% of total assets outstanding for a period of greater than 5 and greater than 10 years respectively.
- Forecast data suggests a slight change in the categories of lending which will be undertaken with increases forecast in commercial and house lending. The average percentage of total loans outstanding by loan category in March 2018 and September 2022 is displayed in table 7 below.
- There is no significant change forecast in respect of the funding profile of these credit unions over the forecast time period. Currently 98% of these credit unions' savings are on-demand, by 2022 this is forecast to have reduced slightly to 94%.

Table 7| Profile of Current and Forecasted Credit Union Lending by Loan Category

Loans by Category as a % of Total Loans	March 2018	September 2022
Car Loans	28.1%	24.5%
Home Improvement Loans	25.6%	24.8%
Education Loans	3.3%	3.5%
Other Personal Loans	35.6%	30.8%
Commercial Loans	2.9%	5.6%
House Loans	4.5%	10.8%

Source: Credit Union Longer Term Lending Questionnaire

The figures presented above in relation to the questionnaire analysis are the average of all survey respondents included in the data set. While the response analysis on categories of credit union by asset size did not differ significantly to the averages presented above, there were some individual credit union responses which did vary significantly to the averages presented above. Further detail on the data analysis from the questionnaire responses received can be found in Section 2 of the RIA.

Commentary provided in questionnaire

Question 11 of the longer term lending questionnaire provided an opportunity for credit unions to make any additional comments which they had in relation to longer term lending in their credit union. Over 60% of respondents to the questionnaire answered this question. The commentaries provided by respondents were wide ranging but the overarching message is that the majority of credit unions have called for a change of the lending maturity limits (this is also the request from many of those credit unions that anticipate they can meet projected member loan demand for the next 5 years within the current limits). It was suggested that amended lending limits are required to strengthen credit union business model growth, sustainability and viability and that a change is necessary for developing an expanded product offering and an enhanced, more prudently configured, loan portfolio mix. Some respondents put forward suggestions on what the new limits should be including that the limits should be set as a percentage of total assets and that they should be calibrated in a more sophisticated manner based on a combination of metrics such as risk profile, liquidity and savings behaviour. There was an acknowledgement from a number of respondents that increased longer term lending should be supported by a robust ALM system.

4. Lending Proposals

Section 84 of the 1997 Act outlines that the Central Bank shall administer the system of regulation and supervision of credit unions with a view to ensuring (i) the protection by each credit union of the funds of its members and (ii) the maintenance of the financial stability and well-being of credit unions generally. In considering amendments to the lending framework for credit unions, in addition to the statutory mandate the Central Bank has been informed by a number of other factors including engagements with the sector on lending, the current profile of sector lending, the current regulatory framework, and data analysis of questionnaire responses.

The Central Bank recognises that the provision of loans to members is a core function of credit unions. The proposals for amendments to credit union regulations contained in this consultation are guided by what is considered prudentially appropriate for credit union lending and takes account of the risk management and operational capabilities of credit unions.

The Central Bank is supportive of credit unions growing their loan books on a prudent basis, recognising that some of this growth may come from longer term lending as part of a balanced loan portfolio, to diversify credit risk by borrower, loan category and duration. The Central Bank recognises the limitations associated with the current calibration of longer term lending limits (expressed as a percentage of total lending). However, it is important to recognise that increasing longer term lending, including the provision of house loans, will not on its own address the sector's sustainability challenges.

As set out above the credit landscape has undergone fundamental change since the financial crisis and the re-scaling of the credit market combined with higher regulatory standards and increasing competitive pressures will present challenges to credit unions intending to grow their lending and provide new credit products. The Central Bank would caution that growth in loan books should not result in imbalanced loan portfolios with excessive exposures to a particular category of loan, a particular borrower or group of connected borrowers or a specific maturity category. Similarly consideration needs to be given to the ALM implications of growth in longer term lending as part of a balanced loan portfolio. It is important that credit unions who wish to change the profile of their lending understand the specific risks and profitability profiles and how this change in lending profile fits within the credit union's lending strategy, risk appetite and capabilities. Changes to the lending profile of a credit union must be supported by critical enablers such as the necessary competence, skills, expertise and risk management and operational frameworks to ensure that such specialised lending is appropriately managed. Where credit unions are considering increasing longer term lending and/or expanding house lending it is important that they identify the risk factors specific to longer term lending and also those unique to house loans and how they would mitigate these risks.

Section 5 sets out a number of key areas for consideration by credit unions prior to them significantly changing the profile of their loan books. The Central Bank expects credit union boards to assess any strategic plans on long term lending in the context of the issues set out in the Long Term Lending – Guidance for Credit Unions, issued in December 2017.

In summary, having undertaken the review described in section 3, the Central Bank is proposing a number of changes to the lending framework for credit unions as follows:

i. Removal of the 5 year and 10 year lending maturity limits contained in Regulation 14 of the 2016 Regulations;
ii. Introduction of a maximum loan term of 10 years for unsecured lending;
iii. Introduction of a combined concentration limit (expressed as a percentage of total assets) for house and commercial lending for all credit unions on a tiered basis;
iv. Re-name and re-define the commercial loan category; and
v. Introduction of a prescribed large exposures amount for credit union lending.

Further detail and the rationale for each of these proposals is outlined in the following sections and the Central Bank welcomes views on each of these areas.

4.1 Removal of 5 and 10 Year Lending Maturity Limits

The 2016 Regulations place a restriction on the maximum amount of loans which may be outstanding for periods of greater than 5 years and greater than 10 years. These limits are currently 30% and 10% of gross loans for 5 and 10 year maturities respectively, but these limits may be increased to 40% and 15% respectively where a credit union is approved by the Central Bank to avail of increased limits.

Data analysis indicates that at a sector level there is significant scope for further utilisation of the lending maturity limits (the current average lending > 5 years is 12.9% and > 10 years is 2.1%). However, the Central Bank acknowledges that there are a number of credit unions who are operating at close to the maximum lending maturity limits permitted under the 2016 Regulations. These credit unions tend to have a higher proportion of their overall lending exposed to house and/or commercial loans, and it has been suggested via sector engagements that the lending maturity limits may be restricting their ability to consider more material increases in longer term lending. Existing lending limits have no impact on the capacity of credit unions to issue personal loans in the 0 to 5 year maturity category however, it is acknowledged that underutilisation of the lending maturity limits may be somewhat related to the cost/benefit of utilising these limits. For example it may not be a viable business proposition for a credit union to undertake a small number of mortgages given the systems and expertise required to undertake such business.

In addition, the sector has articulated concerns with the basis for the lending maturity limits which currently expresses the limits as a percentage of total loans. It is viewed that this constrains the capacity available to credit unions to increase their longer term lending as short term lending must be increased in order to provide additional scope for longer term lending. As illustrated in section 3.3.1, the current Section 35 lending limit calibration has a constraining impact on credit unions in that it is not possible to grow longer term lending without growing shorter term lending. This issue has been exacerbated due to the low loan to asset ratios at present in credit unions. As short term lending has contracted (due to reduced demand for short term unsecured credit), it has impacted on the capacity of some credit unions to undertake longer term lending.

Data gathered through the questionnaire has provided details on the maturity profile of loans by lending category. This data analysis suggests that it is predominantly house and commercial loans which have longer term maturities with c.89% and c.39% of house and commercial loans respectively having a maturity of greater than 5 years. Conversely the maturity profile of personal loans outstanding indicates that only c.12% are outstanding for greater than 5 years. Similarly, the forecasted lending data provided by questionnaire respondents indicates that they expect house loans will have longer maturities going forward.

Taking all of the above into account, the Central Bank considers that it may be more appropriate and effective to manage loan book duration and concentration risk by reference to the type of lending in which the credit union engages to ensure appropriate prudential oversight of exposures to loans which by their nature tend to be higher risk and have longer maturities. The Central Bank is proposing the removal of the 5 year and 10 year overall maturity lending limits contained in Regulation 14 of the 2016 Regulations and the introduction of a combined concentration limit expressed as a percentage of assets for house and commercial lending and a number of other changes to the lending framework. This suite of changes, when taken together, will in effect allow for the management of loan book maturities. In addition, they will increase the flexibility of individual credit unions to manage the composition of their loan books through the removal of the limit on personal lending with maturity between 5 and 10 years, and the provision of scope to gain exposure to specific categories of lending and specific maturity profiles, within the stated risk appetite for lending and risk and operational capabilities of individual credit unions. This will permit credit unions to undertake balance sheet transformation in line with their aspirations in terms of serving member needs, while developing well balanced loan portfolios.

The Central Bank is seeking views on the following:

1. Do you have any comments on the proposal to remove the 5 year and 10 year lending maturity limits contained in Regulation 14 of the 2016 Regulations (taking account of the other changes to the lending framework)?

4.2 Maximum Loan Maturity for Unsecured Loans

The 2016 Regulations place an overall maximum term of 25 years on any credit union loan. The removal of the lending maturity limits which are contained in Regulation 14 of the 2016 Regulations increases the scope for credit unions to increase longer term lending. Longer term lending by its nature has an increased risk profile relative to shorter term lending. The Central Bank views that the 25 year maximum maturity term remains appropriate taking account of the funding profile of credit unions. In addition, it is not viewed that this maturity term will limit to a material extent the capacity for credit unions to engage in increased longer term lending.

Notwithstanding that the data analysis of both current and forecasted lending suggests that the majority of lending > 5 years and > 10 years is and will be comprised of house loans and to a lesser extent commercial loans, the removal of the lending maturity limits introduces a risk that the maturity profile of other credit union lending extends and as a result could increase the level of duration risk in the loan book and by extension in the overall asset maturity profile of the credit union. In order to mitigate against this risk, the Central Bank proposes to introduce a maximum maturity limit for unsecured loans of 10 years. In proposing this change, the Central Bank views that it would not be best practice from an underwriting perspective for an unsecured loan to be advanced for a period of greater than 10 years.

The Central Bank also proposes to introduce a definition for a secured loan in the regulations to provide clarity on what loans are subject to the maximum maturity limit of 10 years. The proposed definition for a secured loan is as follows:

A ***secured loan*** is any loan which is secured by way of:

i. a first legal charge on property;
ii. a pledge of shares; or
iii. an assignment of a deposit.

An ***unsecured loan*** is any loan which is not a secured loan.

The Central Bank is seeking views on the following:

2. Do you have any comments on the proposal to introduce a maximum maturity limit of 10 years for unsecured loans?
3. Do you have any comments on the proposed definition of a secured loan?

4.3 Concentration Limit for House and Commercial Loans on a Tiered Basis

The 2016 Regulations prescribe commercial and house loans as permitted categories of loans for credit unions. They also prescribe a concentration limit for commercial lending of 50% of regulatory reserves. The 2016 Regulations further prescribe that only commercial loans issued for €25,000 or greater utilise this concentration limit. There are specific underwriting and reporting requirements contained in the regulations for commercial loans granted which are >€25,000.

The Central Bank is proposing the removal of the provision contained in the 2016 Regulations whereby the concentration limit for commercial lending is not utilised for commercial loans granted which are less than €25,000. This is to ensure that all exposures to commercial loans are captured under the concentration limits proposed. The 2016 Regulations contain lending practices for specific categories of lending whereby a commercial loan may only be granted where a comprehensive business plan and detailed financial projections are provided and in place before granting the loan. In addition it is required that a performance report in writing on such loans shall be provided to the board of directors on a monthly basis. Commercial loans granted for less than €25,000 are currently excluded from these lending practice requirements and the Central Bank does not propose any changes in this regard.

The Central Bank intends introducing board reporting requirements on the performance of house loans similar to the reporting requirements contained in the 2016 Regulations for commercial loans in acknowledgement of the different credit risk profile which these loans present versus traditional credit union lending.

The definition of a house loan contained in the 2016 Regulations refers to a loan to a member secured by property for the purpose of enabling the member to:

(a) have a house constructed on the property as their principal residence;

(b) improve or renovate a house on the property that is already used as their principal residence;

(c) buy a house that is already constructed on the property for use as their principal residence; or

(d) refinance a loan previously provided for one of the purposes specified in (a), (b) or (c) for the same purpose.

The definition of a house loan does not include a house loan for the purchase of buy to let property. It has come to the attention of the Central Bank that in some instances loans are being granted for buy to let property purchases under the commercial loan lending category. The Central Bank intends to state, through revised regulations, that a loan made for the purchase of buy to let residential or buy to let commercial property is prohibited under the credit union lending framework. This prohibition on buy to let loans takes account of credit union risk management and operational capabilities and what is prudentially appropriate for credit union lending given the higher risk profile of this type of lending.

As outlined above, the Central Bank proposes to introduce a combined concentration limit for house and commercial loans which will place a maximum amount on the exposure which a credit union can have to these loan categories. This could be applied on a tiered basis. Given that the majority of loans with maturities of greater than 5 and 10 years are granted as house or commercial loans[7], this concentration limit will also help to ensure that the maturity profile of credit union lending remains appropriate and does not result in a disproportionate amount of credit union balance sheets being held in longer term assets. In particular, this concentration limit will contribute to helping to ensure balanced loan portfolios for individual credit unions.

Base Concentration Limit for House and Commercial Loans

The Central Bank proposes a combined house loan and commercial loan concentration limit of 7.5% of Total Assets of the credit union. This base limit would be available to all credit unions. The linking of this limit to Total Assets will ensure that a credit union's potential to engage in house and commercial lending is not constrained by reference to its overall lending and will provide increased flexibility to credit unions as regards loan book composition. In addition to this concentration limit, the Central Bank is proposing that within this concentration limit no more than 5% of Total Assets may be exposed to a specific category of lending i.e. no more than 5% of Total Assets may be in commercial loans or no more than 5% of Total Assets may be in house loans. These limits have been arrived at taking account of the governance, risk management and related capabilities of credit unions to engage in these categories of lending as evidenced through the Central Bank's supervisory findings across the credit union sector.

Given the longer term nature of house and commercial lending and the balance sheet implications of an increase in this type of lending, this concentration limit has also been developed taking into account the allowable amount available to all credit unions to invest in Tier 3 Approved Housing Bodies (AHBs) under the investment framework. Such investments by their nature are longer term with a permitted maximum maturity of 25 years under the regulations. The 2016 Regulations permit a credit union to invest in Tier 3 AHBs up to 25% of regulatory reserves. Where a credit union has total assets of at least €100 million Tier 3 AHB investment can be increased up to 50% of regulatory reserves.

The Central Bank is seeking views on the following:

4. Do you have any comments on the proposal to require that all commercial loan exposures utilise the concentration limit for commercial lending?
5. Do you have any comments on the Central Bank's intention to introduce board reporting requirements for house loans?
6. Do you have any comments on the proposal to introduce a base combined concentration limit for house and commercial loans of 7.5% of Total Assets?
7. Do you have any comments on the proposal to limit the maximum amount of house or commercial lending which a credit union may undertake to 5% of Total Assets within the base combined concentration limit?

Tiered Concentration Limit for House and Commercial Loans

The Central Bank views that it may be appropriate for an increased concentration limit for house and commercial lending to be available to certain credit unions who can demonstrate with appropriate evidence that they have strong core foundations including the skills, expertise, risk management and operational capability to undertake an increased element of lending in these loan categories via an approval process. In addition, credit unions seeking to avail of this

[7] Based on data provided on sector questionnaire.

increased concentration limit will be required to demonstrate that they have financial strength and resilience including a strong reserve and liquidity position and a clear understanding and appreciation of the specific risks associated with this type of lending. They will also be required to outline how they propose to address and mitigate these specific risks.

The Central Bank proposes that the increased combined concentration limit for house and commercial loans, for those credit unions who demonstrate that they have strong core foundations to undertake additional house and commercial lending, would be 15% of Total Assets. The Central Bank considers that it is only those credit unions of sufficient scale who would have the capability to avail of this increased concentration limit - credit unions with total assets of at least €100 million may be indicative of those credit unions who will be capable of demonstrating the necessary scale, available resources and capability to undertake increased house and/or commercial lending.

The Central Bank envisages that, in order for a credit union to avail of this increased concentration limit, it would submit an application accompanied by a robust business case clearly setting out the rationale for requesting the additional capacity to undertake house and commercial lending and a clear understanding of the profitability implications of entering into these markets to a more significant degree. Additionally, applicant credit unions will need to be able to demonstrate that they clearly understand the risks associated with this type of lending and have the capabilities and systems to mitigate these risks appropriately. This application would be required to provide projections on how the credit union would make use of an increased lending capacity in house and commercial lending and give consideration to broader ALM implications. Only where the Central Bank approves the application would the credit union be permitted to avail of the increased limit. A phased approach to utilisation of additional capacity to undertake house and commercial lending will ensure that such lending is originated over the economic cycle. It is our intention to require credit unions to use the additional capacity to issue house and commercial loans in a gradual/phased way. This would be set as a condition of any approval for an individual credit union to avail of increased concentration limits for house and commercial lending.

The Central Bank is seeking views on the following:

8. Do you have any comments on the proposal to permit an increased combined concentration limit for house and commercial loans for those credit unions who can demonstrate the necessary financial strength, skills, expertise, operations and risk management capability to undertake increased lending in these loan categories?
9. What skills, expertise, operational and risk management capabilities do you consider necessary to support increased lending in house and commercial loans?
10. Do you have any comments on the proposed increased combined concentration limit for house and commercial lending of 15% of Total Assets?
11. Do you have any comments on the application process referred to above?

4.4 Re-name and Re-define Commercial Loans Loan Category

The 2016 Regulations define a commercial loan as a loan, the primary objective of which is to fund an activity whose purpose is to make a profit. Credit unions currently undertake a small amount of commercial lending which is largely small scale in nature focusing on small business and agricultural lending.

The Central Bank is proposing to re-name the ‘commercial loan’ lending category to ‘small business loan’ lending category, as it is viewed that this would more accurately reflect the lending which credit unions undertake in this area. The proposed definition for a small business loan is ‘*a loan made for the purpose of financing the working capital or capital* *investment needs of owner managed small business enterprise'*. A small business enterprise would also require to be defined and it is anticipated that this definition would reflect the definitional approach to small and medium sized enterprises under European Union law i.e. the criteria currently applicable to lending to micro and small enterprises currently contained in S.I. No. 585/2015 - Central Bank (Supervision and Enforcement) Act 2013 (Section 48) (Lending to Small and Medium-Sized Enterprises) Regulations 2015.

If the commercial loan lending category is re-named and re-defined, it is the Central Bank's intention that the concentration limit outlined in section 4.3 above for house and commercial lending would apply to the new loan category of small business lending and all small business loans granted, regardless of size, will utilise these proposed concentration limits. In addition, it is the Central Bank's intention that the additional requirements for commercial loans, with a value of €25,000 or greater, contained in the 2016 Regulations would continue to apply to the small business loan category.

As outlined above, the Central Bank intends to state in the regulations that buy to let residential and buy to let commercial property lending is prohibited under the lending framework.

The Central Bank is seeking views on the following:

12. Do you agree with the proposal to re-name the commercial loan lending category to small business loan?
13. Do you have any comments on the proposed definition for a small business loan?

4.5 Large Exposures

The 2016 Regulations contain a large exposure limit which places a limit on the maximum total exposure a credit union can have to a borrower or group of borrowers who are connected. This is currently set at €39,000 or 10% of the regulatory reserve of the credit union, whichever is greater.

The Lending Chapter of the Credit Union Handbook contains guidance on large exposures. The Central Bank is of the view that, notwithstanding the large exposure limit for credit unions contained in the 2016 Regulations, credit unions should remain cognisant of the credit risk posed by any large exposures which they have. This is of particular importance for credit unions who engage in increased house and commercial lending as loans advanced for these purposes are likely to have larger individual loan size than traditional credit union loans.

The Central Bank is proposing to amend the lending regulations to embed the principal of large exposures. It is proposed that a large exposure will be prescribed as any exposure to a borrower or group of borrowers who are connected of 2.5% or greater of the regulatory reserves of the credit union. This proposal will ensure that a proportionate approach is taken in the application of large exposures as the value of total exposures which is defined as a large exposure will increase as the assets and accordingly the regulatory reserves of the credit union increase. For example, assuming a credit union has a 10% regulatory reserve, a large exposure in a €400 million asset size credit union would be a total exposure to a borrower or group of connected borrowers of €1 million or greater while in a €60 million asset size credit union a large exposure would be a total exposure to a borrower or group of connected borrowers of €150,000 or greater.

From a prudential perspective, the introduction of a large exposures regime allows for the management and monitoring of borrower concentration risk by credit unions. A large exposure regime exists for other credit institutions under the Capital Requirements Directive/Capital Requirements Regulation. Post commencement of amending lending regulations for credit unions the Central Bank intends to enhance the current reporting framework to gather additional information on large exposures to require reporting on, at a minimum, the number and aggregate value of all large exposures held by the credit union including reporting such large exposures on a loan category basis.

The maximum large exposure limit of €39,000 or 10% of the regulatory reserves of the credit union will remain in the Regulations. At this time, the Central Bank is not proposing to include an aggregate large exposure limit, which would limit the total number of large exposures which a credit union could have in the lending regulations. The proposed concentration limits for house and commercial lending will act as an effective limit on the number of large exposures that a credit union may grant, as these are the loans that are likely to be of higher value for credit union lending.

The Central Bank is seeking views on the following:

14. Do you agree with a large exposure being prescribed as an exposure to a borrower or group of borrowers who are connected of 2.5% or greater of the regulatory reserves of the credit union?

4.6 Transitional Arrangements

On introduction of any amendments to the lending framework, the Central Bank proposes to introduce a transitional arrangement which would allow for any loans which are not in compliance with the amended lending framework to be held to maturity. This transitional arrangement would only apply to those loans which were in compliance with the applicable lending framework at the time the loan was granted.

The Central Bank is seeking views on the following:

15. Do you have any comments on the proposed transitional arrangements?

5. Liquidity and Asset and Liability Management

The Central Bank is of the view that the proposals set out in section 4 address the rigidity associated with the current calibration of the longer term lending limits and introduce an appropriate level of flexibility to the lending framework for credit unions including an increase in the capacity for some credit unions to undertake longer term lending including house loans. Such increased capacity for longer term lending would only be available where credit unions have strong core foundations backed up by financial resilience including a strong capital and liquidity position. The proposals contained in this consultation paper take account of the current liquidity position of credit unions, the composition of liquidity and the quality of liquid assets held across the sector.

Credit unions considering any significant change in the profile of their loan books will have to give careful consideration to the consequential impacts. Moving beyond traditional short term lending represents a significant step change for any individual credit union. Balance sheet transformation toward a higher proportion of longer term lending requires appreciation of the associated risks including liquidity and ALM considerations and how to mitigate these risks. When considering balance sheet transformation credit unions also need to consider the combined impact of longer term investments and longer tem lending on ALM. The broader considerations for credit union boards when assessing long term lending activities are set out in the Central Bank's December 2017 paper 'Longer Term Lending – Guidance for Credit Unions'.

5.1 Asset and Liability Management

Consideration needs to be given to the potential impact that changes to the current lending framework and resulting changes to the profile of credit union loan books in addition to any longer term investments may have on the structure of credit union balance sheets. Given the on-demand nature of credit union funding (i.e. savings from members), any proposal that has the potential to lengthen the maturity of assets needs to be considered in a broader asset and liability management context. Credit unions should be cognisant of their obligation under section 85A(2) of the 1997 Act to ensure that they at all times keep a proportion of their total assets in liquid form so as to enable the credit union to meet its obligations as they arise and that the proportion of assets kept in liquid form must take into account the nature, scale and complexity of the credit union and the composition and maturity of its assets and liabilities. Additionally consideration needs to be given to the profile of funding with appropriate monitoring and evaluation of asset and liability mismatches.

5.2 Credit Union Liquidity

The current structure of credit union balance sheets (low LTA ratios and investments predominantly held in short dated 'low risk' instruments) gives rise to high levels of liquidity. Credit unions are currently required to hold 20% of their unattached savings in relevant liquid assets with additional requirements for credit unions that increase lending over 5 years above 20% of total gross loans outstanding[8]. Average liquidity for the sector currently stands at 43.6% based on March 2018 Prudential Return data.

[8] Credit unions with lending over five years above 20 per cent of total gross loans outstanding must hold additional liquidity as set out below.

Lending Over Five Years	Minimum Liquidity Ratio
>20% and <25%	at least 25%
≥25% and <29%	over 25%
≥29%	at least 30%

5.3 Banking Sector Liquidity Measures

The Basel III framework introduced two liquidity monitoring measures for credit institutions in order to strengthen the resilience of the global financial market; the liquidity coverage ratio (LCR) and the net stable funding ratio (NSFR).

Liquidity Coverage Ratio

The LCR measure is set out in the Capital Requirements Regulation (EU) 575/2013 Article 412 and 460. This liquidity measure requires credit institutions to hold enough high quality liquid assets (HQLA) to cover net liquidity outflows under stressed conditions over a period of thirty days. HQLA are categorised over three levels; level 1, level 2A and level 2B, depending upon the availability of a liquid secondary market and overall credit quality of the particular asset class. Credit institutions have been required to have an LCR of 100% since 1 January 2018.

$$\frac{\textbf{Stock of High Quality Liquidity Assets}}{\textbf{Total Net Cash Outflows Over the Next 30 Days}} \geq 100\%$$

Net Stable Funding Ratio

The NSFR measure requires credit institutions to ensure that long-term obligations are adequately met with a diverse source of stable funding under normal and stressed conditions over a period of one year. Credit institutions have been required to have a NSFR of 100% since 1 January 2018.

$$\frac{\textbf{Available Stable Funding}}{\textbf{Required Stable Funding}} \geq 100\%$$

The Central Bank undertook high level analysis to consider LCR and NSFR in a credit union context. All credit unions would currently meet the LCR requirement reflecting the sector's low LTA ratio, profile of investments and the high proportion of funding drawn from retail deposits which are covered by a deposit guarantee scheme which are subject to lower outflow rates under the LCR. Similarly all credit unions would meet the NSFR requirement reflecting the sector's level and source of stable funding relative to the sector's LTA.

The Central Bank does not consider that these liquidity requirements are suitable in a credit union context given the relative complexity of these requirements and fundamental differences between credit unions and credit institutions including the comparative difference in LTA ratios and available sources of funding.

Taking account of the changes introduced to the definition of relevant liquid assets for credit unions from 1 March 2018, the capacity of credit unions to grow their LTAs, the permitted classes of investment for credit unions under the investment framework which supports the availability of high quality liquid assets and the scope for longer term lending being provided under our proposed changes for all credit unions, the existing liquidity framework is deemed appropriate for credit unions seeking to undertake commercial and house lending up to 7.5% of total assets.

Those credit unions who wish to undertake additional longer term lending and/or additional longer term investments will be required to have more advanced ALM frameworks, liquidity contingency plans and will be required to monitor and report on asset and liability mismatches regularly to the Central Bank. Credit unions will be required to demonstrate their understanding of ALM and provide an overview of their ALM frameworks in any application submitted to avail of an increased concentration limit for house and commercial lending.

The Central Bank notes that credit unions do not have access to alternative sources of liquidity such as a centralised liquidity mechanism which impacts on their ability to manage and access liquidity on an on-going basis. This impacts on the appropriate level of asset and liability mismatch for credit unions and has informed the calibration of the limits set out in this consultation.

The Central Bank is seeking views on the following:

16. Do you have any comments on liquidity and broader ALM considerations for credit unions wishing to increase the proportion of their loan books held in house and commercial loans particularly where those loans have longer maturities?

6. Other Considerations

Additional considerations for credit unions seeking to change the composition of their loan books and expand lending in specific loan categories which may be longer term in nature, including increased lending in house and commercial loans, are outlined below. The proposals contained in this consultation paper have been informed by the Central Bank's statutory mandate to regulate and supervise credit unions with a view to (i) the protection by each credit union of the funds of its members and (ii) the maintenance of the financial stability and well-being of credit unions generally. In addition the Central Bank considers it appropriate that the changes proposed to the lending framework would be accompanied by a number of changes to existing requirements and the introduction of some additional requirements for credit unions. Additionally, some existing requirements will become increasingly relevant for credit unions where they increase their exposure to longer term lending.

6.1 Risk Considerations

The Central Bank is supportive of credit unions prudently engaging in long term lending as part of a balanced loan portfolio. However, it is important that credit unions that wish to undertake such lending understand the specific risks including financial impacts, and how these risks fit within the credit union's lending strategy, risk appetite and capabilities. As outlined in section 4, credit unions wishing to undertake increased lending in house and commercial loans will be required to demonstrate to the Central Bank that they have strong core foundations of governance and risk management and an appreciation for the specific risks associated with these types of lending.

There is a need for credit unions to fully understand the risks associated with all lending and ensure that it is in line with the risk appetite of the credit union. Credit unions are required to develop, implement, document and maintain a risk management system with such governance arrangements and systems and controls to allow it identify, assess, measure, monitor, report and manage the risks which it is, or might reasonably be, exposed to. In addition, credit unions are required to implement systems and controls to manage and mitigate the risks identified by the risk management system.

The decision to proceed with investment in new services and/or expansion into new ventures requires critical assessment of the costs and benefits as they apply to the credit union and its individual situation in terms of member profile, common bond and operational and financial capabilities.

The role of outsourcing and shared services in supporting new product and business line development has been a feature of business model development in other jurisdictions and may warrant consideration.

Long Term Lending – Guidance for Credit Unions published in December 2017 provides an overview of some of the main risk factors associated with longer term lending. As highlighted in this guidance mortgages, as a distinct longer term lending product, present particular challenges and additional risk factors which need to be considered. The key risks identified in the paper are:

- Financial Risk – the risk that lower revenues or higher than anticipated costs result in longer term lending negatively impacting financial performance and position of the credit union. It is essential that revenue and cost models are comprehensive and realistic.

The financial risks attaching to house loans are quite considerable if scale is not achievable, which may be the case in credit unions with narrowly-based common bond limitations and an increasingly competitive market for the provision of house loans. The level of investment required to operate in a highly regulated market for high value, low margin business, amplifies the financial risks. Failure to consider the nature and scale of the constituent elements will expose credit unions to long-term adverse financial consequences.

- Credit Risk – longer term lending will have specific credit risks given its nature and characteristics. For example, mortgages are higher value loans and cumulatively can assume material volume – elevated risk exists as a result. For many credit unions, by virtue of their common bond, the matter of geographic or sectoral concentration should be considered and reflected in the risk policy.

- Funding & Liquidity Risk – risk associated with the on-demand nature of credit union funding. Credit unions sole funding source are members' shares and deposits, typically on-demand. Funding stability is the necessary counterpart to longer term lending, to ensure liquidity risks are being managed appropriately. It is expected credit unions will have completed an analysis of their membership profile to appropriately profile funding, identify any concentrations and understand the impact, for example, inter-generational change can have on the credit union's funding.

A phased approach to utilisation of additional capacity to undertake lending in specific loan categories can play an important role in mitigating some of these risks by ensuring that such lending is originated over the economic cycle. In recognition of this, it is our intention to require credit unions to use the additional capacity to issue house and commercial loans in a gradual/phased way. This would be set as a condition of any approval for an individual credit union to avail of increased concentration limits for house and commercial lending.

Other risks referred to in the paper include:

- Market Risk – the risk of loss arising from movements in interest rates.
- Governance & Management Risk – risk associated with poor strategy or oversight.
- Operational & Conduct Risk – risk of loss from inadequate or failed internal processes, people and systems.
- Regulatory and Compliance Risk – risk of regulatory sanctions, material financial loss or loss to reputation which may arise as a result of failure to comply with applicable laws, rules, regulations, standards and codes of conduct.

Where credit unions are considering increasing longer term lending and expanding or commencing mortgage lending, it is important that they identify the risk factors specific to this type of lending. Credit union boards should appreciate and incorporate these in their strategic planning, business execution, governance and management systems and policies and processes. As set out above the credit landscape has undergone fundamental change since the financial crisis and the re-scaling of the credit market combined with higher regulatory standards and increasing competitive pressures will present challenges to credit unions intending to grow their lending and provide new credit products.

6.2 Consumer Protection

The Consumer Protection Code 2012 (CPC), the Central Bank (Supervision and Enforcement) Act 2013 (Section 48(1)) Minimum Competency Regulations 2017 (MCR) and Minimum Competency Code 2017 (MCC) currently apply to credit unions authorised as insurance intermediaries with respect to their insurance intermediary business. The MCC/MCR also apply to credit unions when providing mortgages. They do not apply to other regulated activities carried out by credit unions, for example, their core lending and term deposit business. The Code of Conduct on Mortgage Arrears (CCMA) which outlines the framework that lenders must use when dealing with borrowers in mortgage arrears or pre-arrears does not apply to credit unions. The Central Bank has articulated its intention, following further consultation, to apply the MCC/MCR to credit unions for their core lending and term deposit business[9].

The European Union (Consumer Mortgage Credit Agreements) Regulations 2016, which transpose Directive 2014/17/EU on credit agreements for consumers relating to residential immovable property (the Mortgage Credit Directive) into Irish law, apply to credit unions who are involved in the provision of mortgages to their members. These Regulations include requirements relating to:

- financial education;
- information and practices preliminary to the conclusion of the credit agreement - including conduct of business obligations when providing credit to consumers;
- creditworthiness assessment; and
- sound execution of credit agreements and related rights.

The Central Bank is of the view that the changes being proposed in relation to the lending framework should be accompanied by enhanced consumer protections for all credit union members. It is the Central Bank's expectation that credit unions adopt a consumer focused culture when advancing credit and when dealing with borrowers in arrears and treat borrowers fairly and sympathetically, with the objective of assisting the borrower to meet their lending obligations. The Central Bank intends commencing a review of the CPC in 2019 and as part of that review intends consulting on the application of the CPC to the regulated activities of credit unions that are not currently in scope of the CPC.

6.3 Mortgage Measures

In 2015, the Central Bank introduced a series of mortgage measures as a permanent feature of the mortgage market. The purpose of the measures is to increase the resilience of borrowers and the financial system so that they can better withstand any future economic shocks. Credit unions are within scope of the Mortgage Measures and must ensure full compliance with the requirements of the mortgage measures where they are engaging in the provision of house loans. These measures are designed to stop house buyers from borrowing more than they can afford and prevent excess

[9] Minimum Competency Code 2017 and Minimum Competency Regulations 2017 Questions and Answers -outlines the Central Bank's intention to undertake further work (seeking information from the credit union sector about the level of qualifications already held by staff) to gain a better understanding of the impact of proposed changes on the sector while taking account of comments made in CP106 submissions to determine an appropriate implementation approach for the application of MCC to credit unions for their core loan and savings business.

credit from building up within the Irish financial system through the setting of limits on the size of mortgages that consumers can borrow through the use of LTV and LTI limits.

The Central Bank is of the view that LTV and LTI limits represent an important risk mitigant that can potentially protect both credit unions and their members where credit unions increase their exposure to house loans and that consideration should be given to appropriate LTV and LTI levels in a credit union context.

The mortgage measures are reviewed annually by the Central Bank and information on the measures, the reviews and changes to the measures are available on the Central Bank's website:

https://www.centralbank.ie/financial-system/financial-stability/macro-prudential-policy/mortgage-measures

Pursuant to Section 22 of the Central Bank (Supervision and Enforcement) Act 2013, credit unions with total mortgages advanced in excess of €50m in a reporting period are required to make a detailed return to the Central Bank. Additionally, the Central Bank intends to place a new reporting requirement on credit unions who engage in house loans on a bi-annual basis, whereby they will be required to provide data on all house loans issued, which will enable the Central Bank to assess the credit unions' compliance with the Mortgage Measures.

6.4 Section 35 Regulatory Requirements for Credit Unions (October 2013)

The Section 35 Regulatory Requirements for Credit Unions issued in October 2013 currently set out requirements for credit unions relating to:

- Liquidity;
- Lending Practices for Rescheduled Loans;
- Provisioning for Rescheduled Loans; and
- Systems, Controls and Reporting.

Given the application of Accounting Standard FRS102 to credit unions in 2016 and publication of Provisioning Guidelines for Credit Unions in April 2018, it is now appropriate to rescind the provisioning requirements for rescheduled loans set out in the Section 35 Regulatory Requirements for Credit Unions. It is also proposed to move the liquidity requirements set out in the Section 35 Regulatory Requirements for Credit Unions into Part 3 of the 2016 Regulations for clarity and ease of access. Finally, it is proposed that requirements for lending practices for rescheduled loans and systems, controls and reporting will be reflected in the Lending Chapter of the Credit Union Handbook.

6.5 Supervision/Reporting

Our reporting framework and supervisory approach will reflect any changes made to the lending framework. The Central Bank intends to amend the Prudential Return to gather information on loan book maturities by specific loan category and additional information on large exposures to support our analysis of credit union lending. Both the application process for additional lending scope and our supervision of larger credit unions will include analysis of the sustainability of business models, funding risks, governance and risk appetite, capital and credit underwriting.

7. Regulatory Impact Analysis

In accordance with the Consultation Protocol for Credit Unions, issued on 27 November 2012, the Central Bank has conducted a RIA to assess the impact of the potential changes to the lending regulations set out in this consultation paper.

The full RIA is set out in Appendix D. Credit unions and other sector stakeholders may also wish to provide additional information or analysis they may have on the likely impact of the potential changes to the lending regulations.

8. Next steps

The table below sets out proposed next steps and indicative timelines for the introduction of potential changes to the lending regulations for credit unions set out in this consultation paper.

Date	Step
24 October 2018	Consultation Paper published
09 January 2019	Consultation period closes
Q2 2019	Undertake statutory consultation as required under S84A of the Credit Union Act, 1997
Q2 2019	Publish Feedback Statement and Draft Regulations
Q2/Q3 2019	Commencement of Final Regulations

9. Summary of areas where Central Bank is seeking views

The Central Bank is seeking views on the following:

Removal of 5 and 10 Year Lending Maturity Limits:

1. Do you have any comments on the proposal to remove the 5 year and 10 year lending maturity limits contained in Regulation 14 of the 2016 Regulations (taking account of the other changes to the lending framework)?

Maximum Loan Maturity Limit for Unsecured Loans:

2. Do you have any comments on the proposal to introduce a maximum maturity limit of 10 years for unsecured loans?
3. Do you have any comments on the proposed definition of a secured loan?

Concentration Limits for House and Commercial Loans:

4. Do you have any comments on the proposal to require that all commercial loan exposures utilise the concentration limit for commercial lending?
5. Do you have any comments on the Central Bank's intention to introduce board reporting requirements for house loans?
6. Do you have any comments on the proposal to introduce a base combined concentration limit for house and commercial loans of 7.5% of Total Assets?
7. Do you have any comments on the proposal to limit the maximum amount of house or commercial lending which a credit union may undertake to 5% of Total Assets within the base combined concentration limit?
8. Do you have any comments on the proposal to permit an increased combined concentration limit for house and commercial loans for those credit unions who can demonstrate the necessary financial strength, skills, expertise, operations and risk management capability to undertake increased lending in these loan categories?
9. What skills, expertise, operational and risk management capabilities do you consider necessary to support increased lending in house and commercial loans?
10. Do you have any comments on the proposed increased combined concentration limit for house and commercial lending of 15% of Total Assets?
11. Do you have any comments on the application process referred to above?

Definition of Commercial Loans:

12. Do you agree with the proposal to re-name the commercial loan lending category to small business loan?
13. Do you have any comments on the proposed definition for a small business loan?

Large Exposures:

14. Do you agree with a large exposure being prescribed as an exposure to a borrower or group of borrowers who are connected of 2.5% or greater of the regulatory reserves of the credit union?

Transitional Arrangements

15. Do you have any comments on the proposed transitional arrangements?

Liquidity and ALM Considerations

16. Do you have any comments on liquidity and broader ALM considerations for credit unions wishing to increase the proportion of their loan books held in house and commercial loans particularly where those loans have longer maturities?

10. Making Submissions

Please make your submissions in writing, if possible electronically as a word document or a .pdf document by email, on or before 09 January 2019.

When addressing the questions raised in this Consultation Paper, please use the relevant section heading to identify the section you are referring to and clearly set out the basis for your views.

The Central Bank intends to make all submissions available on the Central Bank website. Information deemed to be potentially libellous or defamatory will not be published. The Central Bank will accept no liability in respect of any information provided which is subsequently released, or in respect of any consequential damage suffered as a result. Submissions should be marked "Consultation on Potential Changes to the Lending Framework for Credit Unions (CP125)" and sent by email to rcuconsultation@centralbank.ie.

In the event that you are unable to send your response electronically, please forward it by post before 09 January 2019 to:

Registry of Credit Unions
Central Bank of Ireland
PO Box 559
New Wapping Street
North Wall Quay
Dublin 1

Appendix A: Existing Lending Regulations

CREDIT UNION ACT 1997 (REGULATORY REQUIREMENTS) REGULATIONS 2016

(S.I. No. 1 of 2016)

(This Chapter has not reproduced the entirety of Part 1 – please consult the Credit Union Act 1997 (Regulatory Requirements) Regulations 2016 for the full provision.)

PART 1

PRELIMINARY AND GENERAL

Interpretation

In these Regulations, unless the context otherwise required:-

"the Bank" means the Central Bank of Ireland;

"commercial loan" means a loan, the primary objective of which is to fund an activity whose purpose is to make a profit;

"community loan" means a loan to a community or voluntary organisation which is established for the express purpose of furthering the social, economic or environmental well-being of individuals within the common bond of the credit union in any of the following areas -

(a) sport and recreation;

(b) culture and heritage;

(c) the arts (within the meaning of the Arts Act 2003);

(d) health of the community;

(e) youth, welfare and amenities; and

(f) natural environment;

"final repayment date" means the date on which the loan is due to expire, as indicated on the relevant credit agreement in accordance with section 37C(1)(j) of the Act or any subsequent date agreed between the credit union and the member to whom the loan has been made;

"house" means any building or part of a building used or suitable for use as a dwelling and any outhouse, yard, garden or other land appurtenant thereto or usually enjoyed therewith;

"house loan" means a loan made to a member secured by property for the purpose of enabling the member to:

(a) have a house constructed on the property as their principal residence;

(b) improve or renovate a house on the property that is already used as their principal residence,

(c) buy a house that is already constructed on the property for use as their principal residence, or

(d) refinance a loan previously provided for one of the purposes specified in (a), (b) or (c) for the same purpose;

"member of the family" means in relation to any person, that person's father, mother, spouse or civil partner, cohabitant, son, daughter, brother, or sister;

"personal loan" means a loan to a natural person, once the loan is for purposes unrelated to the person's trade, business, profession or the purchase of property;

"related company" means companies related within the meaning of section 2(1) of the Companies Act 2014;

"related party" means -

(a) a member of the board of directors or the management team of a credit union;

(b) a member of the family of a member of the board of directors or the management team of a credit union; or

(c) a business in which a member of the board of directors or the management team of a credit union has a significant shareholding;

"significant shareholding" means 10 per cent or more of the shares or voting rights in the business;

"the Act" means the Credit Union Act, 1997;

"unattached savings" means those total savings which are not attached to loans or otherwise pledged as security and are withdrawable by members.

PART 4

LENDING

Categories of Lending

11. (1) A credit union shall only make loans that fall within the following categories:

(a) Personal loans;

(b) Commercial loans;

(c) Community loans;

(d) House loans;

(e) Loans to other credit unions.

(2) A commercial loan granted by a credit union, where the total amount of commercial loans granted to a borrower, or group of borrowers who are connected, is less than €25,000, is not subject to Regulations 12(a) or 16. For the purposes of paragraph (2), a commercial loan is included in the calculation of commercial loans until the commercial loan has been repaid in full.

Concentration Limits

12. A credit union shall not make:

(a) a commercial loan, where such a loan would cause the total amount of outstanding commercial loans of the credit union to exceed 50 per cent of the credit union's regulatory reserve,

(b) a community loan, where such a loan would cause the total amount of outstanding community loans to exceed 25 per cent of the credit union's regulatory reserve, or

(c) a loan to another credit union, where such a loan would cause the total amount of outstanding loans to other credit unions to exceed 12.5 per cent of the credit union's regulatory reserve.

Large Exposure Limit

13. (1) A credit union shall not make a loan to a borrower or a group of borrowers who are connected which would cause the credit union to have a total exposure to the borrower or group of borrowers who are connected of greater than €39,000 or 10 per cent of the regulatory reserve of the credit union.

(2) Where an exposure to a borrower or group of borrowers who are connected exceeds the limit set out in paragraph (1), the credit union must hold the amount of the exposure that is in excess of the limit in a realised reserve, separate from the regulatory reserve of the credit union.

(3) The requirement specified in paragraph (2) shall not apply, to exposures existing at the time of commencement of these Regulations, for a period of 2 years from the commencement of these Regulations.

Maturity Limits

14. (1) A credit union shall not make a loan to a member:–

(a) for a period exceeding 5 years if, were the loan to be made, the total gross amount outstanding in relation to all loans with more than 5 years to the final repayment date would exceed –

(i) 30 per cent of the total gross loan book balance outstanding at that time in relation to all loans made by the credit union, or

(ii) if the Bank so approves in writing, 40 per cent of the total gross loan book balance outstanding at that time in relation to all loans made by the credit union, or

(b) for a period exceeding 10 years if, were the loan to be made, the total gross amount outstanding in relation to all loans with more than 10 years to the final repayment date would exceed –

(i) 10 per cent of the total gross loan book balance outstanding at that time in relation to all loans made by the credit union, or

(ii) if the Bank so approves in writing, 15 per cent of the total gross loan book balance outstanding at that time in relation to all loans made by the credit union.

(2) The Bank may impose on approval, for the purposes of subparagraph (a)(ii) or (b)(ii) of this Regulation, any condition that the Bank considers appropriate.

(3) A credit union shall not make a loan to a member for a period exceeding 25 years.

Requirement for House Loans

15. A credit union shall only grant a house loan where it holds the first legal charge on the property in respect of which the loan is to be provided.

Lending Practices for Specific categories of Lending

16. (1) A credit union shall only grant a commercial loan, community loan or loan to another credit union where a comprehensive business plan and detailed financial projections (supported by evidence based assumptions), appropriate for the scale and complexity of the loan, are provided and in place before granting the relevant loan.

(2) A credit union shall report on the performance of loans, in writing, to the board of directors of the credit union on a monthly basis. For the purposes of paragraph (2), such a report shall include details on the performance of commercial loans, community loans and loans to other credit unions.

General Lending Practices

17. (1) A credit union shall permit a member to repay a loan on any day that the credit union is open for business (including opening hours of branch or otherwise available for business).

(2) A credit union shall establish and maintain the matters specified below in writing:

(a) limits in respect of credit concentration and loan portfolio diversification including the maximum amount of commercial lending, community lending and lending to other credit unions; and

(b) processes which the credit union will follow in relation to arrears management and rescheduling.

(3) A credit union shall ensure that its credit assessment process is based on coherent and clearly defined criteria and that the process of approving loans and amending loans is clearly established and documented in its credit policy.

Related Parties-General

18. (1) A credit union shall not make a loan to a related party which would provide that party with more favourable terms than a loan by the credit union to non-related parties (including, without limitation, terms as to credit assessment, duration, interest rates, amortisation schedules, collateral requirements).

(2) A credit union shall not manage a loan to a related party on more favourable terms than a loan by the credit union to non-related parties (including but not limited to varying the terms of a loan, permitting rescheduling, interest roll-up, granting a grace period for payment, loan write-off in whole or in part, provisioning against a loan, decisions to take or not to take enforcement action).

Related Parties-Specific

19. (1) Subject to Regulation 18, a credit union shall ensure that the making of a loan to a related party is subject to individual prior approval in writing by the credit committee and that actions in relation to the management of a loan are subject to individual prior approval in writing by the credit committee or the credit control committee of the credit union as appropriate.

(2) A credit union shall exclude individuals on the credit committee or the credit control committee with conflicts of interest in relation to matters specified in paragraph (1).

Related Parties-Exempt Exposures

20. (1) Regulations 19 and 21 do not apply where the total credit union exposure to the related party is not greater than €2,000.

(2) In relation to exempt exposures referred to in paragraph (1), a credit union shall ensure that:-

(a) the credit union monitors these loans to ensure that the limit imposed is not exceeded;

(b) a register of these loans recording how it has complied with this requirement is maintained by the credit union; and

(c) a report on these loans is reviewed and approved by the board of directors of the credit union on a quarterly basis.

Related Parties- Recording and Monitoring Requirements

21. (1) A credit union shall record and monitor loans made to related parties and report, in writing, to the board of directors on related party loans on a monthly basis. Such a report shall include details of loans advanced to related parties during the month, total loans outstanding to related parties, the performance of loans to related parties and actions in respect of the management of loans to related parties.

(2) A credit union shall ensure that the internal audit function assesses, at least annually, the compliance or otherwise by a credit union with Regulation 19 and paragraph (1) of this Regulation and, after each assessment, submit a written report to the board of directors indicating their findings and conclusions and, where appropriate, making recommendations on any changes required.

Related Parties- Credit Policy

22. A credit union shall include the process in relation to lending to a related party in its Credit Policy.

Lending Policies

23. A credit union shall, at a minimum, establish and maintain the following written lending policies:-

(a) Credit Policy;

(b) Credit Control Policy; and

(c) Provisioning Policy.

Transitional Arrangements

24. (1) Nothing in these Regulations shall render unlawful any loan made in accordance with or under the Act to a member before the commencement of these Regulations.

(2) Where, at the commencement of these Regulations, a credit union is failing to comply with the requirements in this Part, that credit union shall only make a loan where the making of such a loan would not cause the credit union to either fail to comply or exacerbate a failure to comply with any of the requirements in this Part.

Appendix B: Comparison Table of Current Framework versus Proposals

Lending Area	Existing Lending Framework	Proposals for Amendment to Existing Lending Framework
Categories of Lending	Framework permits: i. Personal Loans ii. Commercial Loans iii. Community Loans iv. House Loans v. Loans to Other Credit Unions	i. Amendment to the naming and definition of commercial loans. ii. Clarification that buy to let residential and buy to let commercial lending is prohibited.
Maturity Limits for Lending	i. Maximum loan term 25 years ii. No more than 30% of gross loans outstanding can have a maturity of > 5 years; and No more than 10% of gross loans outstanding can have a maturity of > 10 years. With additional approval: iii. No more than 40% of gross loans outstanding can have a maturity of > 5 years; and No more than 15% of gross loans outstanding can have a maturity of > 10 years.	i. Removal of the lending maturity limits (the 30%/40% and 10%/15% limits). ii. Introduction of a maximum loan term for unsecured loans of 10 years. iii. Introduction of a definition for secured loans.
Concentration Limits for Lending	i. Total commercial loans cannot represent more than 50% of the regulatory reserves of the credit union. ii. Total community loans cannot represent more than 25% of the regulatory reserves of the credit union. iii. Total loans to another credit union cannot represent more than 12.5% of the regulatory reserves of the credit union.	i. Introduction of a combined concentration limit for commercial and house loans which limits the total amount of commercial and house loans which a credit union can have to 7.5% of total assets. Within this, no more than 5% of the total assets of the credit union may be exposed to a particular loan category i.e. no more than 5% of total assets may be held in house or commercial loans. The proposed concentration limit of 7.5% of Total Assets may be increased to 15% of Total Assets where approval is granted by the Central Bank.

		All commercial loans granted, regardless of size will utilise the concentration limit for commercial lending.
Large Exposures	Maximum exposure to a borrower or group of borrowers who are connected is limited to the greater of €39,000 or 10% of regulatory reserves of the credit union.	i. Prescribe a large exposure amount as any exposure to a borrower or group of borrowers who are connected representing at least 2.5% of the regulatory reserves of the credit union. Enhanced reporting of large exposures to be introduced following commencement of amending regulations.
Lending practices for specific categories of loan	i. A credit union shall only grant a loan for commercial, community or loan to another credit union where a comprehensive business plan and detailed financial projections are provided. ii. A credit union shall report on the performance of commercial, community and loans to other credit unions to the board on a monthly basis.	Board reporting requirement to be introduced on the performance of house loans.

Appendix C: Longer Term Lending Questionnaire

1. Please complete the table below with details of gross loans outstanding currently classified as 'personal loans' (as defined in the Credit Union Act 1997 (Regulatory Requirements) Regulations 2016 (as amended) (the 2016 Regulations)) as at 31 March 2018.

Specific sub categories of loans which typically fall within the 'personal loans' category are specified.

			Gross Loans Outstanding € by Remaining Maturity as at 31 March 2018							
Personal Loan Category	Number of Loans	Gross Loans Outstanding €	≤ 1 Year	> 1 and ≤ 3 Years	> 3 and ≤ 5 Years	> 5 and ≤ 7 Years	> 7 and ≤ 10 Years	> 10 and ≤ 15 Years	> 15 Years	Typical Interest Rate on Loan Category
Car loans										
Home improvement loans										
Education loans										
Other personal loans										
Total	-	-	-	-	-	-	-	-	-	
Total Gross Loans Outstanding by:										
Unsecured loans and loans secured by shares										
Secured loans other than by way of shares										

2. Please complete the table below with details of gross loans advanced which were classified as 'personal loans' (as defined in the 2016 Regulations) from 1 October 2016 to 30 September 2017.

Specific sub categories of loans which typically fall within the 'personal loans' category are specified.

			Gross Loans Advanced € by Maturity at date of loan issue (from 1 October 2016 to 30 September 2017)							
Personal Loan Category	Number of Loans	Gross Loans Advanced €	≤ 1 Year	> 1 and ≤ 3 Years	> 3 and ≤ 5 Years	> 5 and ≤ 7 Years	> 7 and ≤ 10 Years	> 10 and ≤ 15 Years	> 15 Years	Typical Interest Rate on Loan Category
Car loans										
Home improvement loans										
Education loans										
Other personal loans										
Total	-	-	-	-	-	-	-	-	-	
Total Gross Loans Advanced by:										
Unsecured loans and loans secured by shares										
Secured loans other than by way of shares										

3. Does the credit union currently engage in 'house loans' (as defined in the 2016 Regulations)? If yes, please populate the table below with details on 'house loans' (as defined in the 2016 Regulations).

			Gross Loans € By Maturity Category					
	Number of Loans	Gross Loans €	≤ 5 Years	> 5 and ≤ 7 Years	> 7 and ≤ 10 Years	> 10 and ≤ 15 Years	> 15 Years	Typical Interest Rate
Gross House Loans Outstanding as at 31 March 2018								
Gross House Loans Advanced from 1 October 2016 to 30 September 2017								
House Loans committed to issue for **next 12 months from 1 April 2018**								

4. Does the credit union currently engage in 'commercial loans' (as defined in the 2016 Regulations)? If yes, please populate the table below with details on 'commercial loans' (as defined in the 2016 Regulations).

			Gross Loans € By Maturity Category					
	Number of Loans	Gross Loans €	≤ 5 Years	> 5 and ≤ 7 Years	> 7 and ≤ 10 Years	> 10 and ≤ 15 Years	> 15 Years	Typical Interest Rate
Gross Commercial Loans Outstanding as at 31 March 2018								
(i) Unsecured loans and loans secured by shares								
(ii) Secured loans other than by way of shares								
Gross Commercial Loans Advanced from 1 October 2016 to 30 September 2017								
(i) Unsecured loans and loans secured by shares								
(ii) Secured loans other than by way of shares								
Commercial Loans committed to issue for **next 12 months from 1 April 2018**								
(i) Unsecured loans and loans secured by shares								
(ii) Secured loans other than by way of shares								

5. Please populate the table below with details of total savings held by members in the credit union and gross loans outstanding with members of the credit union, by age profile of the member as at 31 March 2018.

Age of Member:	Number of Savings Accounts	Total Savings €	Number of Loan Accounts	Gross Loans Outstanding €
< 30 years				
≥ 30 <45 years				
≥ 45 <55 years				
≥ 55 <65 years				
> 65 years				
Other accounts				
Total	-	-	-	-

6. Do you consider that the lending limits contained in the 2016 Regulations are sufficient for the credit union and will enable the credit union to meet loan demand over the next 5 years? If yes, please proceed to question 11. If no please complete questions 7 to 11.

7. Based on analysis of likely loan demand from members within your common bond and taking account of the credit union's past lending activity, what is the credit union's total gross loans outstanding and total assets forecast to be for each of the dates listed on the table below? Please specify how the Gross Loan Balance amount is forecast to be allocated in each of the maturity categories.

These forecasted figures should ignore any lending limits which currently exist in the lending framework for credit unions (i.e. no more than 30% of gross loans can have a maturity of > 5 years and no more than 10% of gross loans can have a maturity of > 10 years/and the related limits where LTL approval has been granted)

					Gross Loans Outstanding € by Maturity Category		
Time Period	Gross Loans Outstanding €	Imputed Loan Growth Rate	Total Assets	Loan to Asset Ratio	≤ 5 Years	> 5 and ≤ 10 Years	> 10 Years
30 September 2016							
30 September 2017		0.00%					
31 March 2018	-	0.00%			-	-	-
30 September 2018		0.00%					
30 September 2019		0.00%					
30 September 2020		0.00%					
30 September 2021		0.00%					
30 September 2022		0.00%					

8. Following on from question 7, based on the Gross Loans Outstanding € forecast for 30 September 2022 please provide a breakdown of the forecasted split of loans in each of the following categories (taking account of Asset and Liability Management/the funding profile of the credit union). The corresponding data as at 31 Mar 2018 is provided based on the data reported in Q1, Q3 and Q4.

Loan Category	Gross Loans Outstanding € 31 March 2018	Typical Interest Rate 2018	Gross Loans Outstanding € 30 September 2022	Typical Interest Rate 2022
Car Loans	-	0.00%		
Home Improvement Loans	-	0.00%		
Education Loans	-	0.00%		
Other Personal Loans	-	0.00%		
Commercial Loans	-	0.00%		
House Loans	-	0.00%		
Total	-		-	

9. Based on the forecast provided in Q7 and Q8 for gross loans at 30 September 2022, please populate the table below with the projected split of gross loans in each of the loan categories specified and the maturity buckets specified.

	Personal Loans €	Housing Loans €	Commercial Loans €	Total €
Loans ≤ 1 Year Maturity (including MPCAS overdrafts and Budget accounts) as a % of total assets				0
Loans > 1 Year and ≤ 5 Years to Maturity				0
Loans > 5 Year and ≤ 10 Years to Maturity				0
Loans > 10 Years to Maturity				0
Total	-	-	-	0

10. Taking account of the analysis undertaken to forecast the loan activity of the credit union in questions 7 and 8, please populate the table below with details of the forecasted funding profile of the credit union for each of the time periods requested.

		Total Savings € Split By:		Total Term Deposits € Split by Maturity Term:			
Time Period	Total Savings €	On Demand	Term Deposits	≤ 3 Years	> 3 and ≤ 5 Years	> 5 and ≤ 10 Years	> 10 Years
30 September 2016							
30 September 2017							
31 March 2018	-						
30 September 2018							
30 September 2019							
30 September 2020							
30 September 2021							
30 September 2022							

11. Having considered internally and discussed with the board of the credit union, please provide any additional commentary which you have in relation to longer term lending in the credit union.

Appendix D: Regulatory Impact Analysis

Banc Ceannais na hÉireann
Central Bank of Ireland

Eurosystem

Regulatory Impact Analysis on Potential Changes to the Lending Framework for Credit Unions

October 2018

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1. Introduction

Section 35 of the Credit Union Act, 1997 (the 1997 Act) provides regulation making powers to the Central Bank in relation to lending. The Credit Union Act 1997 (Regulatory Requirements) Regulations 2016 (as amended) (the 2016 Regulations) commenced on 1 January 2016 with Part 4 of these regulations setting out permitted categories of lending for credit unions, the concentration limits for specific lending categories and related lending maturity limits. The 2016 Regulations also contain a large exposures limit and outline lending practices for certain categories of loan.

To ensure that the lending regulations for credit unions remain appropriate the Central Bank undertook to carry out a review of the lending framework in 2018. As part of this process, the Central Bank is carrying out a consultation on potential changes to the lending framework **'Consultation on Potential Changes to the Lending Framework for Credit Unions- Consultation Paper 125'** (CP125). These proposed changes have been informed by the Central Bank's statutory mandate in relation to credit unions as set out in section 84 of the 1997 Act which requires that the Central Bank shall administer the system of regulation and supervision of credit unions with a view to (i) the protection by each credit union of the funds of its members, and (ii) the maintenance of the financial stability and well-being of credit unions generally.

The 'Consultation Protocol for Credit Unions', issued on 27 November 2012, states that a Regulatory Impact Analysis (RIA), which will contain an examination of the impacts of the new regulations and consideration of alternative options, will be carried out by the Central Bank, where practicable, when consulting on new regulations.

As part of the review of the lending framework for credit unions, the Central Bank undertook a RIA, set out below, to examine the impact of potential changes to the lending framework for credit unions.

The RIA is structured as follows:

- Section 2 sets out the policy context and objectives and provides an overview of the credit union sector based on sector Prudential Returns and data gathered via a questionnaire which was issued on 11 April 2018 to credit unions on lending and savings;
- Section 3 outlines potential changes to the lending framework for credit unions;
- Section 4 analyses the costs, benefits and impacts of the potential changes to the lending framework;
- Section 5 provides detail on the consultation paper related to this RIA;
- Section 6 specifies the responsibilities for enforcing and ensuring compliance with the lending regulations for credit unions;
- Section 7 provides detail on a review of the lending framework which the Central Bank will perform to assess the actual impact which the potential changes have had, should they be introduced; and
- Section 8 provides detail on the publication of the RIA and related consultation paper.

2. Policy Context and Objective

There are currently 253[1] actively trading credit unions with total membership reported to be in the region of 3.3 million. Based on 31 March 2018 Prudential Return data total assets in the sector are €17.2bn comprising total loans of €4.5bn and total investments of €12bn. Total sector savings are €14.3bn and total realised reserves are €2.8bn.

The current profile of sector lending is set out below. This is based on analysis undertaken on Prudential Returns submitted by credit unions for 31 March 2018. It also reflects analysis of responses received to the questionnaire on lending which was issued to credit unions in April 2018, further detail on which is contained in the consultation paper to which this RIA is appended. Where current lending trends data is presented as extracted from questionnaire responses, this analysis comprises data gathered from 172 credit unions which reflects over 80% coverage in terms of overall sector lending. Therefore it is considered to be a representative sample of the sector for analysis purposes.

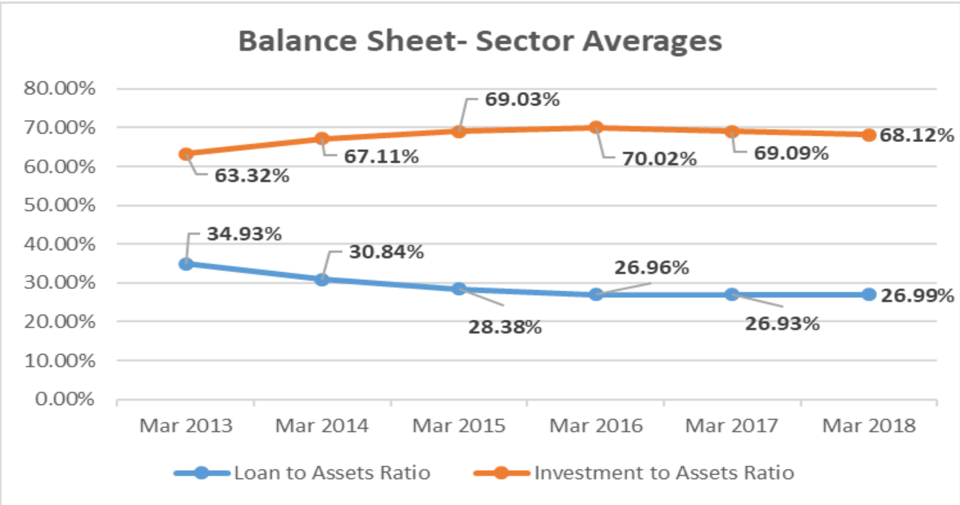
Data is also presented on the forecasted profile of sector lending which is based on analysis of questionnaire responses from the 63 questionnaire respondents who indicated that the current maturity limits contained in the lending framework are not sufficient to meet forecasted loan demand out to 30 September 2022.

2.1 Profile of Current Sector Lending

2.1.1 Sector Lending Activity

Total assets have increased by c.25% since March 2013 however the average sector loan to asset (LTA) ratio has declined steadily from close to 35% in March 2013 to 27% at March 2018. At the same time investments have been increasing year on year with the average sector investment to asset ratio now standing at close to 70%.

Chart 1 | Evolution of Loans to Assets Ratio and Investments to Assets Ratio for Sector (2013 to 2018)



Source: Credit Union Prudential Returns

[1] As at 22 October 2018.

2.1.2 Loan Category Profile

Data analysis indicates that the majority of credit union lending is within the personal loan category. Of the €4.5bn total loans outstanding at 31 March 2018, €4.3bn are categorised as personal loans. Table 1 illustrates the breakdown of sector lending across the various loan categories permitted in the 2016 Regulations.

Table 1 | Breakdown of Sector Lending

Loan Category	€
Personal Loans	4.3bn
Commercial Loans	0.1bn
Community Loans	0.0bn
House Loans	0.2bn
Loans to Other Credit Unions	0.0bn
Other	0.0bn
Total	**€4.5bn**

Source: 31 March 2018 Prudential Return

Responses received to the questionnaire provided a breakdown on the composition of lending within the personal loan category. Table 2 illustrates the average % of overall personal lending in each of the personal lending sub-categories specified for questionnaire respondents. The split of personal loans outstanding across each of the personal loan sub-categories was similar across credit unions of all asset sizes indicating that the majority of credit union personal lending relates to car loans or home improvement loans.

Table 2 | Average Percentage of Overall Personal Lending by Loan Category

Personal Lending Sub-Category	% of Overall Personal Lending
Car Loans	29.9%
Home Improvement Loans	28.4%
Education Loans	3.5%
Other Personal Loans	38.2%
Total	**100%**

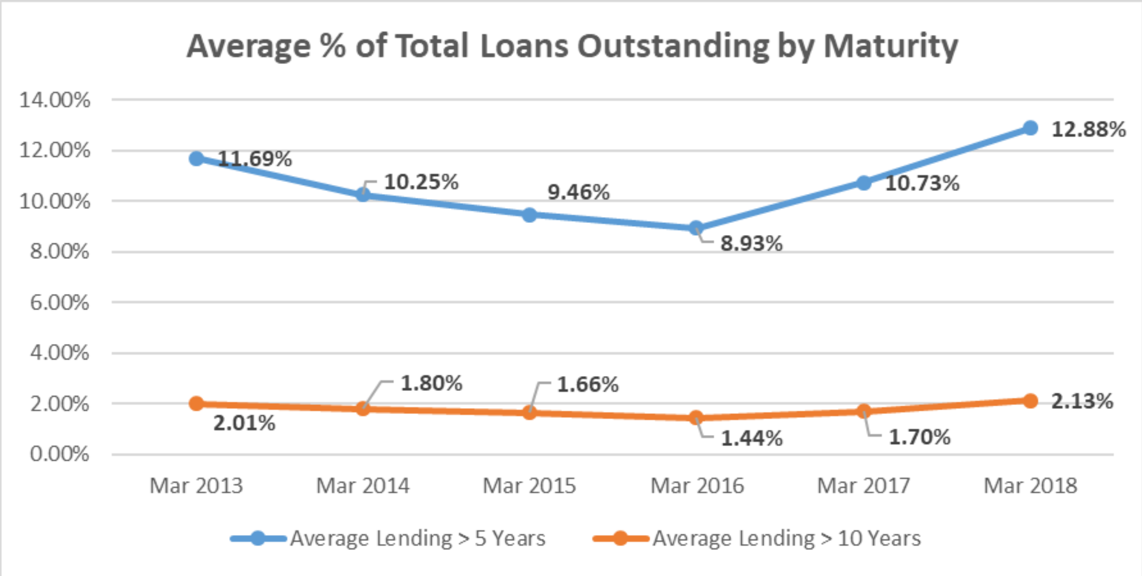
Source: Credit Union Longer Term Lending Questionnaire

2.1.3 Loan Maturity Profile

The 2016 Regulations contain lending maturity limits which place a restriction on the total amount of an individual credit union's gross loans which may be outstanding for periods of greater than 5 and greater than 10 years. The regulations specify that no more than 30% of gross loans may be outstanding for more than 5 years and that no more than 10% of gross loans may be outstanding for more than 10 years. These percentage limits may be increased to 40% and 15% respectively for lending greater than 5 and 10 years, where additional approval is granted by the Central Bank.

Chart 2 provides detail on the utilisation of the current lending maturity limits for the period March 2013 to March 2018. The years 2014 to 2016 saw a decline in the average percentage of sector loans outstanding for greater than 5 and 10 years, however since 2017 the average loan maturity has increased and surpassed levels reached in 2013. The average percentage of gross loans outstanding greater than 5 and 10 years is 12.9% and 2.1% respectively.

Chart 2 | Evolution of Sector Average Lending > 5 Years and > 10 Years (2013 to 2018)



Source: 31 March 2018 Prudential Return

Table 3 provides a breakdown of the average % of total gross loans outstanding for periods greater than 5 and 10 years, split by credit unions of varying asset size. This data indicates that it is the larger credit unions (i.e. credit unions with assets of at least €100m), who have the highest proportion of their total gross loans outstanding for longer maturities.

Table 3 | Profile of > 5 Year and > 10 Year Lending by Credit Union Size

Credit Union Asset Category	Average % of Gross Loans Outstanding > 5 Years	Average % of Gross Loans Outstanding > 10 Years
Credit Unions Total Assets ≥€100 million	17.3%	4.4%
Credit Unions Total Assets ≥€40 million and < €100 million	13.7%	1.8%
Credit Unions Total Assets <€40 million	10.5%	1.4%

Source: 31 March 2018 Prudential Return

Data gathered through the responses to the questionnaire provide an insight into the loan maturities of specific loan categories, data which has not previously been collected from credit unions. The high level results of the analysis of this data is presented in Table 4 and provides detail on the average % of total gross loans outstanding per loan category and maturity bucket.

Table 4 | Maturity Profile by Loan Category

Loan Category	Maturity ≤ 5 Years	Maturity >5 and ≤7 Years	Maturity >7 and ≤10 Years	Maturity >10 and ≤15 Years	Maturity > 15 Years
Personal Loans	88.3%	5.2%	5.5%	0.8%	0.2%
Commercial Loans	60.8%	13.5%	18.9%	5.3%	1.5%
House Loans	10.9%	8.9%	26.8%	25.2%	28.2%

Source: Credit Union Longer Term Lending Questionnaire

Table 4 indicates that, based on the responses received to the lending questionnaire, the majority of credit union personal and commercial lending has a maturity of less than 10 years with only 1.0% and 6.8% of personal and commercial loans respectively having an outstanding maturity of greater than 10 years. House loan lending has a more diverse split in terms of maturity profile, with questionnaire analysis indicating that 47% of house loans reported have a maturity of less than 10 years, and 53% have a maturity of greater than 10 years.

2.1.4 Loan Size Profile

Based on 31 March 2018 Prudential Return data, the average loan size across the sector was €6.6k. Table 5 illustrates the average loan size for credit unions of different asset sizes.

Table 5 | Average Loan size for Credit Unions of varying Asset Size

Credit Union Asset Category	Average Loan Size
Credit Unions Total Assets ≥€100 million	€7,318
Credit Unions Total Assets ≥€40 million and < €100 million	€6,613
Credit Unions Total Assets <€40 million	€6,216
Average Sector	**€6,559**

Source: 31 March 2018 Prudential Return

Table 6 illustrates the average loan size for each category of lending across the sector[2].

[2] The average loan size was calculated in each credit union by loan category. The average of these loan sizes was then calculated to present the sector average loan size for each of the specified loan categories.

Table 6 | Average Loan size by Loan Category

Loan Category	Average Loan Size
Personal Loans	€6,347
Commercial Loans	€21,123
Community Loans	€30,428
House Loans	€55,471
Loans to Other Credit Unions	€0
Other	€15,078

Source: 31 March 2018 Prudential Return

2.1.5 Security Profile

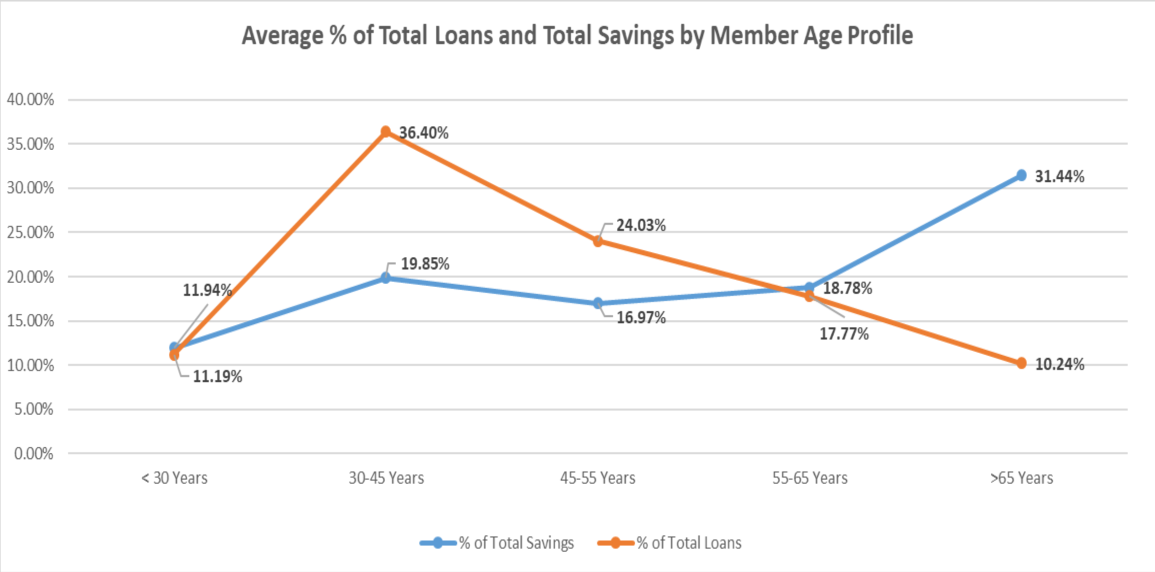
The requirements for house loans contained in the 2016 Regulations specify that a “house loan” may only be granted where the credit union holds the first legal charge on the property in respect of which the loan is to be provided. Common practice for other credit union lending is for loans to be secured by way of attached shares. Based on 31 March 2018 Prudential Return data there are €1.63bn shares attached against overall sector loans.

Data gathered on the questionnaire sought to determine if other categories of lending, namely personal lending and commercial lending, are secured other than by way of shares. Questionnaire respondents provided detail on the split of loans in each of the maturity categories by loans secured other than by way of shares and unsecured loans. Data analysis indicates that a very small proportion of credit union lending for personal loans is secured other than by way of shares with on average c.0.5% of total personal loans being secured other than by way of shares. The average level of commercial lending which is secured, other than by way of shares, based on data provided by respondents to the questionnaire is c.17.5%.

2.1.6 Age Profile of Credit Union Borrowers

The average proportion of loans and savings held by credit union borrowers and savers, split by age profile of the borrower or saver, is outlined in Chart 3. As can be seen c.72% of credit union loans are outstanding with borrowers aged 55 and under, with c.50% of savings held by members aged over 55. This trend is broadly consistent across all credit unions regardless of their asset size.

Chart 3 | Member Age Profile- % of Total Loans and % of Total Savings



Source: Credit Union Longer Term Lending Questionnaire

2.2 Profile of Forecasted Sector Lending

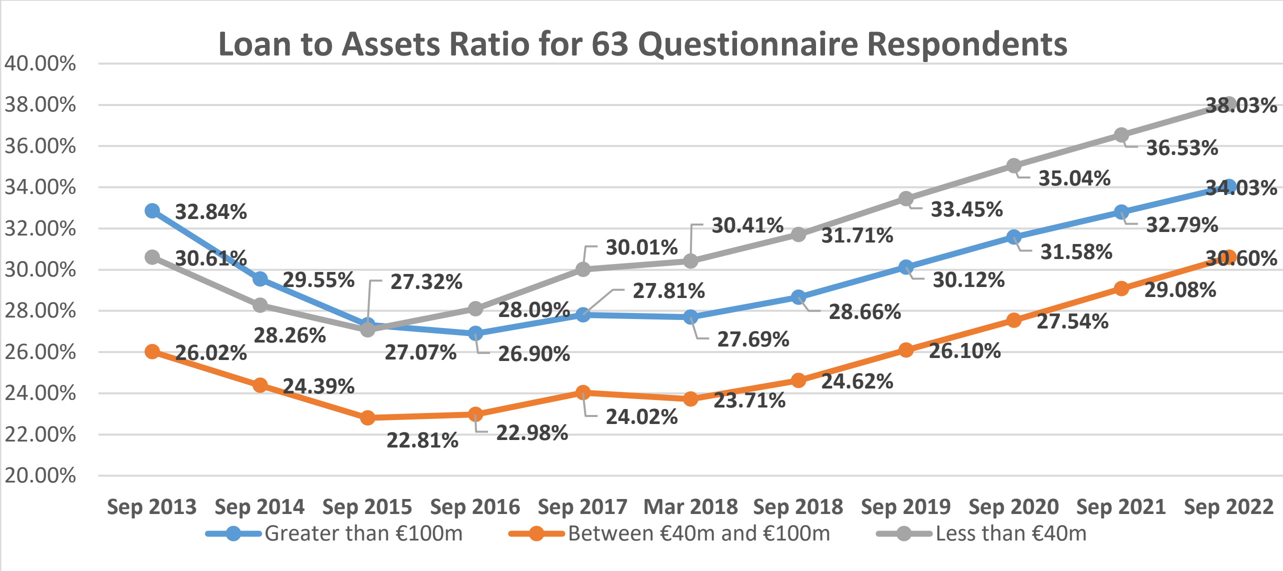
The responses from 172 individual credit unions to the questionnaire comprise the dataset for analysis purposes of the questionnaire[3]. Of the respondents contained in the dataset, 63[4] of these respondents indicated that the current lending maturity limits are not sufficient for them to meet forecasted loan demand out to 30 September 2022. These 63 credit unions were requested to provide a breakdown of the forecasted loan activity for the credit union from March 2018 to September 2022 which included the forecasted loan category split and loan maturity split for lending. Outlined below is a summary of the information provided by these respondents in relation to forecasted loan activity.

2.2.1 Forecasted Lending Activity

The average loan to asset ratio is forecast to increase from 27.4% to 34.1% for these 63 credit unions – the forecasts demonstrate an incremental increase year on year in the LTA ratio over the period to September 2022. Total loans are forecast to grow on an overall basis by 50.5% with a corresponding increase in total assets of 19.9%. Chart 4 demonstrates the forecasted average LTA ratio for credit unions of varying asset size and also illustrates the historic LTA for these credit unions.

[3] 181 responses were received to the questionnaire, 9 of these were excluded from the dataset for analysis purposes due to data quality and consistency issues.
[4] 37 of these credit unions have total assets of at least €100 million.

Chart 4 | Loan to Asset Ratio for Credit Unions of Varying Asset Size



Source: Credit Union Prudential Returns and Credit Union Longer Term Lending Questionnaire

2.2.2 Forecasted Lending Activity by Loan Category

The data provided by questionnaire respondents in relation to forecasted lending outlines that there will be a change in the profile of credit union lending with a higher average proportion of total loans forecast to be in the house loan and commercial loan categories with a corresponding reduction in the proportion of total loans in the personal loan category. Table 7 illustrates the average proportion of total loans held in each of the loan categories specified at 31 March 2018 versus the forecasted split of total loans by 30 September 2022.

Table 7 | Percentage of Total Loans by Loan Category (March 2018 v Forecast September 2022)

Loan Category	% of Total Loans Mar 2018	% of Total Loans Sep 2022
Car Loans	28.1%	24.5%
Home Improvement Loans	25.6%	24.8%
Education Loans	3.3%	3.5%
Other Personal Loans	35.6%	30.8%
House Loans	4.5%	10.8%
Commercial Loans	2.9%	5.6%

Source: Credit Union Longer Term Lending Questionnaire

Table 8 displays the forecasted average split of total loans by loan category for 30 September 2022 for credit unions with varying asset sizes. This indicates that it is the larger credit unions (i.e. those with total assets of at least €100 million) on average that are likely to have a higher proportion of total lending exposed to house loans.

Table 8 | Forecasted Average Split of Total Loans by Credit Unions of Varying Asset Size

Loan Category	Credit Unions Total Assets ≥€100 million	Credit Unions Total Assets ≥ €40million and < €100 million	Credit Unions Total Assets < €40 million
Car Loans	24.3%	22.9%	26.8%
Home Improvement Loans	24.6%	20.9%	29.1%
Education Loans	3.4%	3.4%	4.1%
Other Personal Loans	31.3%	37.1%	22.9%
House Loans	12.0%	9.6%	8.7%
Commercial Loans	4.3%	6.3%	8.5%

Source: Credit Union Longer Term Lending Questionnaire

2.2.3 Forecasted Lending Activity by Maturity

Data analysis for the 63 respondents included within the dataset indicates that these credit unions currently have a higher proportion of their loan books over longer maturities when compared to the sector average- 19.2% of loans are outstanding for periods of greater than 5 years (versus a sector average of 12.9%) and 4.6% of loans are outstanding for periods of greater than 10 years (versus a sector average of 2.1%).

These credit unions forecast to increase their loan book maturities across both maturity categories out to 30 September 2022. Table 9 illustrates the forecasted average proportion of lending in each of the maturity categories expressed as a percentage of total forecasted loans and as a percentage of total forecasted assets.

Table 9 | Forecasted Average Lending by Maturity by Credit Unions of Varying Asset Size

Credit Union Asset Category	Average % of Gross Loans Outstanding > 5 Years as a % Total Forecasted Loans	Average % of Gross Loans Outstanding > 10 Years as a % Total Forecasted Loans	Average % of Gross Loans Outstanding > 5 Years as a % Total Assets	Average % of Gross Loans Outstanding > 10 Years as a % Total Assets
Credit Unions Total Assets ≥€100 million	32.3%	12.7%	11.3%	4.6%
Credit Unions Total Assets ≥€40 million and <€100 million	30.3%	9.8%	9.3%	2.9%
Credit Unions Total Assets <€40 million	31.0%	9.3%	12.4%	4.0%

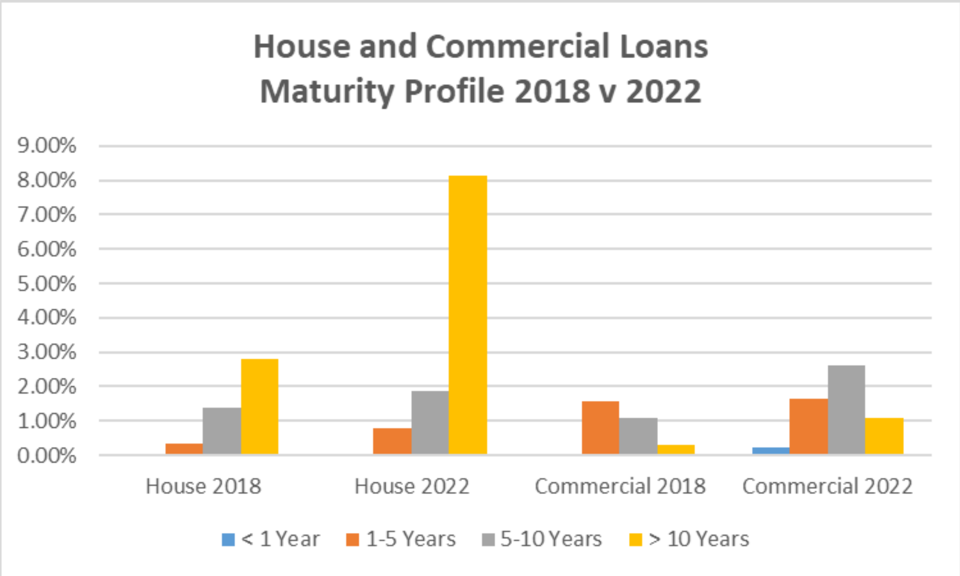
Source: Credit Union Longer Term Lending Questionnaire

2.2.4 Forecasted Lending Activity by Loan Category and Maturity Profile

Data analysis of the questionnaire dataset indicates that credit unions' longer term lending will be concentrated within the house and commercial loan categories. Questionnaire respondents indicated that currently 92.6%, 4.5% and 2.9% of total loans outstanding relate to personal, house and commercial loans respectively. This is forecasted to change to 83.6%, 10.8%, 5.6% by September 2022 for personal, house and commercial loans respectively.

As indicated previously, 4.5% of total loans are currently outstanding for greater than 10 years for those credit unions who have indicated that the maturity limits are not sufficient to meet forecasted loan demand. This is forecast to increase to 11.4% by 2022 with personal, house and commercial loans over 10 years as a percentage of gross loans outstanding being 2.2%, 8.2% and 1.1% respectively. The most significant forecast change in loan maturity profile is within the house and commercial loan categories in the greater than 5 and 10 year maturity buckets. This is illustrated on Chart 5 below.

Chart 5 | House and Commercial Lending Maturity Profile – 2018 versus 2022 Forecast



Source: Credit Union Longer Term Lending Questionnaire

2.2.5 Forecasted Funding Profile

Questionnaire respondents forecast savings growth of c.19.8% from 31 March 2018 to 30 September 2022 when it is forecast that savings held by these respondents will amount to c.€8.5bn compared to €7.1bn at 31 March 2018. Currently c.98% of total savings are available on demand. This is forecast to decrease slightly to c.94% which suggests that these credit unions are not planning to significantly change their funding profile as their lending profile shifts to longer term maturities.

3. Potential Changes to Lending Framework

The following changes, which reflect what the Central Bank views to be an appropriate lending framework for credit unions taking account of their risk management and operational capabilities, are being considered in relation to the credit union lending framework:

- removal of the 5 and 10 year maturity limits currently contained in the lending regulations;
- imposition of a maximum loan term for unsecured lending;
- introduction, on a tiered basis, of a combined concentration limit for house and commercial lending;
- re-name of the 'commercial loan' lending category and re-define of the same; and
- prescribe what constitutes a large exposure.

It is considered that all of these changes, when taken together, would provide an appropriate framework for credit union lending into the future. The composition of the loan book, including exposure to different loan categories and different maturity profiles, remains a matter for each credit union taking into account the risk appetite of the credit union and its members.

3.1 Lending Maturity Limits

Regulation 14 of the 2016 Regulations contains lending maturity limits which restrict the overall percentage of a credit union's total loans which can be outstanding for periods of greater than 5 and 10 years. The 2016 Regulations state that no more than 30% and 10% of total gross loans may be outstanding for more than 5 and 10 years respectively. These percentage limits may be increased to 40% and 15% where additional approval is granted by the Central Bank.

The Central Bank is giving consideration to the removal of these lending maturity limits from the lending framework. This would remove the restriction on the overall percentage of lending which can be outstanding over 5 and 10 years. The proposals allow for the management of loan book maturities by reference to the type of lending in which the credit union engages.

3.2 Maturity Limit for Unsecured Lending

The proposal to remove the lending maturity limits which limit the overall percentage of lending which can be outstanding for longer periods as outlined in 3.1 would introduce a potential for the maturity profile of credit union lending to lengthen. The maximum loan term for credit union lending is currently 25 years, which is still viewed as appropriate given the funding profile of credit unions and the type of longer term lending credit unions are likely to undertake (i.e. residential mortgages), therefore no change is proposed in that regard. The Central Bank is considering the introduction of a maximum loan term of 10 years for unsecured lending to ensure that such lending has an appropriate maturity profile.

3.3 Concentration Limit for House and Commercial Loans

The 2016 Regulations contain a concentration limit of 50% of regulatory reserves for commercial lending. The Central Bank is giving consideration to the introduction of a new combined concentration limit for house and commercial lending to ensure suitably balanced portfolios with appropriate weightings in these loan categories. In addition, this concentration limit would facilitate the monitoring of loan book maturities given that the majority of longer term loans in credit unions are house or commercial loans. The potential combined concentration limit for house and commercial (small business loans as set out in section 3.4 below) lending being considered is 7.5% of Total Assets.

It is also being considered that a further permitted level of lending could be introduced on a tiered basis, whereby credit unions would be permitted to apply for approval to avail of an increased concentration limit for house and commercial loans of 15% of Total Assets. The Central Bank would have to approve individual credit unions to avail of this additional limit. Credit unions will be required to demonstrate with appropriate evidence that they have strong core foundations including the skills, expertise, risk management and operational capability to undertake an increased element of lending in these loan categories via an approval process. In addition, credit unions seeking to avail of this increased concentration limit will be required to demonstrate that they have financial strength and resilience including a strong reserve and liquidity position and a clear understanding and appreciation of the specific risks associated with this type of lending. They will also be required to outline how they propose to address and manage these specific risks.

It is also being proposed that the current provision contained in the 2016 Regulations whereby only commercial loans granted for > €25,000 utilise the commercial lending concentration limit will be removed so that all commercial loans issued/outstanding will utilise the commercial lending concentration limit. This is aimed at ensuring that a credit union would not have an exposure to commercial lending additional to that provided for in the concentration limit.

It is also the Central Bank's intention to state in the regulations that buy to let residential lending and buy to let commercial lending is prohibited under the lending framework for credit unions. This prohibition on buy to let loans takes account of credit union risk management and operational capabilities and what is prudentially appropriate for credit union lending given the higher risk profile of this type of lending.

3.4 Re-name and Re-define of Commercial Loans Lending Category

The Central Bank is giving consideration to re-naming the permitted loan category of 'commercial loans' to 'small business loans' as it is viewed that this definition might more accurately reflect the type of lending being undertaken in this category. The current definition for a commercial loan contained in the 2016 Regulations is 'a loan, the primary objective of which is to fund an activity the purpose of which is to make a profit'. A proposed definition for a small business loan would be 'a loan made for the purpose of financing the working capital or capital investment needs of an owner managed small business enterprise'.

If the commercial loan lending category is re-named and redefined, it is the Central Bank's intention that the concentration limit outlined in section 3.3 for house and commercial lending would apply to house loans and the new loan category of small business lending.

3.5 Large Exposures

In order to mitigate the concentration risks arising from an increase in exposure to larger loans, the Central Bank is considering prescribing in the lending regulations what constitutes a large exposure.

The Central Bank is proposing that a large exposure will be defined as any exposure to an individual borrower or group of borrowers who are connected of 2.5% or more of the regulatory reserves of the credit union. From a prudential perspective the introduction of a large exposures regime allows for the management and monitoring of borrower concentration risk. A large exposure regime exists for other credit institutions and was introduced under the Capital Requirements Directive. Post commencement of amending lending regulations for credit unions the

Central Bank intends to enhance the current reporting framework to gather additional information on large exposures.

4. Analysis of Costs, Benefits and Impacts for each Potential Change

The costs and benefits for credit unions and the credit union sector as a whole have been considered for each of the potential changes to the lending framework outlined in section 3. The impact of each of the potential changes including the potential limits has been assessed on an individual and collective basis to understand the impact on individual credit unions and on the sector overall.

The Central Bank would like to highlight the challenges/limitations associated with undertaking a RIA on these potential changes to the lending framework. The analysis on the likely impact of the potential changes has been undertaken subject to certain assumptions which are specified throughout this section. It is a matter for individual credit unions to set their own risk appetite for lending within the parameters set out in the lending framework. The resulting impact of the potential changes to individual credit unions in terms of the composition of their loan book and the resulting impact on their Asset and Liability Management (ALM) will be specific to the decisions taken by each individual credit union. No specific analysis has been performed on the likely impact on income, as this is considered a matter for each credit union to identify relative to the composition of their loan book.

4.1 Information Sources

Data provided to the Central Bank through the quarterly Prudential Return informed the analysis of the impact of the potential changes and associated limits. Where financial data analysis has been performed this is by reference to the March 2018 Prudential Returns submitted by individual credit unions. In addition, data analysis has been informed by the responses to the questionnaire on lending which was issued in April 2018.

Credit unions may wish to provide additional information or data analysis they may have on the potential impact of the potential changes to the lending framework through any responses they provide to CP125.

4.2 Costs

The changes to the lending framework outlined in CP125 are unlikely to introduce significant additional costs for credit unions, however this will be dependent on the lending strategy being pursued by each individual credit union. If the proposals contained in CP125 are introduced to the 2016 Regulations, this will provide increased scope for credit unions to engage in increased longer term lending including house and commercial lending. The portfolio composition of credit union loan books, including the proportion of loans held over longer maturities and the proportion held in specific loan categories, is a matter for credit unions to determine in accordance with their strategy and risk appetite.

With discussion for a number of credit unions turning to business model development, with an increased focus on house loans in particular, the Central Bank expects credit unions to undertake a thorough assessment of the incremental costs associated with increased lending with longer maturities or additional lending in specific loan products/categories.

Expanding longer term lending carries specific financial risks - if the forecast revenues fail to materialise to the extent anticipated, and / or the associated costs are higher than anticipated, it may be detrimental to the overall financial position of the credit union and its members. It is essential, therefore, that revenue and cost models are comprehensive and realistic at the outset before the lending profile of the credit union is changed significantly. A change in the strategy of a credit union to focus more heavily on specific categories of lending may also increase costs to the credit union as additional investment may be required related to the risk management framework, the acquisition of specific skillsets required to facilitate such lending, staff training and increased marketing, compliance and legal costs. IT system changes to facilitate enhanced management information and reporting requirements for house and commercial lending will also be required with associated costs. Credit unions may find the Longer Term Lending Guidance for Credit Unions which the Central Bank published in December 2017 useful in informing these considerations.

4.3 Benefits

The potential changes to the lending framework outlined in CP125, including the move away from maturity limits based on a percentage of outstanding loans, will provide increased flexibility for credit union lending. The removal of the lending maturity limits will provide additional scope to credit unions to increase longer term lending in a risk appropriate manner. This in turn may allow for increased diversification across credit union loan books, both in terms of loan category and maturity profile. The combined concentration limit for house and commercial loans in conjunction with the removal of the lending maturity limits will provide credit unions with increased flexibility to manage their loan books within their own individual risk appetite against the backdrop of a regulatory framework that facilitates credit unions' development through a balanced loan portfolio. An increase in the proportion of longer term, larger scale loans may also result in lower churn rates in loan books which may positively impact on return on lending- this was mentioned by a number of respondents to the questionnaire on longer term lending which was issued to credit unions.

The proposed changes to the lending framework and the potential increased flexibility which these changes will afford to credit unions may also present credit unions with an opportunity to increase lending capacity overall. Given depressed LTA ratios across the sector, the changes may facilitate credit unions who wish to increase LTA ratios across a balanced loan portfolio and potentially make a positive contribution to return on assets.

4.4 Impacts

The impact of each of the changes to credit union limits has been assessed to identify how they will affect credit union lending capacity. Calculations have been performed to assess the potential overall sector impact and the impact on credit unions of varying asset sizes. Where assumptions have been made, these are specified within the relevant section. In addition to this analysis, where practical, an assessment of the impact of the proposed limits has also been assessed by reference to the lending data forecast by respondents to the lending questionnaire.

4.4.1 Removal of Lending Maturity Limits

The 2016 lending regulations place a limit on the maximum amount of loans which can be outstanding for periods of greater than 5 years and greater than 10 years. The proposed changes to the regulations including the removal of the lending maturity limits provide for increased concentration limits for house and commercial lending which can be utilised based on the credit union being granted additional approval by the Central Bank.

The lending maturity limits are currently calibrated as a percentage of total loans of the credit union. Based on credit union lending as at 31 March 2018, the capacity at an overall sector level which the limits and any additional approvals which have been granted under the 2016 Regulations (currently availed of by 15 credit unions as at 30 September 2018) provide lending capacity for loans outstanding for greater than 5 and 10 years as illustrated on Table 10.

Table 10 | Sector Lending Capacity under the 2016 Regulations

	Lending > 5 Years	Lending > 10 Years
Sector Capacity in Each Maturity Category	€1.43 bn	€0.49 bn

Source: Credit Union Prudential Returns

The removal of these limits will remove the constraint placed on credit unions with regard to the proportion of loan books which can be held in maturities of greater than 5 years and greater than 10 years. This will provide increased flexibility to credit unions with regard to the composition of their loan book. This should address concerns that credit unions are unduly constrained within the 5 to 10 year maturity bucket which is limiting capacity to pursue personal lending opportunities in that area.

Analysis has been undertaken in section 4.4.6 which considers broader balance sheet maturity implications for the changes being proposed to the lending framework.

4.4.2 Maturity Limit for Unsecured Lending

The introduction of a maturity limit of 10 years for unsecured lending is aimed at ensuring that an inappropriate amount of credit risk is not introduced into credit union loan books by unsecured loans being advanced for longer maturities.

Data analysis based on questionnaire respondents indicates that a very small proportion of personal and commercial loans with a greater than 10 year maturity are unsecured loans. The data indicates that c.0.9% and c.1.6% of total personal and commercial loans respectively are unsecured with a maturity of greater than 10 years. Based on this, it is envisaged that the introduction of a maximum loan term for unsecured lending of 10 years will not constrain to a material extent credit union lending. Furthermore, when it is considered that these loans could be secured by way of shares and the proposed definition for secured lending recognises attached shares as security, the impact of the proposal to introduce a maximum loan term for unsecured loans of 10 years will be limited.

4.4.3 Tiered Concentration Limit for House and Commercial Loans

Analysis has been undertaken to assess the impact of the proposed combined concentration limits for house and commercial lending[5]. Analysis has been undertaken with reference to the proposed base limit of 7.5% of total assets for all credit unions and the proposed increased concentration limit of 15% of total assets which would be subject to an application and approval process for credit unions of sufficient scale who can demonstrate that they have the capability to avail of this increased concentration limit. The adequacy of the limits by reference to the forecasted lending activity for those respondents who provided this information in the questionnaire has also been assessed. The results of this analysis is presented below.

1. Base Proposed Concentration Limit for House and Commercial Lending – available without approval

This analysis is based on the proposed concentration limit of 7.5% of total assets as outlined in CP125 for combined exposures in house and commercial lending. This analysis has also assessed the maximum amount of lending which would be available to all credit unions in either the house loan or commercial loan categories i.e. the 5% of Total Assets specific loan category limit inherent in the overall combined concentration limit proposed.

[5] Which will be re-named and re-defined as "small business lending".

Table 11 outlines the maximum capacity that this limit would provide to credit unions for lending within commercial and house loans.

Table 11 | Lending Capacity for House and Commercial Loans – Proposed Base Concentration Limit

Credit Union Asset Category	Combined Concentration Limit 7.5% Total Assets	Inherent Specific Loan Category Limit for Commercial or House Loans 5% of Total Assets
Credit Unions Total Assets ≥€100 million	€713.8 m	€475.8 m
Credit Unions Total Assets ≥€40 million and <€100 million	€377.5 m	€251.6 m
Credit Unions Total Assets <€40 million	€199.6 m	€133.1 m
Total Sector	**€1,291 m**	**€861 m**

Source: Central Bank Analysis

These proposed limits for all credit unions would provide scope for c.€1.29 billion of overall sector lending to be advanced for house and commercial loans. The maximum amount of lending for any one specific category of loan would be limited to €861 million at a sector level i.e. no more than this amount could be exposed to house loans or commercial loans.

Analysis has been undertaken to assess the total capacity which this proposed base combined concentration limit would provide to credit unions of varying asset sizes for house and commercial lending. Table 12 presents the results of this analysis and illustrates the maximum and minimum capacity of credit unions within these asset categories (reflective of the largest and smallest credit union by asset size in each cohort). Given that the capacity is a function of asset size, it is those credit unions with larger assets who will have higher capacity for house and/or commercial lending. Table 13 presents the maximum exposure which the 5% of total assets proposed limit for a specific category of lending would permit in addition to illustrating the maximum and minimum capacity available to credit unions of varying asset sizes in either of these loan categories.

Table 12 | Lending Capacity for House and Commercial Loans – Proposed Base Concentration Limit- Credit Unions of Varying Asset Size

Credit Union Asset Category	Average Capacity	Maximum Capacity	Minimum Capacity
Credit Unions Total Assets ≥€100 million	€13.5 m	€31 m	€7.8 m
Credit Unions Total Assets ≥€40 million and <€100 million	€4.7 m	€7.4 m	€3.0 m
Credit Unions Total Assets <€40 million	€1.5 m	€2.9 m	€0.1 m

Source: Central Bank Analysis

Table 13 | Max Lending Capacity for either House or Commercial Loans – Proposed Base Concentration Limit- Credit Unions of Varying Asset Size

Credit Union Asset Category	Average Capacity	Maximum Capacity	Minimum Capacity
Credit Unions Total Assets ≥€100 million	€8.9 m	€20.7 m	€5.2 m
Credit Unions Total Assets ≥€40 million and <€100 million	€3.1 m	€4.9 m	€2.0 m
Credit Unions Total Assets <€40 million	€1.0 m	€1.9 m	€0.05 m

Source: Central Bank Analysis

An assessment has also been undertaken to identify the potential impact for credit unions should these concentration limits be introduced relative to their current loan book portfolio and the amount of loans currently outstanding for house and commercial lending. Where assessment is made by reference to commercial loans this is by reference to all commercial loans currently outstanding as it is being proposed that all commercial loans issued and outstanding will now utilise the concentration limit for commercial lending contained in the lending framework.

This analysis suggests that all credit unions with the exception of 2 would have additional scope for increasing their combined house and commercial lending. Table 14 illustrates the proportion of total house and commercial loans outstanding as a percentage of total assets and the number of credit unions within each of these percentage categories. As can be seen the vast majority of credit unions (248) have less than 4% of total assets in house and commercial loans combined and as a result the proposed concentration limits would provide headroom/additional capacity for these credit unions to increase lending within these loan categories. The monetary value of this headroom is also presented in table 14.

Table 14 | Analysis of Current House and Commercial Lending and Applicable Headroom relative to Proposed Base Concentration Limit

Total Commercial and House Loans as a % Total Assets	Number of Credit Unions	Headroom €
< 1%	182	672.5 m
≥ 1% and < 2%	36	206.2m
≥ 2% and < 3%	20	86.4 m
≥ 3% and < 4%	10	43.0 m
≥ 4% and < 5%	7	23.3 m
≥ 5% and < 6%	3	14.4 m
≥ 6% and < 7%	3	1.5 m
≥ 8% and < 9%	1	0 m
≥ 9% and < 10%	1	0 m
Total	**263**	**€1,047.3 m**

Source: 31 March 2018 Prudential Return and Central Bank Analysis

Table 15 illustrates the percentage of total assets which are currently held by credit unions in house and commercial loans separately. As can be seen the majority of credit unions have total house or total commercial loans individually at less than 3% of total assets. This suggests that if the proposed concentration limit was introduced, which would place a limit of 5% of total assets on the amount of house or commercial lending which a credit union may undertake, headroom would exist for credit unions to increase their lending in either of these loan categories to 5% of total assets, within the parameters of the combined concentration limit for house and commercial lending of 7.5% of total assets.

Table 15 | Analysis of Current House and Commercial Lending as a % of Total Assets

Commercial and House Loans as a % Total Assets	Number of Credit Unions- Commercial Loans	Number of Credit Unions- House Loans
< 1%	223	217
≥ 1% and < 2%	25	25
≥ 2% and < 3%	6	10
≥ 3% and < 4%	4	5
≥ 4% and < 5%	4	4
≥ 5% and < 6%	0	1
≥ 6% and < 7%	0	1
≥ 7% and < 8%	1	**0**
Total	**263**	**263**

Source: 31 March 2018 Prudential Return

Based on the March 2018 Prudential Return data and as illustrated above there are only 3 credit unions who currently have an exposure to house or commercial loans of greater than 5% of total assets. If the proposed concentration limits were introduced these credit unions would not be permitted to increase their lending within the loan category which has a current exposure of greater than 5% of total assets. Transitional arrangements in the regulations would allow these credit unions to retain all loans which they hold from the point of introduction of these proposed limits to maturity. In addition, these credit unions may have the option of applying for approval (subject to meeting required criteria) to avail of the increased combined concentration limit for commercial and house loans of 15% of total assets, if this proposed concentration limit is also introduced into the framework.

2. Proposed Increased Concentration Limit for House and Commercial Lending

CP125 proposes an increased concentration limit for house and commercial loans of 15% of total assets for those credit unions approved by the Central Bank. Analysis has been undertaken to assess the scope which this increased limit would provide for credit unions with regard to house and commercial lending. It has been articulated in CP125 that scale, available resources and capability would be a necessary pre-requisite for those credit unions wishing to expand their lending into longer term lending products. As a result it is envisaged that in the initial stages it is only larger credit unions who are expected to apply for approval to avail of the increased concentration limit. Therefore, for the purposes of this analysis it is assumed that only those credit unions with assets of at least €100 million will apply for approval to avail of the increased limit[6].

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[6] It is noted in the CP that credit unions with total assets of at least €100 million may be indicative of those credit unions who will be capable of demonstrating the necessary scale, available resources and capability to undertake increased house and/or commercial lending.

Table 16 outlines the maximum amount of house and commercial lending which these credit unions could undertake based on approval being granted, in addition to the maximum and minimum amount of loans in these loan categories. Table 17 indicates the additional headroom which approval would afford to these credit unions versus the proposed base concentration limit.

Table 16 | Lending Capacity for House and Commercial Loans – Proposed Increased Concentration Limit- Credit Unions with Total Assets ≥ €100 million

Credit Unions Total Assets ≥ €100 million	Increased Limit of 15% Total Assets
Overall capacity for house and commercial lending	€1,427.5 m
Average capacity for house and commercial lending	€26.9 m
Maximum capacity for house and commercial lending	€62.1 m
Minimum capacity for house and commercial lending	€15.5 m

Source: Central Bank Analysis

Table 17 | Lending Capacity for House and Commercial Loans for credit unions with Total Assets ≥ €100 million- Proposed Base Concentration Limit versus Proposed Increased Concentration Limit

Credit Unions Total Assets ≥ €100 million	
Base Limit- house and commercial lending	€713.8 m
Increased Limit- house and commercial lending	€1,427.5 m
Additional headroom with increased limit	€713.8 m

Source: Central Bank Analysis

Adequacy of limits relative to forecasted house and commercial loans

Notwithstanding that the level of house and commercial lending across the sector is quite small at this time at an average of 3.6% of total loans combined, and that the analysis above indicates that the proposed base limit would provide headroom to the majority of credit unions to increase their lending in these categories, the Central Bank has also undertaken analysis to assess the adequacy of the proposed concentration limits (both the base and increase combined concentration limits) relative to the forecasted lending activity of credit unions based on the data provided by credit unions in their responses to the lending questionnaire issued in April 2018.

Of the 172 questionnaire respondents included within the dataset for analysis of questionnaire responses, 63 provided forecasted lending data which shows the projected split of credit union lending in specific loan categories and across specific maturity buckets out to September 2022. These forecasts are discussed in detail in section 2 of this RIA.

The projected percentage of house and commercial lending for questionnaire respondents expressed as a percentage of forecasted total assets is displayed on Table 18.

Table 18 | Forecasted Lending Data in House and Commercial Loan Categories as a % of Total Assets

	Number of Credit Unions Total Assets ≥ €100m	Number of Credit Unions Total Assets ≥€40m and < €100m	Number of Credit Unions Total Assets < €40m	Total Number of Credit Unions
Total Number of Questionnaire Respondents	37	13	13	**63**
House and Commercial Loans as a % Forecasted Assets				
< 5%	19	7	6	**32**
≥ 5% and < 7.5%	8	5	1	**14**
≥ 7.5% and < 10%	6	0	1	**7**
≥ 10% and < 15%	3	1	3	**7**
> 15%	1	0	2	**3**

Source: Credit Union Longer Term Lending Questionnaire

The analysis above appears to show that the base limit of 7.5% of total assets will provide sufficient capacity for 46 of the 63 questionnaire respondents. However, further analysis of the data shows that the base concentration limit will provide sufficient capacity for 40 of the 63 questionnaire respondents to undertake their forecasted lending on a 5 year time horizon. This is because 6 credit unions forecasted to lend more 5% of the individual category limit in either commercial or house lending (3 of these credit unions have assets less than €100m and 3 have assets more than €100m). Of the 23 credit unions for which the base limit is not sufficient for forecasted lending, 10 have assets of less than €100 million and 13 have assets of at least €100 million.

Of the 10 credit unions with assets less than €100 million that the base does not satisfy forecasted lending, 7 credit unions forecasted combined house and commercial lending in excess of the 7.5% base concentration limit and 3 forecasted either house or commercial lending over the 5% single category limit.

The increased concentration limit of 15% of total assets would provide sufficient capacity for the forecasted lending activity of 12 of the 13 credit unions with assets of at least €100 million for which the 7.5% base limit is not sufficient[7]. This would leave just 1 credit union of 37 credit unions with assets of at least €100 million where the increased lending limit would not provide sufficient capacity for forecasted lending over a 5 year time horizon to September 2022.

In summary, data analysis of forecasted lending activity provided by the 63 questionnaire respondents indicates that the proposed concentration limits (7.5% of total assets base limit and 15% of total assets increased limit) will be sufficient to facilitate the forecasted house and commercial lending for 52 (83%) of these credit unions. The Central Bank is supportive of credit unions increasing lending including engaging in new areas of lending and increasing exposure to longer term lending as part of a balanced loan portfolio. It is viewed that a balanced loan portfolio, supported by strong risk management capability can increase diversification in loan books and help to manage credit

[7] For the purpose of this analysis we assume that it is only credit unions with assets of at least €100 million that seek approval for the increased combined house and commercial lending limit of 15% of total assets.

concentration risks to which credit unions may be exposed. We would caution however that all lending should be prudently undertaken, well-managed and in line with credit unions' strategy, capabilities and risk appetite. Credit unions should be aware of the risks and related considerations for new areas of lending including increased longer term lending.

4.4.4 Re-name and Re-define of Commercial Loans Lending Category

It is not considered that the re-name of commercial loans to small business loans would have any significant impact on credit unions undertaking this category of lending. It is considered that the definition of a small business loan will better reflect the types of business lending which credit unions currently engage in and as a result will not preclude credit unions from any area of lending in which they aspire to engage.

4.4.5 Large Exposures

Analysis has been undertaken based on the 31 March 2018 Prudential Returns submitted by individual credit unions to assess whether any credit union loan would currently qualify as a large exposure based on the proposal to define a large exposure to a borrower or group of borrowers who are connected as any exposure equal to or greater than 2.5% of the regulatory reserve of the credit union.

Large Exposures

Analysis of the Top 5 Large Exposures information provided on the Prudential Return indicates that 81 credit unions or 30.8% of credit unions who reported for March 2018 currently have loans which meet the proposed definition of a large exposure of equal to or greater than 2.5% of the regulatory reserve of the credit union. The number of loans which these credit unions currently have which would qualify as a large exposure is detailed in Table 19[8].

Table 19 | Number of Credit Unions with Large Exposures (by number of Large Exposures)

Number Of Large Exposures Based on Top 5 Borrowers	Number of Credit Unions
1 Large Exposure	32
2 Large Exposures	9
3 Large Exposures	6
4 Large Exposures	5
5 Large Exposures	29
Total	**81**

Source: 31 March 2018 Prudential Return

Table 20 indicates the average loan amount which would meet the definition of a large exposure within each of the different asset size credit unions.

[8] Credit unions only report their Top 5 Large Exposures on the Prudential Return so the 29 credit unions who currently have 5 loans which would meet the proposed definition of a large exposure could potentially have more loans that would also meet the proposed large exposure definition.

Table 20 | Average Value of Large Exposure by Credit Unions of Varying Asset Size

Credit Union Asset Category	Average Large Exposure Loan Size
Credit Unions Total Assets ≥€100 million	c.€0.493m
Credit Unions Total Assets ≥€40 million and <€100 million	c.€0.173m
Credit Unions Total Assets <€40 million	c.€0.056m

Source: Central Bank Analysis based on 31 March 2018 Prudential Return

It is not viewed that the proposed definition of a large exposure will impact significantly on credit unions. As indicated in CP125 credit unions will be required to report more detail than they currently do on large exposures which they have granted and which are outstanding at the relevant reporting date. It is not envisaged that this enhanced reporting will pose a significant challenge for credit unions.

4.4.6 Balance Sheet Maturity Profile

CP125 proposes the removal of the lending maturity limits for credit unions and analysis of the proposal is contained in 4.4.1 above. The consultation paper also proposes to introduce a combined concentration limit for house and commercial loans on a tiered basis and the impact of this has been considered in 4.4.3. The combined impact of these two proposals will now be considered.

The maximum loan maturity of 25 years will remain for all credit union loans. It is viewed that the imposition of concentration limits for house and commercial lending will allow for the monitoring of loan book maturities given that data analysis suggests it is these two categories of loans which are likely to have longer maturities. The investment framework for credit unions places a maximum maturity on credit union investments of 10 years with the exception of investment in Tier 3 Approved Housing Bodies (AHBs), which subject to a concentration limit may have a maturity of up to 25 years.

In arriving at the proposed concentration limits for the base and increased combined concentration limits for lending in house and commercial loans, the interaction with the concentration limit for Tier 3 AHBs was considered. This concentration limit permits that 25% of the regulatory reserves of a credit union can be invested in Tier 3 AHBs where the total assets of the credit union are less than €100 million. This can be increased to 50% of regulatory reserves of a credit union where the total assets are greater than €100 million. Based on a 10% regulatory reserve, this equates to 2.5% and 5% of total assets respectively.

Combining the permitted percentage of total assets which may be held in house and commercial loans and the permitted percentage of total assets which may be held in Tier 3 AHBs gives an indication of the maximum amount of credit union sector assets which may be held over longer maturities i.e. greater than 10 years. Table 21 presents the percentage of total assets of an individual credit union which may be held over 10 years based on an assumption that all lending in house and commercial loans has an origination maturity of greater than 10 years, that all investments in Tier 3 AHBs have a maturity of greater than 10 years and that no other credit union lending has a maturity of greater than 10 years. This also assumes that the maximum concentration limit is exercised for both lending and investment. The available limit for longer term assets for an individual credit union is obviously dependent on the applicable Tier 3 AHB concentration limit and the allowable combined concentration limit for house and commercial lending.

Table 21 | Potential Percentage of Credit Union Assets > 10 Years Maturity

	Tier 3 AHB Basic Concentration Limit	Tier 3 AHB Higher Concentration Limit
Base Proposed Concentration Limit for House and Commercial Loans	10.0%	12.5%
Increased Proposed Concentration Limit for House and Commercial Loans	17.5%	20.0%

Based on the table above if a credit union has total assets of €120 million and therefore has a concentration limit for Tier 3 AHB investment equivalent to 5% of Total Assets and has not applied to avail of the increased limit for house and commercial lending so has the base proposed concentration limit of 7.5%, this credit union will have the potential for 12.5% of its total assets to be held longer term, on the assumption that house and commercial loans are longer term.

As can be seen from Table 21, if the proposals for amendment to the lending framework are introduced there is potential that the percentage of credit union assets which may be held over longer maturities could increase to 20%. However this figure is likely to be significantly less given that not all house and commercial loans will have a maturity of greater than 10 years, and where loans have a maturity of greater than 10 years at origination, as the loan amortises the outstanding maturity of the loan will reduce. In addition, no credit unions have undertaken Tier 3 AHB investment to date.

Data provided in response to the questionnaire indicates that the funding structure of credit unions is unlikely to change significantly with c.94% of funding forecast to be on demand in 30 September 2022. The Central Bank considers that the proposals contained in CP125 for amendment to the lending framework will not exacerbate to a material extent the asset and liability mismatch which exists on credit union balance sheets due to the nature of credit union funding. Credit union funding tends to be quite stable and has performed as such over and since the onset of the financial crisis. In addition, the strong liquidity profile of the sector is recognised which is mainly a result of the low loan to asset ratio and the excess funds available to credit unions for investment supported by the liquidity requirements contained in the 2016 Regulations.

5. Consultation

As outlined in the Consultation Protocol for Credit Unions issued on 27 November 2012, the Central Bank has committed to consult on proposed new regulations, which in the Central Bank's view, will have a significant impact on the business of credit unions.

Consultation on potential changes to the lending framework for credit unions is contained within CP125. This RIA is included as an Appendix within the consultation paper.

6. Enforcement and Compliance

The responsibility for enforcing and ensuring compliance with the lending regulations for credit unions will rest with the Central Bank.

7. Review

The Central Bank will consider the feedback received on CP125and this RIA before publishing final lending regulations for credit unions. The Central Bank commits to performing and publishing an analysis on credit union sector lending three years post commencement of the new lending regulations for credit unions to assess and analyse the actual impact which any changes to the regulations have had.

8. Publication

The RIA will be published as part of CP125 which is available at https://www.centralbank.ie/.

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