

CP 88 - Consultation on Regulations for Credit Unions

on

commencement of the remaining sections of the 2012 Act.

Submission of Kilmallock Credit Union Limited

Kilmallock Credit Union Limited

Sarsfield St.,

Kilmallock,

Co. Limerick.

February 2015

Introduction & Background

We welcome the opportunity to address the issues, as we see them, arising from the Draft Regulations which are the subject of this consultation paper.

Kilmallock Credit Union is a small to medium size credit union with assets of 30m approx.

We have 7500 members in a mainly rural base. A lot of our common bond area has seen a reduction in services from financial institutions, leaving the credit union the main service provider for large numbers of members.

It is imperative that we remain in a position to provide current and new services to our members.

Main submission

We have structured our submission in line with the questions as set out in CP88.

1. **Draft Reserves Regulations** – the main change here appears to be the Initial reserve requirement for new Credit Unions. While we acknowledge that there have not been new credit unions established recently we are strongly of the belief that the freedom to set up a new credit union is an important right and choice that this regulation undermines. It is likely that there will be a need for new credit unions in the future given the absence of any credit union in some large towns/areas.
Any new regulations should be drafted on a risk weighted basis.
As it stands this regulation penalises new credit unions with reserve requirements that are significantly out of touch with the low level potential risk involved. Any Reserve Regulations specific to new credit unions should be commensurate with potential risk and should foster the growth of the movement as member's desire. This regulation is anti-democratic and punitive.

2. Draft liquidity regulations

The new definition of short term liquidity is helpful.

We have a question regarding the minimum liquidity ratios. The minimum liquidity ratio of 20% this is referred to as 20% of unattached shares, and the 10% short term liquidity ratio is referred to as 10% of unattached savings. There would appear to be an inconsistency here and it requires clarification.

In this credit union we have approximately €22million in unattached shares, but we also have over €7m in deposits. The minimum liquidity ratio as above would be 20%

of €22m, but the minimum short term liquidity would be 10% of €29m. Theoretically this could lead to the 10% being a larger sum than the 20%?

This regulation does not support the principle of good Asset Liability Management. It actually punishes credit unions for careful and prudent management.

ILCU Credit Unions have a total of € 8 billion in unattached savings in the Republic of Ireland. This regulation would require €80m of that to be left sitting in the banks with virtually no income. It appears that the Central Bank wants to support the Banks at the expense of credit unions. Regulations should not be introduced that give one operator an unfair advantage over another. This is unnecessary, unfair and it goes against the will of the people who choose to use credit union services as is their right. High Short term liquidity in Banks at the moment is due to low interest rates and when the ECB increases rates, which it will inevitably do, this situation will change.

3. Draft Lending Regulations

There are a number of issues with the lending regulations that we would like to address –

12.1 (a)-(e) There is insufficient definition of the categories of loan i.e. is a home improvement e.g. small extension loan, a personal or a house loan?

This is significant in that the regulations require the credit union to obtain the first legal charge for a house loan. This will be extremely difficult in most circumstances and for that reason the definition of house loan should be limited to the purchase of a house or site at most.

(For the purposes of clarification here there is some confusion as to whether a home improvement loan would be classified as a home loan, and thereby require a first legal charge.)

15. In general the concept of Maturity limits is acceptable however the limit at (15.3) of 25 years limits lending for housing or land purchase is anti-competitive. This is a portion of the market that should be open to Credit Unions on the same basis as it is open to other lending institutions by way of a Credit Union Services Organisation with maturity limits comparable to other institutions.

19. Related Party Lending – the treatment of related parties as suggested in the draft regulations amounts to unequal and partial treatment of members based not on their individual membership but on the involvement of a related party.

This requires treating such a member differently to others in borrowing and any change to the terms of such borrowing to the point of reporting it separately in the annual accounts. We feel very strongly that this unequal treatment is unfair.

The underwriting done by the Credit Union on all lending is sufficiently strong to protect all members. This regulation is likely to lead to a loss of volunteers and as such will weaken the movement as a whole. If this restriction were imposed on a bank the related parties would have the choice of moving to another branch of the same bank. This would keep the member's business within that bank.

Credit Union members do not have that choice. Each credit Union is an autonomous business and membership depends on being part of a common bond, often a geographically defined area. It is not open to members to simply move branches if they are related to a party in their credit union. They are left with no choice but to be treated differently.

The Central Bank at page 8 of CP88 states that *"The regulations have been developed to take account of the Central Bank's statutory mandate to regulate and supervise credit unions with a view to ensuring the protection of member's savings and the financial stability and well-being of credit unions generally"*

We accept that the Central Bank has such a mandate but believe that this treatment of related parties shows that these regulations have not been developed with the *"well-being of credit unions generally"* in mind.

The Guidelines for the Drafting of Regulations state, that in drafting regulations regard must be had to, among other things, *"promotion of equality in ... the supply of and access to goods and services"*.

Ireland's equality legislation prohibits discrimination on nine grounds including **family status** and we feel that this regulation offends that guidance and the provisions of the equality legislation. (See Appendix A)

The exemption at (21.2) of € 2,000 total exposure is in any event far too low. If these regulations are to stand then this amount should be upwards of € 10,000 at least.

Section 35 limits

We feel that the existing s35 limits are too restrictive and anticipate difficulties as loan demand increases. We would ask that the new regulations revise the percentages upwards.

We would like to know the reasoning behind changing from the current system of calculating maximum loans (% of total assets) to % of regulatory reserve. We feel very strongly that Credit Union Boards and management are best placed to make decisions on and agree concentration limits within their own credit unions

4. Draft Investments Regulations

We think that Equities should continue to be allowable at the present 5% rate.

The following concentration limits are being introduced for investments in other credit unions and Industrial and Provident societies:

- Investments in the shares in or deposits with other credit unions must not exceed 12.5% of regulatory reserves; and
- Investments in the shares of societies registered under the Industrial and Provident Societies Acts 1893 to 1978 must not exceed of 12.5% of regulatory reserves.

Is this another ploy by the CB to prevent us in the future from investing in our own safe, secure, stable sector? Is this another ploy to get us to prop the Banks that cost the taxpayer billions?

Based on the Central Bank's analysis, less than 1% of credit unions have exposure to either of these investment types. Why on earth are you the Central Bank, introducing a restriction on something that does not affect us now? You are again introducing a restriction that of course is more favourable to the banking sector, in which we can have deposits of up to 100% of our portfolio. Is the Central Bank afraid the day might come that a deposit in a Credit Union will be more attractive and secure than a deposit in one of the pillar Banks?

If it was up to us as a Credit Union we would have a balance sheet with an insignificant investment portfolio, as our business has and always will be loans. However due to the worst recession since the Wall Street Crash of the 1920's which was directly caused by the reckless behaviour of those at the helm of the Banking sector, we are prevented from doing what we know best, i.e. lending. We have no choice but to invest our funds. We have been restricted by the Central Bank, who we can lend to and how much we can lend. We are restricted what institutions we can invest in and how much we can invest in them. Now the C.B. wishes to place further investment restrictions on us.

For us to have 10% of our unattached shares available within 8 days, means our credit union has to have to have approximately €2,250,000.00 lying in an account earning little or nothing. Who will this benefit? Certainly not our members.

We fully support the submission submitted by Davy on the 26th February 2015 and attach it as an appendix to this submission

Along with the ILCU we are in agreement with the application of maturity limits to the Investments portfolio rather than Individual Classes, and with the expansion of Irish and EEA State Securities.

Restriction of Authorised classes:-

It would seem suitable, given the underlying ethos of the credit union movement, that it become involved in social and economic initiatives in the state. The Social Housing Strategy 2020: Support, Supply and Reform, which was approved by government in November of 2014 announced that public investment of the proceeds of the sale of Bord Gais could be used to *“leverage private sector finance which will be raised from a variety of sources which could include EIB, ISIF, Pension Funds, **Credit Unions** and other financial institutions both domestic and international.”*

If credit unions are to play a role in this area additions must be made to the proposed list of authorised investments (Reg25) e.g.

Centralised lending

Social housing

State Guaranteed Projects

Or otherwise as approved by the bank.

Proposed maturity limits

The proposal of a 25 year maximum on loans, but a 10 year maximum on investments is contradictory to the need for cohesive asset liability management.

The proposed 10 year maximum on investments is unlikely to be sufficient for all required investment activities i.e. centralised lending and social housing.

5. Draft Savings Regulations

The Regulatory Impact Assessment refers to c.55% of credit unions being impacted by this new requirement, but that only 0.11% of members and 1.18% of Members savings would exceed the new maximum savings limit.

This implies that the effect of such a regulation would be minimal when we believe it would be catastrophic.

The imposition of this limit by the Central Bank, an institution of the State, would have the effect of saying that member’s money is not safe in Credit Unions because the

limit of €100,000 is equal to the State Guarantee limit of € 100,000 and implies a lack of confidence in the safety of higher deposits.

The members who make up the above statistics are most likely to be the longest standing and most loyal members. They will have stayed with the Credit Union during the boom, when there were more attractive rates available, only to now be asked to withdraw their savings!

The negative reputational impact of such a move would be enormous and would shroud the credit union in uncertainty and insecurity that is unfair and unnecessary. It could easily cause a run on savings which the new regulation would be responsible for.

Our members are entitled to freedom of choice as to where they keep their hard earned savings. Their savings are safe in credit unions and to imply otherwise is grossly unfair and inaccurate.

In the context of increased regulation of credit unions, of Fitness & Probity requirements, the growing number of professionals on Boards and volunteering, it is unfair and unrealistic to impose further restrictions on members by asking them to move funds.

This limit on savings has the potential to limit the competitiveness of credit unions generally and this in contrary to sensible fiscal practice and to the guidelines for Regulatory Impact Analysis (see extract in Appendix A). The Central Bank is again showing support for the banks over credit unions in this regard.

This is contrary to Competition and Consumer Protection legislation.

If these regulations are imposed on us the movement will have no choice but to take a challenge to the Competition Authority and Consumer Protection Commission, and further if necessary up to and including the European Courts.

We would like to know if other financial institutions are subject to a similar limit on deposits?

Individual Member Savings Limit v Total Member Savings Limit

For this credit union in particular there is also the issue of how the requirement not to have deposits greater than 100% of shares affects our credit union in practical terms.

If this is based on individual members we would be restricted to holding only € 40k on each member's behalf, due to our limit of € 20,000 on shares.

If we are forced to increase our maximum shares limit to €50,000, to allow us to hold € 100k on member's behalf it will interfere with our balance sheet and also increase substantially the amount we will have to pay out in year-end dividends on shares.

We would like clarification on this point – is the limit per individual as in the foregoing example, or is it the aggregate of all shares vs all deposits held within our credit union?

We believe that we should not be limited in the amount we hold in savings. This would be in line with how other institutions are treated.

The imposition of a Six month time limit here shows an extraordinary disregard for credit union members. It is disgracefully unrealistic.

6. Draft Borrowing Regulations

This regulation does not pose an immediate problem however it is conceivable that it may be overly restrictive in the future.

We would suggest that this be reviewed within a designated period of time after commencement.

7. Draft regulations on systems, controls and reporting arrangements

Please provide more information on this section:-

What form would the disclosures take?

What would disclosure of the performance of the loan book look like?

Why does the Central Bank want that information in circulation?

- 8. Do you agree with the proposed timelines** for the introduction of the draft regulations set out in this consultation paper, in particular the transition period proposed between the publication and commencement of the regulations? If you have other suggestions please provide them, along with the supporting rationale

We do not agree with the proposed timelines for the introduction of the draft regulations. In particular we strongly oppose the six month time limit in the savings section. If this regulation is put in place, which we do not believe should happen, this time limit is totally unreasonable. If credit unions are to manage this situation without there being a run on savings the very least that will have to happen is to guide and assist members through the

process, allowing them time to reinvest their funds. Even if this is handled expertly it will still have a very negative effect on the movement.

It may in any event be outside of the credit unions control to limit savings and credit unions may find themselves in breach but without the control to remedy that breach (for example, a member may refuse or be unable to withdraw funds).

REVIEW CLAUSE

There are many aspects of these regulations which have an obvious negative outcome for credit unions. There are some aspects which are difficult to predict. In light of the continued uncertainty within the Financial Services system it is imperative that a review clause be included in the final draft of these regulations.

That review clause should state clearly the defined period within which the review shall take place; reporting procedures following the review; consultation processes to be followed and any other necessary conditions to ensure that review and reporting will take place in an effective and timely manner.

SUMMARY/CONCLUSION

Kilmallock Credit Union has taken considerable time to review these draft regulations and we find that there are many worrying aspects to them.

There are unfair restrictions on competition and advantages to other lenders.(Please see Appendix B.) Our members choices are being restricted in a way that interferes with their property rights, financial freedom and independence, and the obvious preference some people have for being part of a larger, community based organisation that has an ethical and altruistic outlook, as opposed to being a cog in the wheels of commercial entities which have behaved in a manner that has directly affected so many people, globally, so negatively.

One of the founding principles of the Credit Union movement is the equal treatment of members. These regulations require us to treat members related to our valued volunteers and management as being a greater risk than all other members, simply by virtue of that relationship. This is illogical and unfair.

The draft regulations go further and attempt to restrict Credit Unions involvement in social projects when that social involvement goes to the very core of the movement.

It is undemocratic to restrict a person's right to deal with their property as they see fit. The only possible justification is where there may be either a risk to the person, so we encourage them to use savings accounts rather than keep funds to hand; or to the greater good, which has certainly not been damaged by Credit Unions.

Generations of Irish people will pay for the damage done to this country by reckless financial institutions. We do not accept that credit unions or their members caused such damage so we reject this attempt to penalise them.

Kilmallock Credit Union Limited.

Appendix A.

Extract from the Guidelines for Drafting Regulations

4.45 The Government is also committed to promoting equality in employment and in the supply of and access to goods and services. Ireland's equality legislation prohibits discrimination on nine grounds: gender, marital status, family status, age, disability, sexual orientation, race, religion and membership of the Traveller community. The scope of the legislation is extensive and covers discrimination in relation to access to employment, advertising job vacancies, conditions of employment, equal pay for work of equal value, promotion opportunities, collective agreements, work experience and vocational training. It also covers discrimination in relation to the supply of and access to goods, facilities and services whether provided by the public or the private sector

The Rights of Citizens

4.57 Assess whether the proposals impinge disproportionately on the rights of citizens.

4.58 In examining such impacts, consideration should be given to the personal rights defined in the Irish Constitution as well as to international agreements to which Ireland is a party. These include United Nations Treaties such as *the Universal Declaration of Human Rights* and Council of Europe Treaties like the *European Convention for the Protection of Human Rights and Fundamental Freedoms*. Examples of such rights are the right to life, liberty and security of person, the right to equal protection before the law, freedom of movement and the right to own property

Appendix B.

Significant Policy Change in an Economic Market/Impact on Consumers and Competition

4.54 The RIA must assess whether the regulatory proposals involve a significant policy change in an economic market. Officials will, in general, be best placed to determine what is a significant change in a particular policy area under their aegis. However, in general terms there are a number of policy changes which are likely to be significant in a particular economic market or sector.

For example, changes to the regulatory framework such as the transfer of power to an Independent Sectoral Regulator, or a significant change to a Regulator's powers and functions, are likely to be significant in their impacts. Other regulations which might fall under this heading include the removal or addition of restrictions on producers in a market, or the liberalisation of the provision of a particular product or service.

4.55 It is also necessary that impacts on consumers and competition be examined under this section of the RIA. Greater competition stimulates innovation and efficiency among businesses; contributes to lower prices of goods and services for consumers; and enhances overall national competitiveness. Regulation can impact on competition in a number of ways. For example, regulations can create barriers to entry such as limiting the number of suppliers in a market e.g. capping the number of licences; it can restrict the supply of certain services e.g. the restriction on the provision of services by persons other than a

particular group.

4.56 In analysing the impact of a regulation on competition and consumer welfare the following questions might be useful:

- Is it introducing higher switching costs for consumers?
 - Will there be restrictions on consumers' choice?
 - Will there be restrictions on firms' choice?
 - Is the regulation likely to restrict entry to the market?
 - Is the regulation likely to alter market structure?
 - Is the regulation likely to increase some firms' market power?
 - Is the regulations likely to reduce the competitive position of small enterprise relative to large?
 - Would set-up costs be higher for new producers?
-
- The socially excluded and vulnerable groups;
 - The environment;
 - Whether there is a significant policy change in an economic market, including consumer and competition impacts;
 - The rights of citizens;
 - Compliance Burdens, including Administrative Burdens;
 - North-South and East-West Relations.