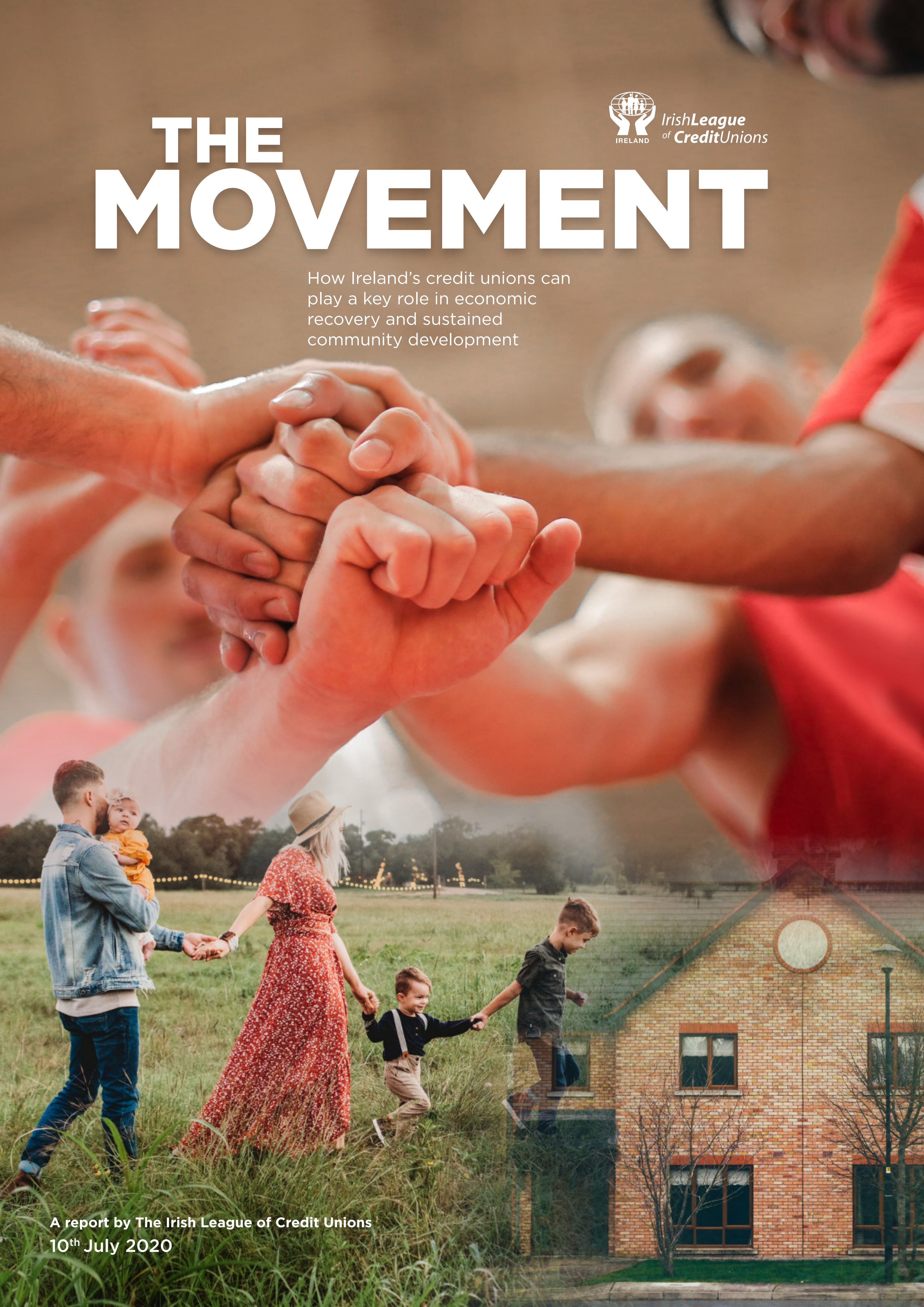

THE MOVEMENT

How Ireland's credit unions can play a key role in economic recovery and sustained community development

Irish League of Credit Unions

A report by The Irish League of Credit Unions

10th July 2020

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FOREWORD

In a time of pandemic and economic downturn, strong community bonds take on renewed importance. The events of the last four months have brought villages, towns, and city neighbourhoods across Ireland closer together, if not physically then in spirit.

In the process, many of us have become more considerate, more neighbourly, and more civically minded. If ever there were a case of a thundercloud having a silver lining, this new positive mentality is it. An engaged and community-focused citizenship is something that we, as a society, and the government, as society's representatives, should encourage and nurture.

It is a sentiment that sits well with the credit union movement; an understanding of what creates community and holds it together is its guiding principle. Credit unions are valued by households and businesses precisely because they are institutions built on a mutual understanding of local people, local needs, and local opportunities. Credit unions are visible, trusted, and viewed as "human" in a financial services market crowded with faceless high-street brands and online apps.

Ireland now faces a battle to recover, and it is precisely the community spirit that has guided us through the pandemic that will also support us through economic recovery.

The ethos of a grassroots, cooperative organisation, owned by members for members, is central to the credit union movement. This ethos, in a post-Covid world, is more relevant than ever. Credit unions are ready to support the communities they are embedded in, as they have always done, but with renewed vigour and sense of purpose.

Ibec estimates that the economy will not recover to pre-Covid-19 levels until at least 2022. While this outlook is nowhere near as dire as our 2008 prognosis, many thousands of Irish businesses will still be forced to close or will at least be severely impacted by nervous and slow-moving international and domestic markets.

There will be a human cost to this, too, much of which will be difficult to quantify. Many thousands of Irish people will be put out of work, which, in turn, will have consequences for local communities, many of which will not have sufficiently recovered from the crash of a decade ago.

Coupled with the increasing possibility of a no-deal Brexit, until only recently relegated to a background act, there is a real danger that some of Ireland's rural and urban communities will be economically disadvantaged for many years to come if they do not have essential access to credit at reasonable rates in the form of loans, mortgages, and other financial supports, which are so important for local communities to prosper.

Indeed, access to credit and investment accelerates economic recovery, and it will be the areas outside our immediate city centres that will need the biggest boost. Credit unions, because of their local knowledge and local relationships, often see opportunity where other mainstream banks do not (or will not). In short, they ensure that these communities are financially backed and have the room to be entrepreneurial, to innovate, and to spend within their local economies

Even before the pandemic, there were already major shifts in credit union members' demands. They still want the personal and reliable savings vehicle that credit unions have provided them with for over six decades, but they also want more. Their needs have changed with their circumstances; they want mortgages, small business loans, and other specialised financial products. While they want these products from their credit unions, which they trust and have strong relationships with, all too often credit unions cannot offer them, often due to the overly restricted environment in which credit unions must operate. This gives traditional banks an unfair competitive advantage and jeopardises the long-term sustainability of the credit union movement.

The financial services sector is heavily regulated for reasons that became abundantly clear in 2008; there is no disputing the need for independent, prudent, and transparent intervention by national and international governments, organisations, and their agencies. Credit unions understand, and are strongly committed to, meeting their regulatory responsibilities and obligations and continue to do so each day.

However, credit unions are increasingly hampered in their desire to do more and become more responsive to their members' needs, despite a changing financial landscape, by the current legislative and regulatory environment.

The lack of progressive policies toward credit unions and the failure of Government to translate their commitments to support credit unions to offer an expanded range of community banking services is one example of the challenges facing credit unions.

These shortcomings and broken promises have the greatest impact on local communities. It deeply limits the growth of local communities, local enterprise, and local families, who might have no alternative sources of finance available to them, either due to infrastructural issues (such as an absence of local bank branches) or relationship issues (such as a failure of those same banks to fully grasp local opportunities).

Faced with an imminent severe economic downturn, now is the time for Ireland's policymakers and regulators to act. Existing legislation must be reviewed and reformed to ensure that credit unions can serve their local communities in the best and most appropriate ways while helping them strengthen their long-term sustainability and development. We welcome the recent commitment in the Programme for Government to do so, however, this commitment must now be acted upon and not become another empty promise.

This report explores the present market situation of credit unions in the Republic of Ireland; the opportunities for growth; the barriers in their way; and the political action and legislative change required to address both. The report also includes a survey of ILCU affiliated credit unions, which asked credit unions CEOs and managers at the coal face what financial products and services their members most need now as Ireland emerges from Covid-19 lockdown, and what are the challenges that credit unions face in meeting the demands of their members.

With a new government in the Republic, there is opportunity for fresh thinking and enhanced ambition on the role that credit unions can play in sustaining Irish communities in the challenging period ahead. A failure to grasp this opportunity will do a disservice to struggling communities across Ireland, especially those who were to the fore in supporting their families, friends, communities, and our country during Covid-19.

While the ILCU is an all-island body with 91 affiliated credit unions in Northern Ireland this report is focused solely on credit unions in the Republic of Ireland. This report sets out the mechanisms by which government and elected representatives can now empower credit unions to help their communities through expanded access to credit and liquidity. We urge policymakers to engage with us in a meaningful way to effect the change that is needed to realise this worthy objective.

Gerry Thompson

Gerry Thompson,
President of the Irish League of Credit Unions

CREDIT UNIONS AT A GLANCE*

*Refers to Irish League of Credit Union affiliated credit unions

ROOTED IN COMMUNITY

317 CREDIT UNIONS across the island of Ireland

3.6 MILLION MEMBERS

1 IN EVERY 2 people living on the island has a credit union account

A LONG TRACK RECORD OF DELIVERY

Over
60 Years
supporting Irish Communities

STRONG, IF UNDERUTILISED, ASSET BOOK

TOTAL ASSET BOOK = €20 BILLION
(€18 billion in ROI and £2 billion in NI)

€15 BILLION IN SAVINGS
(€13.5 billion in ROI and £1.5 billion in NI)

€5 BILLION+ IN LOANS
(€4.46 billion in ROI and £682 million in NI)

FURTHER POTENTIAL FOR CREDIT UNIONS TO SUPPORT COMMUNITIES INCLUDING:

- SME lending
- Home lending
- Social housing
- National Retrofitting Programme
- Green lending and other emerging opportunities

SERVICES MOST IN DEMAND DURING COVID-19

(BASED ON I-REACH SURVEY, JUNE 2020)

1. Rescheduling of loans
2. Banking services to those cocooning
3. Express lodgements

80% believe that rescheduling loan repayments is the measure which can most assist members in the period ahead

PRIORITIES FOR NEXT GOVERNMENT TO SUPPORT CREDIT UNIONS

1. Changes to the capital structures
2. Increased limits for home loans
3. Increased limits for business loans

CHAPTER 1

THE CREDIT UNION MOVEMENT IN IRELAND TODAY

Across Ireland North and South, there are 317 Irish League of Credit Unions (ILCU)-affiliated credit unions, with 226 in the Republic and a further 91 in Northern Ireland. All-Ireland membership now stands at 3.68 million, split between 3.16 million in the Republic and 520,000 in Northern Ireland.

Globally, credit union membership stands at 260 million with more than 89,000 credit unions across 117 countries. Among these countries, Ireland has one of the highest levels of credit union membership anywhere in the world.

One of the most obvious ways in which the credit union movement remains an integral part of Irish life, a key element in the state's financial framework, and an essential part of the communities it serves is demonstrated in the movement's current financial reach.

In the Republic of Ireland alone this includes:

- 226 credit unions*
- 3.16 million members
- €13.55 billion in savings
- €4.46 billion in loans
- €18.01 billion in total assets.

In Northern Ireland:

- 91 credit unions*
- 520,000 members
- £1.36 billion in savings
- £582 million in loans
- £1.942 billion in total assets.

**Those affiliated with the ILCU*

That the level of membership and financial muscle of credit unions in Ireland remains so strong and so prolific is not surprising to those who have been involved with the credit union movement over its long history.

It is a cliché to say that credit unions are different, but they are, and this difference is precisely their strength. It also ensures that they continue to remain a relevant and a much-needed part of our overall financial system in Ireland.

THE CREDIT UNION DIFFERENCE

Credit unions are different to every other financial institution in Ireland:

1 FINANCIAL MODEL BASED ON PEOPLE, NOT PROFITS

Credit unions are not-for-profit democratic financial cooperatives owned by all members. They were created for one reason only – to provide financial services to communities, with every member over 16 having a vote at their local credit union AGM. In addition, any surplus income is used to develop new and existing services, or it is distributed among members in the form of dividends to savers or interest rebates to borrowers.

In recent years, the Central Bank, as Regulator, has justifiably reminded all financial institutions of the importance of putting their customers first, and this has translated into an increased focus on financial conduct and behaviour. Credit unions find this somewhat ironic because they have always had this ethos at their core. Our model, a cooperative one of a local institution run by members for members, means that decisions are always taken by each local board of directors based on prioritising members best interests. This decentralised decision-making ensures greater accountability to all members and puts them at the heart of all strategies pursued by each individual credit union.

2 MEMBERS, NOT CUSTOMERS OR SHAREHOLDERS

Each credit union is an independent, not-for-profit organisation that exists solely for the benefit of its members, not the markets. Credit unions have members, not customers, and membership is open to people who have a unique 'common bond' with other members of the credit union.

This bond can be based on the geographic area the members live in (A Community Bond) or the occupation / employment the members work in (An Industrial Bond).

3. LENDING PRACTICES THAT WORK FOR MEMBERS

There are many aspects to credit unions' approach to lending and providing credit facilities to their members that, although always prudent and responsible, differ from the approach typically taken by banks; they are driven by a desire to work in the most practical way for members.

Credit unions, whether lending for personal or business reasons, have always taken a prudent but personal approach. Credit unions pride themselves on their willingness and ability to take the time to understand each member's credit request, the motivation behind it, and the feasibility of each request relative to each borrower's personal and business circumstances.

Decisions are based on responding to member needs rather than impersonal, one-size-fits-all algorithms, which often do not capture the full situation of each member.

4. THE CUSTOMER EXPERIENCE – MEMBERS' FIRST

Over the last decade, the retreat of the traditional commercial banks from the main streets of our cities and towns has become the norm. A 2018 study found that in the ten years from 2008 to 2018, 160 bank branches had closed[1].

While commercial banks might have benefited from the savings realised from such cost-cutting exercises, customers have not. Credit unions, in contrast, continue to offer a face-to-face member experience.

In addition, credit unions have adapted their service offering in recent years in order to meet the needs of their members. In practice, this has meant the increased availability of modern online services for those who wish to transact in this way while maintaining traditional in-office services for those who prefer this method. In addition, many credit unions also offer Saturday and late opening hours to facilitate the changed working and lifestyle patterns of our members.

That credit unions have members, not customers, and that each credit union is a regulated entity in its own right focused on serving and protecting its members' interests, is a huge differentiator from commercial banks.

Continuing to offer this personal and responsive service is one that our survey evidence has consistently shown is something that the public and members value highly.

Research carried out by independent agencies also validates this view. For the last five consecutive years the CX Company has named the Credit Union the number one organisation in Ireland that offers the best customer experience[2].

The Credit Union was also named as the most reputable organisation in the country by the Ireland RepTrak 2020 Study. This is on the back of coming second in 2019 behind Bord Bia, having topped the poll the previous year. Credit unions also came out of this survey as the most reputable financial organisations in Ireland overall, more than 20 points higher than the average for other financial institutions.

In an era when many make easy assumptions about consumers' preference for online, faceless and impersonal interactions, the Credit Union experience consistently shows that this is not necessarily the case, and that there remains a strong cohort of the Irish public that continues to seek and value a more personal customer experience. There is no singular member preference on how they wish to transact, and credit unions recognise this fact and strive to facilitate all member preferences

Credit unions in the Republic currently have €4.46 billion in loans to members, but as will be outlined further in this report, the movement believes that there is much greater potential to extend its lending portfolio to a broader spectrum of the Irish market, including the mortgage and SME sectors.

5. IMPORTANCE OF VOLUNTEER-LED CREDIT UNION BOARDS

The directors who make up the boards of credit unions are all volunteers, typically individuals drawn from local communities with financial and other expertise who wish to contribute to the work of their local credit union.

That they are derived from the community in which credit unions are located is also significant to the operation of credit unions.

[1]https://www.irishtimes.com/business/financial-services/number-of-european-bank-branches-down-by-21-over-last-ten-years-1.3625712
[2]While the Award refers to customers in reality it in fact recognises our high level of service to the members who comprise each credit union.

They understand and are attuned to the needs of members within that community, respond to those needs, and place a high value on being accountable and transparent to members.

Due to the embedded local nature of credit unions and the boards who drive their development, credit unions are often a focal point of communities, not just by circulating and recirculating local money in the local economy but also through supporting and promoting local initiatives and businesses, or by giving back to their communities through socially beneficial activities, or procuring goods and services from local businesses as required.

In February 2019, the Credit Union Advisory Committee, established by the Minister of Finance to advise him/her on issues relevant to the credit union movement, published research that looked at the role of directors on the boards of credit unions in greater detail[3].

Key findings from the report included:

- The importance of credit unions to marginalised sections of our communities. The report notes that "without credit unions, and the work of their volunteer directors, it is undeniable that many people would be disenfranchised or be at risk of financial exclusion".
- In addition to safeguarding their members' interests, directors are also upholding the ethos of the movement, an ethos that is unique and markedly different to other financial institutions.
- Credit union board directors are largely representative of their communities, distinct from commercial banks and other financial institutions. The age profile of directors is also not unduly weighted towards an older age group, with good gender balance comparable to other financial organisations; the profile includes directors who are well educated and a large proportion of directors who have been recruited relatively recently.

6. EMBEDDED IN COMMUNITY AND RESPONSIVE TO THEIR NEEDS

Credit unions have been at the centre of local and workplace communities for over 60 years, tailoring their products and services to match their members' needs. Over that period, we have served generations of families and communities, helping them grow and prosper. The trust and esteem in which these members hold their local credit unions is reflected in the fact that these members continue to avail of our products and services from savings for key life events, such as saving for education and college fees, to personal and small business loans. This inter-generational relationship between credit unions and their members highlights both the grassroots and wide appeal of the movement in Ireland.

With 226 credit unions in the Republic and a further 91 in Northern Ireland, the movement now has an unrivalled reach into communities. At a time when many traditional commercial banks are in retreat, with branch closures and reduced opening hours, credit unions have continued to serve communities in both urban and rural areas and are working extremely hard to retain their presence in each and every community. This is despite a challenging cost environment.

7. CREDIT UNION DIFFERENCE IN ACTION

CASE STUDY ONE:
SUPPORTING FAMILIES

A Cork-based family with three children built their own home with their own finances derived from many years of savings. However, their savings ran out when their new home was 75% completed. The family had no borrowings or pre-existing mortgage and sought a loan from commercial banks to complete their home. Both parents were working fulltime. Banks turned down their loan application, despite their home, even at 75% completion, being valued at €200,000.

The Credit Union reviewed their financial position and approved a home improvement loan sufficient to allow them to complete their build and move into their home. Today the family continues to meet their repayments and remain valued and active members of their local credit union.

[3] A report on research into credit union directors, the Credit Union Advisory Committee, February 2020.

CASE STUDY TWO:
SUPPORTING LOCAL BUSINESS

A young man wanted to start a plant hire operations business. The credit union supported him in buying his first digger. He has continued to borrow from the credit union to expand his business. The credit union continues to support this entrepreneur in achieving his business objectives and reaching financial targets.

CASE STUDY THREE:
SUPPORTING FARMERS

With the value of Irish agri-food exports worth over €13 billion in 2019, farmers are more than just the backbone of rural communities—they are a central part of the wider Irish economy. The ability of farmers to expand their services, innovate, and continue to produce a high-quality food product is essential to this export success story.

Like all businesses, access to credit and liquidity is a key concern for farmers. The credit union recognised that our farming members required a bespoke lending product that acknowledges their distinct needs and their differences from other forms of businesses.

This has led to the establishment of Cultivate, a unique lending solution, tailored for farmers. Cultivate is an initiative of a group of credit unions that provides short-to medium-term loan opportunities built specifically around the growing needs of farming members. Typical members are a mix of dairy, beef, and sheep farmers accessing farm loans between €5,000 and €50,000.

While this particular scheme is a relatively new and bespoke initiative, more broadly all credit unions provide financial supports to the farming community as part of their service offering to this sector.

CREDIT UNIONS IN A TIME OF COVID-19

The outbreak of Covid-19 and the subsequent restrictions on business and community life has presented challenges for the credit union movement.

However, these challenges have been largely overcome, not least because of the credit unions' flexibility and ability to quickly adapt to the new circumstances presented by Covid-19.

Credit unions have continued to serve their members throughout the pandemic while abiding by national restrictions. Their focus throughout has been to continue to work in a way that best works for members.

In practice, this has meant that our offices have remained open throughout the crisis; telephone consultations have increased; and other measures have been introduced to ensure continuity for members. However, there have been substantial additional costs for credit unions and personal sacrifices made by frontline credit union employees in facilitating these supports.

This 'member-first' approach is closely aligned to the community and member-based structure of the movement. A consequence of this is that credit unions have had a better understanding of the needs of our members during this period and, equally, what will be required as the easing of lockdown accelerates.

Again, this approach contrasts with the decision by most commercial banks to close significant numbers of their branches across Irish towns and communities during Covid-19. For example, Bank of Ireland closed 101 branches during the pandemic; there remains an ongoing doubt as to whether all these branches will reopen[4].

This decision to close commercial banks has negatively impacted communities in different ways. Such as communities with either no or poor broadband, those that are geographically distant from the nearest open commercial bank branch, or who have significant numbers of elderly people who might not be as technologically or internet savvy as younger generations.

[4]https://www.thejournal.ie/bank-of-ireland-branches-shut-coronavirus-5054604-Mar2020/

These factors have further underlined the importance placed by the credit union movement in ensuring continuity of service for members.

The accessibility of credit unions and their ability to continue to provide services to members and communities has brought huge value to many communities during the pandemic.

This manifested itself through agile and responsive solutions championed by credit unions during Covid-19, such as increased telephone consultations, expanded online services, tailored and flexible opening hours, express lodgement facilities, and bespoke offerings for 'cocooning' members. The focus throughout has been to ensure that credit unions provide multiple means for members to financially transact in ways that work best for them.

It is also notable that member behaviour has modified during Covid-19, with electronic fund transfers (EFT) transactions increasing during recent months with our movement-owned payments company (CUSOP) experiencing substantial growth in various electronic payments volumes over the period.

The restrictions on movement during the lockdown phase has also shone a light on the importance of maintaining banking and financial services at the most accessible levels to communities across Ireland.

A demand for local services that ultimately promote the development of the communities we live and work in is something that will strengthen, rather than weaken, post-Covid. Credit unions in Ireland can fulfil and expand this role in the period ahead, with the support of government and policymakers.

CREDIT UNIONS AT A CROSSROADS: UNLOCKING POTENTIAL VS. MISSED OPPORTUNITY

CHAPTER 2

The Irish credit union movement is now at a pivotal point in its history. How credit unions develop over the years ahead will determine their viability and longer-term existence.

It is now reasonable and fair to ask the following questions:

1. Is there a continuing need for credit unions as part of the Irish financial services landscape?
2. Do credit unions currently, and can they continue to, provide an important role in this landscape?
3. If so, and particularly for response by our national decision-makers and leaders—government, policymakers, and elected representatives—are they committed to a future for credit unions in Ireland?

The credit union movement in Ireland, and more importantly the 3.6 million members who avail of our services every day across the island, are clear in their view that the answer to each of these questions is a resounding 'yes'.

Yet this response is, by itself, not enough to ensure the future of credit unions. What matters just as much is whether this view of the importance of credit unions is shared by other key stakeholders, such as those outlined above.

A larger, arguably more pointed question is whether there is a willingness among government, elected representatives, and the Regulator to allow some credit unions to decline and ultimately fail.

If not, are key national decision-makers equally committed to securing the future of the movement and to working with credit unions who want to create a sustainable future for credit unions? And what steps do they need to take to underpin this objective?

An important and often overlooked part of the credit union movement is the wider social value which it provides. Credit unions are not commercial banks, nor do they wish to be.

As noted in the previous chapter, the basis on which they are founded and operate is different and unique relative to commercial banks. Yet, from a regulatory perspective, credit unions continue to be pushed in the direction of the industry norms for commercial banking.

The latter are built on a globalised financial platform of multi-national institutions where the overriding consideration is increasing financial returns for shareholders. This position jars with the raison d'etre of credit unions, which are effectively local co-operatives driven to support members and develop the local communities from which these members come.

Equally, credit unions do not wish to continue in existence merely for the sake of it; rather, they believe that the ideals that drove the creation of the movement over 60 years ago—providing financial inclusion and services to people through a financial co-operative they own and democratically control— remain as valid now as they did then.

However, credit unions are acutely aware that the way they do business cannot stay unchanged. Like all aspects of life, they wish to adapt to the changes that are transforming society, particularly those resulting from the far-reaching impact of technology on daily life. Equally, the financial needs of both households and businesses have changed hugely and become ever more sophisticated and nuanced over recent decades.

Credit unions themselves know they are not immune to these changes and recognise the need to adjust to remain relevant and best meet the requirements of their members. But improvements require ongoing investment by credit unions and scarce resources must be prudently deployed.

There are essentially two scenarios facing the movement in the years ahead, one positive and the other negative. The first, the positive, is unlocking the full potential of credit unions by empowering them to increase their footprint in the Irish financial services market through increased services and products. The second, the negative, is continued restrictions on their ability to meet the sophisticated and evolving needs of their members and wider communities, thereby leading to a gradual and sustained decline.

If the latter is the case, not only will the future of credit unions be at risk, but there will be a huge missed opportunity for communities, businesses, and Ireland's economy to capitalise on the distinct offering and beneficial difference that credit unions are uniquely positioned to provide.

If as a society we support the first positive view of the need to fully unlock the potential of credit unions, several challenges must first be overcome. These are explored below.

CHALLENGES FACING CREDIT UNIONS

1. ADDRESSING THE ISSUE OF UNDER-LENDING BY CREDIT UNIONS

At the most basic level, credit unions currently engage in an extremely low level of lending. This situation developed due to a number of factors including changing lending habits. However, it is equally fair to say that the regulatory environment itself, for many years, also restricted the ability of credit unions to adapt to meet lending demands.

For example, until early 2020 credit unions were largely confined to lending only for short to medium term periods, with the majority (70%) under five years and this effectively not only locked them out of the mortgage market, but it also reduced their attractiveness as lender of choice for other loan products.

Some changes approved by the Regulator, and which took effect in January of this year, allow for longer term lending, such as facilitating a measure of expanded mortgage and business lending, but, with the outbreak of Covid-19 in the interim, it means that it is too early to fully assess the impact of these measures.

More broadly, these low levels of lending form part of a longer-term trend of a declining loans-to-assets ratio, with the gap continuing to widen over the last 20 years. Falling levels of lending across the movement contrast sharply with the increasing overall asset base, currently at €18 billion (ROI).

The loans-to-assets ratios across credit unions in the Republic of Ireland now stands at 26% (a fall of 35%) from a high point of over 61% in 2001. The knock-on effect of this decreasing ratio has resulted in credit unions' gross income declining over the period, while business costs, particularly regulatory-related costs, have continued to increase.

The current financial model of credit unions continues to be based primarily around its members savings, with deposits now standing at almost €14 billion in the Republic. This has led to credit unions often being characterised and viewed as savings unions. While savings are strong and have continued to grow, in contrast credit union lending is much weaker and remains largely confined to unsecured short- to medium-term credit.

Yet the success of this financial model is now what threatens to undermine the very viability of credit unions – savings growth. It is one that many wish to reimagine, not least as it threatens the movement's long-term future.

Lack of loan book diversification

Even within the restricted lending that credit unions undertake currently, there is also an extreme lack of diversification in the Credit Union's loan books.

Almost 95% of the current loan book is based on short-term personal loans, with an average loan value of just over €7,000 per member.

This places credit unions in the Republic of Ireland at odds with credit unions in comparable countries, such as the Canada or US, where diversification is the norm and viewed as essential, and has been a feature of their loan books for many years.

As noted above, in January new Central Bank regulations were introduced. These followed many years of proposals by the credit union movement to allow credit unions to offer a broader and increased level of longer-term lending, including home/mortgage and business lending.

However, as pointed out by the ILCU to the Central Bank and others prior to the introduction of these new regulations, these changes to lending practices are relatively limited in scope and will have little impact on the issue of under-lending in credit unions. This is particularly the case for larger and progressive credit unions that want to offer a more diverse portfolio of financial services to their members, including expanded mortgage and SME lending. In the period ahead, the latter are likely to quickly reach their maximum lending limits and be constrained in growing their loan books any further.

As will be outlined below the ‘perfect storm’ of increasing savings coupled with falling lending is driving down loans-to assets ratios which are in turn forcing credit unions to introduce reduced savings caps thereby making credit unions less attractive and also creating a situation whereby some credit unions are now unable to serve their members needs by being no longer able to take their savings, once their savings are above the caps.

As credit unions incrementally move to grow their lending offering, a more proactive response from Government policymakers in cooperation with the credit union movement itself is needed to ensure that the assets of the credit unions can be used in a more effective way for the benefit of members and communities. Currently these remain underutilised and are serving the interests of neither members nor the Irish economy.

Credit union loan diversification – the international experience

While Irish credit unions are only now beginning to diversify their loan books, this is something that credit unions in United States have been doing for many decades.

Credit unions in the United States offer a full range of banking services, including car loans, mortgages, current accounts, and debit and credit cards, in addition to generating alternative fee income through insurance, investments, and other financial products.

Despite this diversification, they have retained their structure and guiding principle as member-owned co-operatives working for the benefit of their members and communities. A similar evolution has occurred in the Australian credit union movement.

The point to note is that loan book diversification has not diluted the community-based philosophy or guiding principles of the movement in the United States, so it is possible to expand lending offerings while maintaining community roots and a not-for-profit ethos.

Significant impact on members

The current levels of capital reserves (see below for more detail) that must be held by credit unions have direct and negative impacts on ordinary credit union members. The biggest manifestation of this are the caps on the amount of money that ordinary members can save with credit unions. This situation has been exacerbated during the Covid-19 pandemic as the level of lending has fallen and consumers have increased their savings due to financial and economic uncertainty.

However, the impact of savings caps on credit union members is that members with deposits in excess of these savings caps are now effectively being turned away by credit unions who cannot exceed these saving limits, lest they breach the Regulators onerous capital requirement.

For example, one of the largest credit unions in the country, the Health Services Staffs Credit Union (HSSCU) informed members in May that they have been forced to introduce a savings cap of €40,000. This means that once a member reaches this saving limit, they cannot deposit any more savings into their credit union account.

In the case of another large credit union in South Dublin, it too recently announced a similar cap on deposits of €40,000 per member, with further reductions also likely.

While the figure of €40,000 may seem high at first, in circumstances where the membership of this credit union includes 47% retirees, the monies they save with their credit union may constitute their lifelong retirement savings.

Research undertaken by The Irish Times in 2019 found a further 36 credit unions across Ireland had introduced similar savings caps on members[5]. In the current environment of Covid-19-linked higher savings, reduced appetite for consumer loans, and increased regulatory costs, this trend is increasing.

In the period ahead it is likely that for many more credit unions their savings cap could fall as low as €15,000 to €25,000.

In effect, this would mean credit unions could not hold its’ members savings for relatively modest amounts such as purchase price of new

[5]Credit unions impose savings caps on deposit accounts, Irish Times, 13 June 2019.

Nissan Micra, savings for a couple's wedding or a deposit to purchase a home. Members are again the losers and are faced with a situation whereby their credit union can no longer meet their financial needs.

Limited home lending

Credit unions in the Republic currently engage in a very limited amount of home and mortgage lending. This is the case for a number of reasons, such as historical regulatory limitations on the duration/term of loans credit unions could offer, thereby preventing credit unions from engaging in mortgage lending; restrictions on the overall share of credit union lending which could be mortgage related; and, the administrative and cost burdens associated with providing mortgage products.

This is now beginning to slowly change. As noted throughout this report, there is a growing appetite amongst many, particularly larger, credit unions, to offer mortgages to members. However, for those who do wish to either commence mortgage lending or to expand the volume of mortgages they lend to members, there remains significant regulatory barriers to doing so.

In November 2019, following a stakeholder consultation, the Central Bank announced regulatory reforms cited to facilitate a measure of expanded mortgage lending.

For most credit unions these 'reforms' will not significantly change the position in respect of mortgage lending to members or remove the regulatory barriers they face if they wish to grow their loan book in this area.

These new Central Bank regulations took effect in early 2020, however they are limited in scope, allowing the full credit union network across the Republic to issue a limited number of mortgages per annum.

Not only does it continue to restrict credit union mortgage lending in the immediate term, but it also ensures that any longer-term, more ambitious pathway for credit unions to win a greater share of the mortgage market over the years ahead remains unfeasible.

After almost 6 months since the change in regulations, mortgages currently represent just over 3% of the total credit union loan book in the Republic, highlighting the relatively small dent it has made to date in credit union loan books or wider mortgage market.

Some of the reasons for this are set below.

The existing 10% capital reserve requirements means that any credit union currently close to or even a couple of percentage points above this reserving level, such as at 12-14%, is at risk of falling below it if they increase the number of mortgages they lend – even if a relatively modest number of new mortgages.

Linked to the latter is the fact that the costs associated with mortgage lending - including enhanced staffing resources and expertise and legal costs - do not ensure a sufficient margin for credit unions to grow their mortgage book.

Of those credit unions who have considered investing in bringing mortgage products to market, the fact that once they achieve even a modest growth in mortgages, they are then at risk of falling below capital reserving levels, is a substantial deterrent. This is even more so the case, as credit union deposits have increased further in recent months putting reserving levels under even greater strain.

Once credit unions are at or close to the current 10% reserving level, they are then forced to introduce further savings caps on members to come back within the reserving requirements. This knee-jerk response is not conducive to long-term financial planning and product development, undermines the credibility of credit unions amongst members and acts as a strong disincentive to participate in either any or additional mortgage lending.

A further consideration is the fact that the new Central Bank rules are very prescriptive and conservative in the overall levels of mortgage and commercial lending which they permit. The regulations set ceilings of 7.5% of total assets for a single credit union to advance home and business loans, rising to 10% and 15% for credit unions that hold assets of at least €50m and €100m. These ceilings do not enable credit unions to fully develop diversified loan portfolios at the required scale.

Credit unions, while they can attest to a strong demand amongst members for a mortgage lending product, are also keen to ensure that they do not create an inflated demand amongst their members for home lending which they ultimately cannot meet due to the regulatory restrictions outlined above.

While it has long been argued by government and financial commentators that increased competition in the mortgage market in Ireland would be hugely beneficial for Irish consumers, the current regulations do little to position credit unions to compete in this market.

With a membership base of over 3 million across the Republic of Ireland, many of whom are potential home buyers, credit unions are ideally positioned to serve this member base but remain unable to meet members' financial needs in this area.

Imagine, for example, a member who has built up their savings and has a strong credit history with their local credit union. The credit union understands their financial circumstances and their ability to meet their financial obligations better than most. However, regulation means that that member, even though they may want to access a home loan from their credit union, cannot. Instead, they will have to go elsewhere and/or to a financial institution less attuned to their needs and track record.

The ILCU recognises these barriers to mortgage lending and has already developed and launched a full-service mortgage solution, which individual credit unions can avail of. As a result, mortgage applications are now being processed via this service in a small but growing number of credit unions, with support from a centralised Mortgage Hub operated by the ILCU.

However, overall, the most effective mechanism to allow credit unions more actively engage in mortgage lending and at greater volumes would be a reduction in current capital reserving requirements from 10% to 8%.

This solution would provide credit unions with greater leeway to grow their mortgage book in a number of ways.

It would give credit unions the headroom to financially provision for an expanded volume of mortgages; enable credit unions to invest in building their inhouse mortgage lending expertise as required; and, allow credit unions to incrementally grow their mortgage books without a continuous risk of falling below the current 10% capital. The latter continues to stifle both the ability and confidence amongst credit unions to engage in expanded mortgage lending.

SME lending

As with mortgage lending, the ability of credit unions to lend to businesses, particularly SMEs and micro-businesses, situated within their local communities is also currently very restricted, notwithstanding the strong asset base of many credit unions.

SMEs and micro-businesses are the backbone of the Irish economy, representing 99% of active enterprise in Ireland and accounting for more than one million employees (65% of the total workforce).

A report undertaken last year by the Seanad on SME businesses in Ireland[6] found that many small businesses, particularly those in the regions that struggle to access credit, do not even apply to commercial banks because they expect their applications will be rejected. Lack of access to relationship managers in commercial banks, in addition to high interest rates for SMEs (the second highest in the eurozone), were also cited by small businesses as a barrier to securing credit.

The knock-on effect is that often viable small businesses, which have the potential for further growth and job creation opportunities, are constrained in their ability to expand their businesses.

While this was the position before Covid-19, SME difficulties in securing access to credit is now even more important as our economy emerges from the pandemic and is seeking to get businesses back trading. Credit unions with significant assets can have a central part to play in financially supporting small, local businesses during this period. However, their ability to do so remains constrained by the existing regulatory limitations, such as the existing capital reserve requirement of 10%.

The restrictions which inhibit mortgage lending equally apply to increased commercial/business lending.

[6] Seanad Public Consultation on Small and Medium Sized Businesses Report 2019

These include that:

- The current requirement that credit unions must hold a minimum of 10% capital reserves means that many credit unions are faced with an ongoing challenge of bolstering their reserves to maintain this reserving level. This means that credit unions often do not have the capacity to also invest in developing mortgage products;
- The current regulatory ceilings of 7.5% of total assets for a single credit union for mortgage and business lending combined, or 10% to 15% for credit unions with assets of at least €50 m and €100 m, are inadequate to allow for meaningful commercial lending; and
- The additional costs, in areas such as staffing and underwriting expertise and administration costs, which would have to be incurred by credit unions to scale up their business lending, would not generate sufficient margin to justify relatively small increases in commercial lending.

Again, as per mortgage lending, a reduction in current capital reserves requirements to 8% would create headroom and generate increased opportunities for credit unions to increase their lending to small businesses.

Another factor limiting expanded business lending by credit unions is the regulatory restrictions on credit unions offering asset finance. Asset finance products such as leasing finance, PCPs or hire purchase finance were not included as part of the new Central Bank regulations on lending from earlier this year.

Asset finance has grown significantly in recent years as a means for businesses to access short term or working capital loans, with commercial banks and other financial institutions offering this credit facility.

Asset based finance is also particularly attractive to businesses due to the fact that it invites a lower rate of interest as a result of being secured on the back of the asset it is lent against. The restriction on credit unions participating in this market sector places credit unions at a disadvantage relative to other financial institutions in Ireland and makes them less attractive to businesses when choosing a lender.

Credit union ambitions to expand their lending portfolios

Credit unions acknowledge that they also have some responsibility for the significant fall in loans-to-assets ratios, which has occurred over a prolonged period. In the past, credit unions did not always proactively develop the lending side of their businesses as they might have done. This occurred for myriad of reasons, such as a lack of lending expertise in some offices, the administrative burden associated with particular lending products, or other structural barriers that impeded the development of particular types of lending products and services.

However, many credit unions are now working to put in place solutions to address these issues, with an increasing number of individual credit unions now offering more sophisticated products in areas such as home lending or small business loans. There remains much work to be done.

However, the perspective of credit unions on the issue of lending is clear. They want to be able to offer their members a fuller service, which not only meets their day-to-day current banking needs and their saving requirements, but also provides a more diverse range of credit facilities beyond short, unsecured loans to longer-term, secured lending for homes and businesses.

This is the development path that many credit unions are now on, but the regulatory and policy environment must also synchronise with and support this ambition rather than hinder it.

Department of Finance support for community banking

A 2018 Department of Finance report[7] examining the merits of establishing a local public banking system in Ireland based on the German Sparkassen model recommended against the State doing so.

Germany's Sparkassen are regional and community savings banks where a state or other public actor has an ownership stake in a bank or financial institution. They are a substantial force in the overall German financial

[7]Local Public Banking in Ireland: An analysis of a model for developing a system of local public banking in Ireland, 2018, Department of Finance and Department of Community and Rural Development.

system. In opting against pursuing the model in Ireland, the costs of administering such a system was a significant consideration in the Department's decision.

However, so too was the existence of the well-developed credit union network across Ireland, which either already provides much of the proposed services of Germany's Sparkassen, particularly in retail credit, and/or has ambitions to expand their services further in other areas such as increased SME lending akin to the German model.

The report did recommend that existing credit unions be empowered to diversify their loans books and expand their capacity to lend to local businesses. Rather than building a new financial structure from the ground up and the associated costs for the state in doing so, it was recognised that the credit union movement and its network can fulfil such a function.

Despite this endorsement by the Department of Finance for a greater role for credit unions in business lending, it has not yet translated into significant legislative change to facilitate it.

However, it is of note that in recent days the Programme for Government has committed to enable "the credit union movement to grow as a key provider of community banking in the country". ILCU welcomes this commitment but now wants to see the new Government translate it into proactive policy change to realise this objective.

Social housing

There is an unprecedented shortage of housing, particularly social housing. The ability of the credit union movement to financially support and extend credit to increase the stock of social housing across Ireland is something that has been long advocated by a wide range of stakeholders, including government departments and elected representatives.

However, despite such endorsements, as set out below, this role for credit unions in financing much needed social housing remains unimplemented.

A role for credit unions in financing social housing – a timeline of inaction

- **November 2014** - The government published the Social Housing Strategy 2020, which aims to deliver 35,000 social housing units over the six years to 2020. In addition to the public monies that would fund this strategy, it was also predicated on "private sector finance which will be raised from a variety of sources which could include the EIB, ISIF, pension funds, credit unions, and other financial institutions, both domestic and international".
- **October 2015** - In response to that specific request, the Irish League of Credit Unions responded with its detailed proposal 'Social Housing Funding', which set out a roadmap for the role that credit unions could play in the delivery of such funding.
- **June 2016** - The Oireachtas Special Committee on Housing and Homelessness examining the housing crisis, as a priority recommendation stated: "The Government should seek to mobilise as quickly as possible, all possible sources of funding, including funding from the Housing Finance Agency, Strategic Investment Fund, the Irish League of Credit Unions, and Irish Pension Funds, to increase the supply of social and affordable housing."
- **July 2016** - The Department of Housing, Community and Local Government policy document Rebuilding Ireland stated: "The Government is also committed to a range of other structural, funding and policy supports to increase delivery by AHBs [Approved Housing Bodies]. Among these measures will be the establishment of an Innovation Fund to support the development by AHBs of innovative financial models... Support will be provided from this Fund to an Irish Council for Social Housing (ICSH)/ sector-led new special purpose vehicle, involving investors, including the Credit Union movement".
- **October 2017** - The Joint Committee on Finance, Public Expenditure and Reform and the Taoiseach published their report on the review of the credit union sector. The report stated that the credit union movement should be empowered to

contribute to alleviating the housing crisis in the state and the current regulations are not adequate to this imperative.

- **February 2018** - Following sector engagement with the Central Bank in relation to proposals for credit unions to provide funding to AHBs for the provision of social housing, the Central Bank announced, having taken account of the feedback from respondents, that it is appropriate for credit unions to be permitted to provide funding for social housing through investments in AHBs, subject to certain requirements and limits.
- **June 2020** - To date there has been no delivery on the recommendation to leverage credit union funds to support the development of increased social housing. Indeed, in recent parliamentary question responses by relevant ministers, there has been increasingly insistent pushback on any responsibility for delivery at all. Successive commitments for delivery in Q3 2018 and Q1 2019 have not been met. Currently there is no timeline or outcome in view.

This policy issue is not simply one for credit unions. It is inextricably linked to the national imperative of bringing AHBs back off the government balance sheet before the available headroom for funding meets the downward pressure of fiscal limits. Credit unions are not a single fix to that multi-faceted problem, but our finance is a sustainable pillar of a separate source of funding for the future.

As noted throughout this paper, the full potential and capacity of credit unions to contribute to the development of their communities continues to be ignored by policymakers due to the latter's failure to enact the policy and legislative changes needed to tap into the existing strong asset base of credit unions.

Credit unions, with the correct mechanism to unlock the alternative sources of credit they provide (specifically through the establishment of a state-regulated investment vehicle), could make a real difference in ensuring that more families can access affordable housing within their communities.

What is required now from the new Government is delivery on its' commitment to allow for credit union funds to be invested in social housing.

National Retrofitting Programme

The Programme for Government committed the next government to develop and roll out a national programme of retrofitting up to 500,000 homes by 2030. We welcome this initiative. As a financial institution rooted in the community, we believe that credit unions are uniquely placed to support lending to members to enable them to participate in this national programme.

The government has also committed to working with both credit unions and An Post to develop a mechanism to do this to support access to finance for retrofitting. We would urge the Department of Finance, the Strategic Banking Corporation of Ireland (SBCI) and other relevant stakeholders to move quickly to begin a process of consultation and engagement with credit unions representatives to work together to unlock credit union funding streams.

2. ENSURING PROPORTIONATE AND RESPONSIBLE CAPITAL RESERVES

The capital requirements/reserves required to be held by credit unions under regulatory law in the Republic of Ireland are acting as barrier to credit unions' sustainability and development.

The regulatory requirements stipulate that a credit union must reserve 10% of its overall capital from its total funds. This requirement differs from commercial banks in several ways:

- Reserving requirements by commercial banks are based on a risk-weighted approach, unlike credit unions.
- The risk-weighted approach can lead to a lower level of reserving required of commercial banks when compared to how credit unions are currently assessed.

The 'one-size-fits-all' 10% reserving requirement that credit unions are obliged to meet is not fit for purpose, as it fails to take account of the variance in risk that each individual credit union holds at any given time. It can lead to perverse results; a credit union with a higher risk profile is not required to hold a higher level of reserves as you might expect and, equally, a credit union with a lower risk profile does not enjoy a lower reserving requirement.

In addition, currently up to 70% of the assets on credit union balance sheets are classified as non-risky, a fact that provides justification for a lower regulatory reserve to reflect this low level of risk.

However, a more significant point is that a lower rate of reserving for credit unions would give credit unions more “breathing room” and flexibility regarding capital requirements during this unprecedented crisis. This would also allow credit unions to use such flexibility to fund the development of their own services and products to meet member needs.

The Central Bank has traditionally countered that credit unions should not benefit from the risk-weighted model enjoyed by commercial banks due to the fact that credit unions do not provide the complexity of services and investment and lending products offered by commercial banks.

In recent weeks the Central Bank has again stated: “We believe there is no rationale to change to a risk-weighted approach given the current asset mix of Irish credit unions, the nature of the business model, and the costs associated with implementation for credit unions.”

This, they argue, makes a flat (and high) catch-all percentage reserve rate more appropriate. This view is not shared by credit unions.

This argument is circular and does not serve a constructive purpose.

On the one hand, credit unions are advised by many stakeholders, such as Government-established expert groups, and they themselves want to, to offer more sophisticated financial products and services to their members to meet the latter’s changing needs.

On the other hand, when credit union seek to do so, part of which requires having a reserving requirement more in line with international norms for credit unions and to provide them with an enhanced capacity to further develop an expanded offering of products and services, credit unions are told by the Regulator it is not appropriate. This view keeps credit unions in a bind that impedes their future development and long-term sustainability.

The Central Bank has also made the point that credit unions themselves need to develop more robust business plans to facilitate increased lending. This is feedback that credit unions accept, and many credit unions are now moving towards developing such plans.

However, as noted, the more important impact of a lower rate of reserving for credit unions is creating “breathing room” and greater flexibility for credit unions at this time, whilst allowing credit unions to fund the further development of their services and products.

For its part, the ILCU Strategic Plan 2020-2025 includes targets for the development of new products and services for credit unions to enable them to expand the range of services they can offer to their members.

The Central Bank has also made the point that the average level of existing capital reserves across credit unions in Ireland stands at 16%, and that this serves as evidence that there is no necessity to reduce the current minimum reserving levels further.

However, this figure represents an average across the movement in Ireland and does not account for credit unions who are currently operating on or close to the minimum level of 10% and, as a result, are restricted from expanding their lending offering at this time. This is stifling their ability to grow and develop further.

As credit unions face growing operating costs, additional Covid-19 related loan impairments, and increased levels of savings by members, a reduced but proportionate level of capital reserves will allow credit unions to meet challenges and members needs in a sustainable way.

As outlined above, the unwillingness of the Central Bank to countenance a reduction in capital reserve levels as a means to allow credit unions to respond to current challenges contrasts with the approach adopted in respect of commercial banks in recent months, and with the response of peer regulatory authorities internationally.

In March in response to Covid-19, the Central Bank decided to release a capital buffer that domestic commercial banks are required to hold in order to support the continued provision of credit to households and businesses. This buffer, known as the Counter Cyclical Capital Buffer (CCyB), was reduced from 1% to 0% with effect from 2 April 2020.

This unlocked an additional €1 billion for commercial banks to lend to or support struggling customers during the pandemic period. In effect, it has facilitated the 'payment holiday' for a period of up to six months that banks have offered to households and businesses unable to meet their repayment commitments at this time.

While credit unions are not required to hold the CCyB that commercial banks must, the high capital reserve requirement of 10% functions as a comparable safety net for credit unions and the protection of their members funds.

Yet despite the flexibility adopted by the Central Bank toward commercial banks, justifiable in light of the current extraordinary economic fallout from Covid-19, the Central Bank continues to refuse to countenance a reduction in capital reserves for credit unions.

Credit unions' capital reserves, although distinct from the CCyB, if reduced by a prudent 2% would, as noted above, allow credit unions to create greater resources to further develop expanded products and services to support their members.

The Central Bank needs to reconsider its position on this issue. As part of the 2019 Peer Review Report, an independent review of the Central Bank's performance of its regulatory supervisory role in respect of Irish credit unions, it was recommended that additional stress-testing on regulatory reserves under the existing leverage ratio and risk-weighted reserve approach be undertaken.

This work would expand our understanding on the merits of moving to a risk weighted model and must now be undertaken with immediate effect.

3. INTERNATIONAL CAPITAL RESERVING FOR CREDIT UNIONS - HOW IRELAND COMPARES

As we have outlined throughout this report, credit unions continue to be a central part of the financial structure of communities across Ireland.

However, what is also clear is that credit unions are increasingly concerned about their long-term sustainability. Unless there are policy changes in areas such as capital reserves, allowing for expanded services and greater loan book diversification, and proportionate regulatory costs are addressed, then their viability will continue to be in question.

Ireland's credit unions, when viewed as part of a much larger global movement, are not the first country to face such challenges. Indeed, many of the issues that credit unions face in Ireland have also been issues in Great Britain, Northern Ireland, and the United States at various points in recent decades.

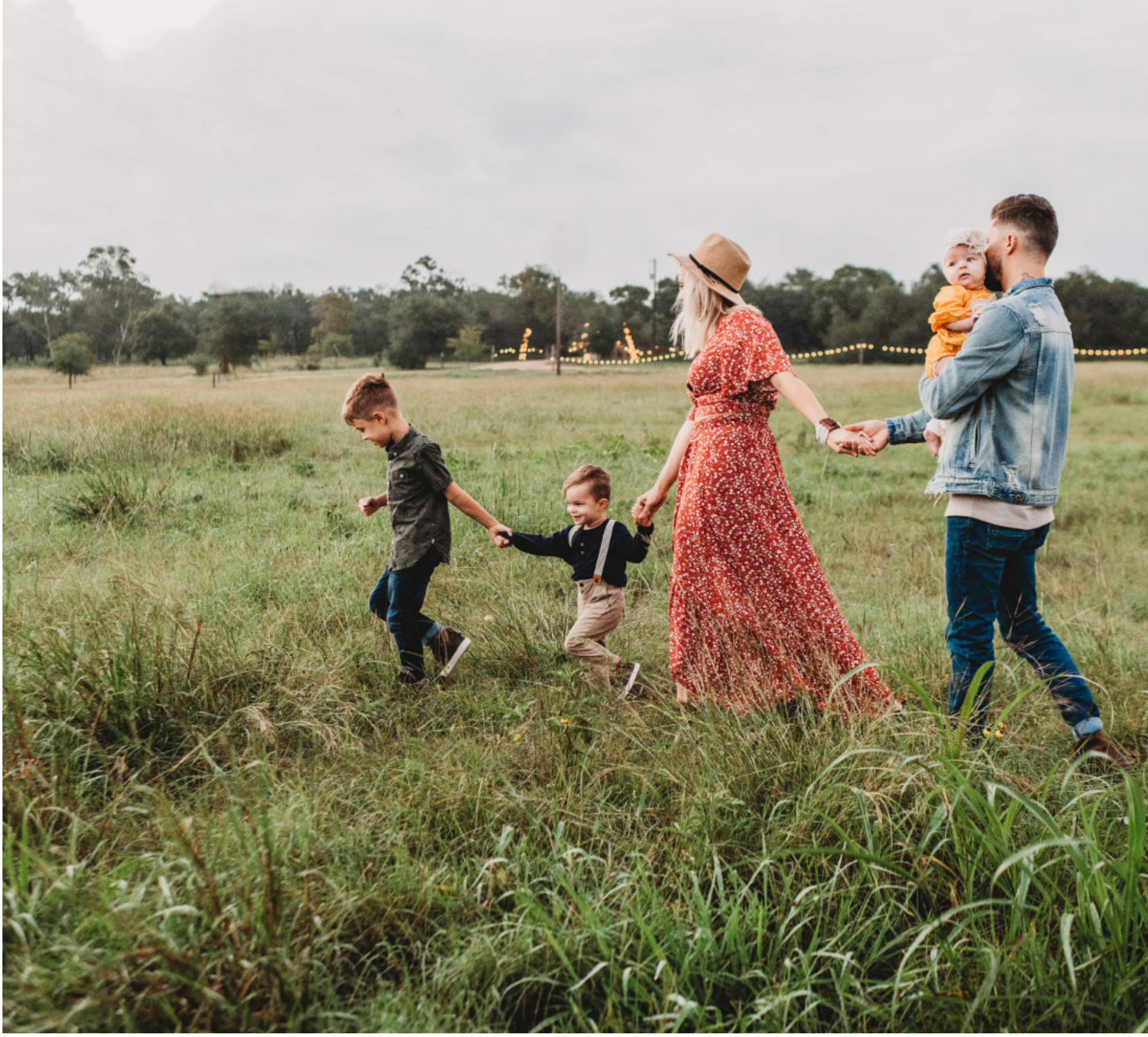
While we acknowledge that the financial provisions which pertain to each jurisdiction will not be identical, they are broadly comparable issues which can be examined further, including:

Capital reserving requirements for credit unions in Ireland are higher than with those in other countries where the 'norm' tends to be 8%.

The chart below sets out the levels of capital reserve requirements in jurisdictions comparable to the Republic of Ireland.

COUNTRY	MINIMUM CAPITAL RESERVE REQUIREMENT	MODEL
Germany	8%	Risk weighted
New Zealand	8-10%	Risk weighted
France	8%	Risk weighted
United States	8-10%	Risk weighted
Australia	8%	Risk weighted
Poland	5%	Risk weighted

The current flat rate of 10% in the Republic of Ireland is forcing many credit unions to introduce savings caps on members as a means to stay with the existing reserving levels. This is not conducive to long-term planning or robust business modelling.



It is also worth remembering that prior to 2009, the reserving requirement for Irish credit unions was 8%. This is the level Irish credit unions wish to see reinstated pending the introduction of a weighted reserve model like that of other jurisdictions.

It is notable that in the UK and Northern Ireland the Regulator there recently completed a consultation process which examined capital reserving requirements and what were appropriate levels given the circumstances of credit unions. It has proposed a tiered approach to capital reserves with smaller credit unions with the lowest levels of risk requiring a much lower rating of (3%) and credit unions with higher levels of risk having a higher reserving requirement. This proposal recognises the risks differences between credit unions and proposes an approach which moves away from a one-size-fits-all approach with a flat rate, as currently pertains in the Republic of Ireland.

ENSURING REASONABLE REGULATORY COSTS

CHAPTER 3

Since the downturn and collapse of the commercial banking system during the 2008 recession, increased regulation of financial services was an essential and necessary response.

While the bailout of commercial banks during this period has ultimately cost the State and taxpayers over €64 billion, it is notable that credit unions remained robust and viable during the recession.

Initial reports that credit unions would require a State bailout of €1 billion were unfounded and did not materialise. In the end, only a very small number of credit unions (six in total) failed during the downturn and required financial assistance from the State.

Notwithstanding this strong track record pointing to a healthy governance structure, our movement fully supports the need for robust regulation of all institutions offering financial services in Ireland, including credit unions.

However, all regulation must be evidence-based and proportionate. Critically, regulation cannot act as a stranglehold on a credit union's ability to meet the needs of its members and the wider communities it serves.

In addition to the administrative and regulatory burden, which has increased hugely for our voluntary-led credit union movement, the issue of regulatory levies and their cost is also of significant concern to credit unions across Ireland.

Levies and charges have generally risen as the credit union sector has grown and income has fallen. Each of these charges are an expense in the credit union's accounts. There are now four different types of levies that credit unions must now contribute to every year, which currently amount to €22 million per annum. See breakdown of regulatory levies below:

LEVY	CURRENT ANNUAL LEVY COST
Deposit Guarantee Scheme	€13.4 million
Credit Institutions Resolution Fund Levy	€4.4 million
Stabilisation Fund Levy	€2.7 million
Industry Fund Levy	€1.5 million
Total	€22 million

In addition to these existing high charges, it is intended that the extent of the burden of levies faced by credit unions will increase further in the period ahead. The Central Bank has ministerial approval to increase the Industry Funding Levy five-fold by 2022. This one levy currently costs our affiliated credit unions approximately €1.5 million per annum, and the proposed increase would increase that to approximately €7.8 million by the end of the cycle in 2022.

This cost burden comes at a time when credit unions are facing increasing competitive pressure from both commercial banks and new fintech start-ups, such as Revolut and N26. Both banks (increasingly) and fintechs tend to be digitally focused and do not provide the personal service offered by credit unions; they are also not subject to the same overhead costs.

The more personal, community-based alternative to the commercial and digital banking that credit unions provide, though in demand, comes at a higher cost and must be borne at a time when credit unions are also seeking to expand the range of services they provide to members. Greater acknowledgement of these pressures must be considered by government and policymakers when determining the level of regulatory levies to be borne by credit unions.

As outlined previously, during the Covid-19 pandemic credit unions have prioritised their pivotal role in local communities in Ireland, ensuring that members can continue to access our services in the most convenient way.

This has included keeping offices open, particularly in towns where commercial banks have opted to close their branches, and in seeking to provide flexible finance arrangements to members during the crisis. Doing so has meant that credit unions have incurred considerable costs in the wider national interest.

Raising the levy to cover regulatory costs, particularly at this time, is not in the best interests of credit union members, the sustainability of the movement, or the need to provide extra supports for members as Ireland emerges from the Covid-19 crisis. It is a tax on

social capital and a levy on volunteers, whose objective is to financially assist communities at the most accessible levels through self-help.

Reviewing both the costs of regulation and the basis for these costs is very appropriate at this time. Consideration must also be given to the fact that the current approach to regulation undertaken by the Central Bank is based on the position of credit unions at the time of the last economic downturn. However, since that time, the risk management procedures and structures operated by credit unions have substantially transformed and have been hugely enhanced.

This significant improvement in credit unions' risk management processes is something which the CBI Peer Report of January 2020 equally recognises, noting that "in its future reviews the Central Bank may wish to develop further its approach to include a differentiation between credit unions operating an inherently low risk, basic savings and loan model and those with more complex, riskier business models".

In the short term, credit unions urgently need greater flexibility from government on regulatory costs in acknowledgement of these additional efforts and their associated costs during Covid-19.

CENTRAL CREDIT REGISTER FEES

A further issue which must be looked at, particularly in terms of fairness and proportionately, is the current Central Credit Register (CCR) fees.

The Register is essentially a database on loans held by financial institutions within the State. Lenders are required to submit personal and credit information on all existing loans valued for €500 or more and also similar information on loan applications for €2,000 or more.

The objective is to create and maintain an accurate and up-to-date credit report for each borrower.

When a financial institution, including a credit union, receives a loan application of €2,000 and above it must review the credit report held by the CCR which pertains to the applicant.

The Register currently charges a flat, universal charge of €3.50 per applicant for each enquiry. However, the cost of each enquiry is not weighted or tiered in relation to the value of each loan application.

For example, it means that €3.50 is charged for a small €2,000 credit union loan and equally €3.50 for a €400,000 commercial bank mortgage.

In practice, it means that the charge places a disproportionate heavy burden on credit unions, who by their nature issue a significant amount of smaller loans than would be the case for commercial banks. (Currently, many credit unions lending polices also stipulates that they order a credit report on all loans over €500, adding further to the costs).

This charge places a further burden on volunteer-led, not-for-profit credit unions, whose smaller loans are often for the benefit of more marginalised or vulnerable people.

We urge the Regulator to examine this charge, with a view to making it more proportionate to the amount of the loan and taking into consideration the unique position of credit unions and their community and voluntary ethos.

WHAT CREDIT UNIONS WANT -
CREDIT UNIONS DURING COVID-19
AND INTO THE FUTURE

CHAPTER 4

That the credit union movement supports change and wants to actively expand its products and services for its members is something which has been echoed by both management and staff across the country for many years now. Many credit unions are actively working to drive this change.

Equally, like so many other sectors during Covid-19, the pandemic necessitated a change in the operations for many credit unions offices or accelerated the pace of change already underway. Management and staff across the country are to be commended for way in which they have quickly adapted to these new circumstances and the new working practices which they have required.

As the movement now looks to the post-Covid-19 landscape the desire to maintain this momentum for change persists, with many credit unions now beginning to focus on what their members and their wider communities will need from them in the period ahead.

To bring greater clarity and insight to the issues outlined above, the ILCU commissioned independent research company, i-Reach, to undertake a piece of research which specifically asked credit union CEOs and managers about their experiences during Covid-19; their views on where credit unions can add the greatest value to members as Ireland looks to recover; and, what are the current barriers, if any, to meeting members' needs at this time.

Keys research findings are set out in full below.

A. CREDIT UNIONS DURING COVID-19

- **Customer engagement during Covid-19:**

  Of the services provided to credit union members during Covid-19, online and telephone banking, at 72% and 59% respectively, had the greatest levels of engagement by members.

- **Services most in demand during Covid-19:**

  The rescheduling of loans, the provision of bespoke banking services by credit unions to those cocooning and express lodgements were top three most in demand services by members during Covid-19. Connacht, on a regional basis, was the region with the highest level of rescheduling of loans requested.

- **Payment holidays during Covid-19:**

  More than six in ten of all credit unions (62%) who responded are providing payment holidays to members during Covid-19, with Connacht being the region where this service is most provided by credit union offices, with 82% of respondents offering such payment holidays.

- **Biggest internal challenges for credit unions during Covid-19:**

  Respondents (55%) stated maintaining social distance for employees was the biggest internal challenge during Covid-19, followed by setting up staff into separate teams at 53%, and maintaining physical distancing for members at 48%.

B. POST-COVID-19 CREDIT UNION SUPPORTS FOR MEMBERS – THE NEXT 12-18 MONTHS

- **Measures which credit unions believe can most support members in the period ahead:**

  80% of those surveyed believe that rescheduling loan repayments is the measure which can most assist members in the period ahead, followed by community supports and back to business loans at 46% and 43% respectively.

  However, in Munster and Connacht there was also strong support for working capital loans for members at 51% and 48% respectively.

- **Biggest challenges facing credit unions post-Covid-19:**

  Respondents believe that the top three challenges facing credit unions in the period ahead are as follows:

  - a lack of appetite amongst members to borrow at 74%,
  - operating costs including regulatory levies at 68%, and
  - a decline in income leading to viability issues for credit unions at 61%.

- **Expanded credit union services:**

  87% of respondents overall believe that credit unions have the capacity to expand their products and services to members, if permitted to do so. In Dublin, the figure is even higher with 94% of respondents believing this to be the case.

- **Priorities for next Government to safeguard the long-term development and sustainability of credit unions:**

  Credit unions managers when asked what the next Government must prioritise to support the credit union movement argued the following were of greatest importance:

  - changes to the capital reserving structure at 87%;
  - increased limits for home loans (mortgages) at 32%; and
  - increased limits for business loans at 30%.

The response to this question is sending a clear message to Government by credit union management. The existing reserving requirements are now acting as a significant barrier for many credit unions who wish to expand their lending into areas such as mortgages or commercial lending but cannot do so currently. It also suggests that if this reserving requirement were reduced from 10% to 8% that an appetite exists amongst credit unions CEOs and managers to expand their lending in these areas.

(The i-Reach survey ran from the 11th to the 23rd of June, with 226 Credit Union CEOs and Managers invited to take part. 133 (59%) completed the survey).

CHAPTER 5

POLITICAL ACTION AND POLICY RECOMMENDATIONS

There is currently a disconnect between the Oireachtas and the Department of Finance on one side, which together have responsibility for credit unions policy and legislation, and the Registrar of Credit Unions, sitting within the Central Bank, which has responsibility for regulation and the rules which govern how credit unions are permitted to operate.

A view has been allowed to take root that regulation and policy formulation for the long-term development and sustainability of the credit union movement is one in the same thing.

This is not the case.

The Central Bank is tasked with activating and implementing the appropriate regulation required of credit unions, but our government and elected representatives must legislate for the vision and direction of the movement overall.

Credit unions are hugely supportive of the need for independent, proportionate, and transparent regulations from the Central Bank; however, our elected representatives must take the lead in formulating and shepherding through the legislative changes needed to support and develop credit unions. This is not currently happening to a sufficient degree.

What is now needed is a more active and progressive approach by government and elected representatives in framing and supporting a legislative framework for credit unions that allows the movement to develop in a way that builds upon its strengths to date, maintains its ethos and character, ensures it continues to be relevant to members financial needs, and future-proofs the credit union's unique offering.

Over the last decade, while there has been much discussion and deliberation on the credit union movement, it has translated into minimal policy changes, very few of which are sufficiently forward-thinking to allow credit unions to develop in the manner many credit unions now wish to do.

The two core pieces of primary legislation that currently pertain to credit unions are Acts that date from 1997 and 2012[8]. However, these are increasingly outdated relative to the fast-changing pace of financial services in Ireland and globally.

There is now an urgent need for a review of this legislation and the development of a new consolidated act that can maintain and uphold the necessary regulatory environment, and also empower the Minister for Finance and other elected representatives to work with credit unions to develop and implement a long-term and sustainable development framework for the movement which can sustain it in the decades ahead.

This legislation must be underpinned by the need to unlock the full potential and opportunity for credit unions in the delivery of an increased range of community banking services and facilities that meet member needs.

In addition, there are also a select number of immediate measures which must be introduced by our new Government to support credit unions in the short term and allow them to make a significant contribution to Ireland's post-Covid-19 recovery phase. If Government now moves quickly to implement these immediate credit union proposals, in addition to supporting the movement at this time, they will also act to build a foundation for the longer-term ambition of credit unions to become a fully developed community bank for communities across Ireland.

OUR EIGHT KEY REFORM PRIORITIES

Both the immediate and longer-term reforms now needed and our recommendations for how these can be addressed are set out below.

IMMEDIATE REFORM PRIORITIES

Reform One: Amending capital reserve requirements to allow credit unions better support members

Recommendation: An immediate reduction in the reserving requirement of credit unions to 8%, from the current 10%, as an interim measure, pending the full introduction of a risk-weighted reserving requirement.

[8]Credit Union Act 1997 and Co-operation with Overseas Regulation Act 2012

This would give credit unions more "breathing room" and flexibility regarding capital requirements during this unprecedented crisis. This would also allow credit unions to allow provisioning to expand lending and access enhanced resources to fund the development of their own services and products to meet member needs, including in critical areas such as mortgage and commercial lending.

The Central Bank has previously committed to conduct additional stress-testing on regulatory reserves under the existing leverage ratio and risk-weighted reserve approach. This assessment must be undertaken immediately as a starting point to support this transition to a risk-weighted reserve approach.

Reform Two: Ensuring proportionate and responsible regulatory levies

Recommendation: Regulatory cost relief measures must be introduced for all credit unions at this time, specifically a suspension of all levy charges for a period of 12 months. We also call for further commitment from the Minister for Finance to fully review all levies faced by credit unions before the expiry of this 12-month period.

Reform Three: Support credit unions in achieving a higher level of loan-to-assets ratio to safeguard their future

Recommendation: The current low level of loans-to-assets ratio must increase to ensure the long-term survival of credit unions. A 40-50% ratio range would be more appropriate. Politicians and policymakers must work with credit unions to create the policy environment and structures to allow this ratio to be achieved.

Credit unions are constantly working to achieve this objective, but we need a policy framework which supports it. The Government, as set out in further detail below, can facilitate expanded opportunities for credit unions to increase their lending over the longer term and this will do most to achieve these higher ratios.

In the interim, the Government and policymakers must work with credit unions to foster greater confidence and certainty amongst credit unions that their development and long-term future is actively supported and encouraged by Government and elected representatives alike.

This approach must include a proactive initiative by Government which is focused on restoring credit union loan-to-asset ratios to more robust and healthy levels.

A longer-term vision for the credit union movement – empowering credit unions to become a full community banking network

Reform Four: A new legislative and policy framework for credit unions

Recommendation: We welcome the recent commitment contained in the Programme for Government to "review the policy framework within which credit unions operate".

Given the need for increased liquidity for communities as we emerge from the Covid-19 pandemic, such a review must be prioritised by the incoming government. It must include a rapid review of the existing credit union legislation and result in new primary legislation (a new Credit Union Act) to support the growth and development of the movement as a national asset.

Reform Five: Expanding the capacity of credit unions to offer mortgages/home lending

Recommendation: Legislate for a more ambitious, future proofed vision of mortgage lending for credit unions in the years ahead, one which is supported by Government and policymakers. This should include a change to the current regulatory position to allow credit unions to operate a centralised investment model, which would allow credit unions to pool their resources together to develop community bank mortgages open to all members (who meet lending criteria).

The latter would allow home loans to make up 20-25% of the total credit union loan book (particularly in the case of larger credit unions), thereby offering a more feasible and member-friendly solution for credit unions who wish to expand their mortgage lending significantly.

This would still be considerably below the extent to which home loans make up the total loan books of commercial Irish banks, such as AIB, where they represent 55%; Bank of Ireland, where they represent 58%; and PTSB, where they represent 75% (figures as of end 2019).

As noted above, a reduction in capital reserving requirements would also support this objective.

Reform Six: Empowering credit unions to participate more fully in SME lending

Recommendation: Credit unions want to be able to grow further their lending to SMEs, which is currently a small part of their overall lending portfolio. However, in order to do so further legislative changes are necessary ensure that such sectoral lending is feasible and can build incrementally on growth already achieved.

Like mortgages, the ILCUs believe that the best way to foster increased SME lending by credit unions is to legislate for centralised investment model shared amongst credit unions.

This would allow all credit unions who wish to participate in such lending be enabled to do so. This proposal to pool resources amongst credit unions also fits with the concept of a credit union-led, developed community banking model for the Republic of Ireland.

Reform Seven: Allowing credit union funds to support the building of increased social housing.

Recommendation: Establish a state-regulated investment vehicle that would create a mechanism by which credit unions could invest in social housing. This would allow the credit union sector to invest up to €900 million in the provision of social housing and fund close to 6,500 new homes.

Existing regulation allows for the creation of collective investment vehicles for credit unions to invest in social housing development through Approved Housing Bodies, which are now to the fore in delivering social housing in Ireland.

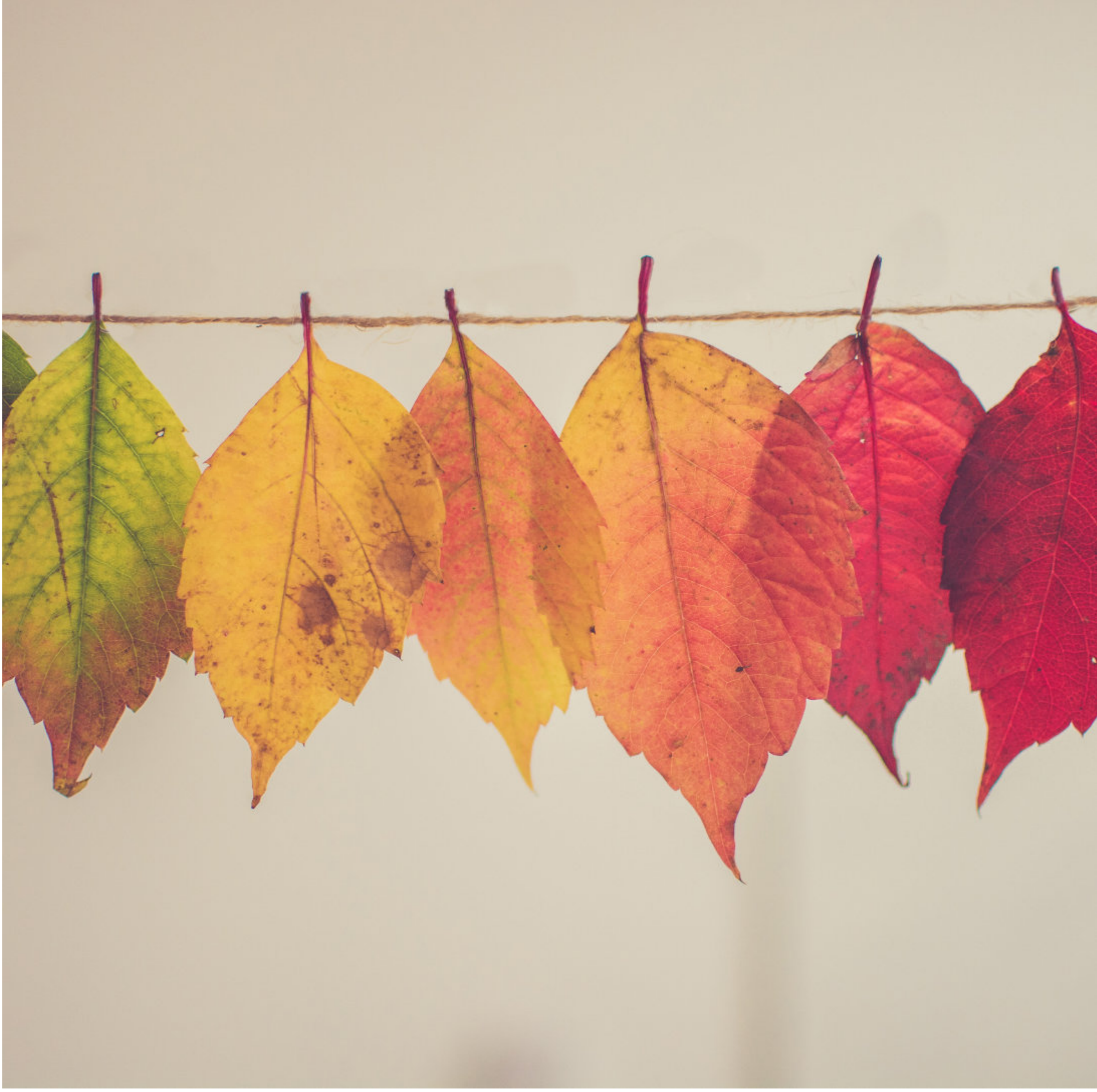
However, this is currently not underpinned by legislation. To date, government has failed to establish the necessary structures to do so. This must now be addressed by the incoming government.

Reform Eight: Credit unions to the fore in supporting a National Retrofitting Programme

The government has committed to an ambitious plan of retrofitting 500,000 homes by 2030 at an estimated cost of €5 billion. Credit unions are well positioned to support this programme by leveraging their assets to provide funding to financially support this programme.

Recommendation: The government and Department of Finance must now work with credit unions to develop a mechanism to do this, such as through a partnership with the Strategic Banking Corporation of Ireland to support access to finance for retrofitting.

This mechanism could also be expanded into the future to support other green lending initiatives.



ACKNOWLEDGING THE WORK THAT CREDIT UNIONS MUST ALSO UNDERTAKE

While the reform proposals outlined above are specifically demanding action of our government, elected representatives, and policymakers, the ILCU and its affiliate credit unions fully recognise the need for a stronger partnership approach between credit unions and state actors.

We equally recognise that while our ask of government and elected representatives is to create the policy environment that allows credit unions to develop and flourish, the movement itself must also undertake a significant programme of change and modernisation to underpin its long-term future.

We have already started this journey, with much work yet to be completed. A key part of this work is the development a strategic long-term plan for the credit union sector and our recently launched Strategic Plan 2020-2025 includes targets for the development of new products and services for credit unions to enable them to expand the range of services they can offer to their members.

CONCLUSION

CHAPTER 6

This report sets out the significant contribution that the credit union movement has made over the past six decades, in financially supporting and underpinning communities on the island. It is a contribution that persists today.

Equally, the movement and its members want to see this work continue and to be maintained for a new generation of families and businesses across Ireland. Now more than ever, as communities grapple with the re-opening of our economy and restoring our small businesses to the financial strength they enjoyed pre-Covid-19, the support of their local credit union will be pivotal.

The ILCU has also highlighted in this report the need and desire for change in the movement to ensure that credit unions remain relevant and can meet the needs of our members.

We have outlined many of the challenges now faced by credit unions across a range of key areas. They are not insurmountable.

The ILCU believes that by working collaboratively with credit unions, government, and elected representatives, policymakers, and the Regulator, these challenges can be addressed, and solutions implemented which will support our members, their communities and Ireland's overall economic recovery.

Greater cooperation between all three—credit unions, government, and the Central Bank—is the only way the long-term future of credit unions can now be secured and their potential to support communities across Ireland in the decades ahead fully guaranteed.

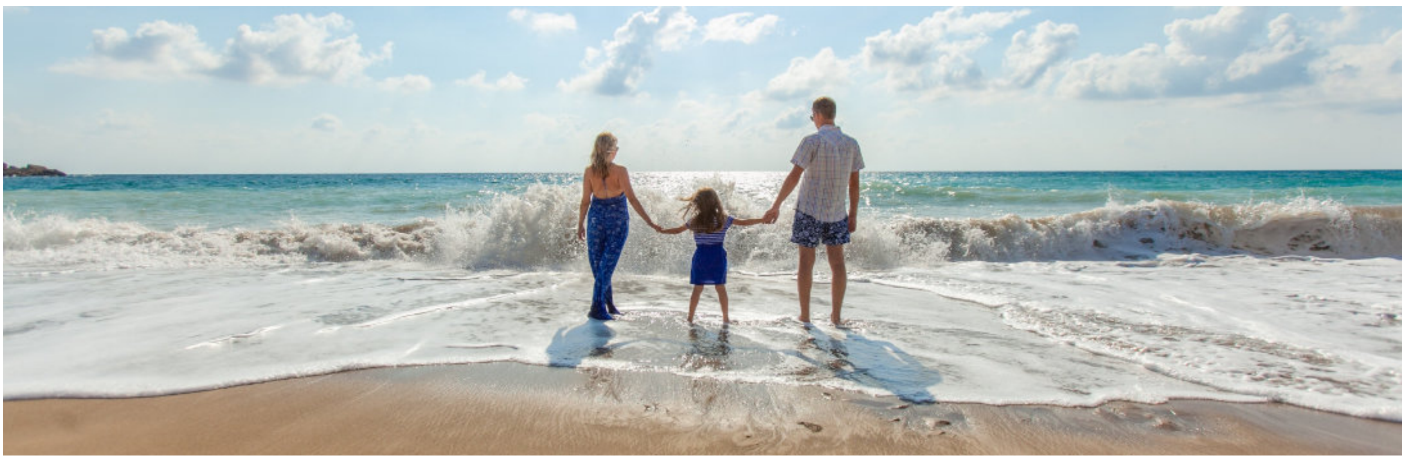
We are calling on these stakeholders to work with our movement to ensure that the recommendations outlined in this report are now prioritised and implemented. The 3.1 million members across the 26 counties who rely on their local credit union, and particularly now, equally want to see that the movement which has supported them for many decades continue to do so.

With a new government comes new momentum, a willingness for change, and a renewed sense of purpose to deliver for communities across the island.

Equally, as Ireland emerges from an unprecedented period and substantial economic challenges now arise, is it essential that the recommendations we have outlined are no longer side-lined.

It makes no sense not to draw on and leverage the significant assets of credit unions at this point of great economic challenges. Drawing on these assets, and at this time, will allow credit unions to support the families and businesses in our communities, that they engage with and who they often understand better than most.

Our eight key asks of government as set out clearly above, are the means to achieve them. We look forward to engaging with all relevant stakeholders, in the best interests of our millions of members and their wider communities, to advance these policy priorities in the weeks and months ahead.



ABOUT THE IRISH LEAGUE OF CREDIT UNIONS

The Irish League of Credit Unions (ILCU) is the largest credit union representative body on the island of Ireland. Founded in 1960 with the aim of providing representation, leadership, co-operation, support, and development for credit unions in both Northern Ireland and the Republic of Ireland, the ILCU today has an affiliated membership of 317 credit unions: 226 in the Republic and 91 in the North. Membership of the ILCU is open to every credit union in Ireland.

The credit union movement is built on an ethos of mutuality, volunteerism, self-help, and not-for-profit philosophy. The ILCU, as an advocate of this ethos, has a vision to influence, inspire, and support the credit union movement to achieve all its goals—social, economic, and cultural—while always respecting the individual's rights and dignity.

In short, the activities of the ILCU include promoting the credit union idea and ethos; lobbying central government on behalf of affiliated credit unions; maintaining a professional working relationship with the regulatory bodies—the Central Bank of Ireland, the Prudential Regulatory Authority (PRA) in Northern Ireland, and the Financial Conduct Authority (FCA)—regarding credit union regulation and compliance, and providing a range of professional services to credit unions.

The services that the ILCU provides to credit unions can be largely grouped into four key areas:

- Trade & representation association
- Business support services
- Monitoring and stabilisation activities; and
- Shared services.

Every two years at the ILCU Annual General Meeting, affiliated credit unions elect the Officers for the Board of Directors of the ILCU. Working through the CEO and the senior management team, the board responds to the needs of the affiliated credit unions during their term of office.

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