

**FINANCIAL SERVICES LEGISLATION
SUBMISSION ON CONSOLIDATION AND SIMPLIFICATION**

Credit Union Development Association (CUDA)

INTRODUCTION

The Credit Union Development Association welcomes the opportunity to make a submission to Government on the 'Consolidation and Simplification Bill' for financial services legislation. We believe the proposed legislation is timely given the Central Bank and Financial Services Authority of Ireland Acts 2003 and 2004 and the formation of a single regulatory authority for the financial services industry.

CUDA was incorporated in 2002 and represents twenty credit unions countrywide with aggregate membership of over three hundred and fifty thousand and €1.75 billion in assets – approaching 20% of the Credit Union Movement in the Republic of Ireland. CUDA credit unions are both large and small, urban and rural, community-based and employment-based. CUDA is the only legally incorporated representative association for credit unions in the State.

Credit unions have been in Ireland since 1958. All credit unions are independent and autonomous of one another. They are financial co-operatives that operate on a not-for-profit basis and are managed by voluntary boards of directors elected from among their shareholders, called members. Every member has the dual role of customer and owner, with a single vote regardless of shareholding (i.e. savings with the credit union). Credit unions offer a unique range of core products and services, some at no direct cost to members. They offer services to all socio-economic groups in the local community and have enviable service satisfaction levels.

Initially credit unions were governed by the Industrial and Provident Societies Acts until the Credit Union Act 1966, which was the first standalone piece of legislation. This Act gave statutory authority to the Registrar of Friendly Societies to regulate credit unions. Since 1 May 2003, credit unions have been regulated by the Registrar of Credit Unions, an independent statutory position within IFSRA, reporting directly to

the Chief Executive. Day-to-day activities are governed by the Credit Union Act 1997, which superseded the 1966 Act, and rules registered with IFSRA.

CUDA regards an independent statutory controlled and operated system of regulation as a necessary precondition for the effective differentiation and sustainable development of the Credit Union Movement in Ireland and the safeguarding of the interests of more than two million members. In this context CUDA argued for the regulation of credit unions to be brought under IFSRA's remit via the creation of a properly funded and dedicated credit union regulatory unit headed by the Registrar of Credit Unions. The boards of the credit unions represented by CUDA regard a suitably differentiated system of statutory regulation as posing no threat for credit unions.

COMMENTS

A. Cross-sectoral or modified sectoral approach ?

Credit unions are unique in terms of their corporate structure, governance and operation. Credit Unions are not banks or credit institutions. To date, this has been accepted by the EU and National Governments. It is reflected in legislation and how credit unions are regulated. This does not mean that the regulatory regime is any less onerous or effective. In many respects there are far tighter restrictions and limitations on credit unions than applied to other financial services providers.

Although there are clear arguments for consolidation and simplification of provisions common to all sectors, CUDA suggests an examination of credit union legislation / structures will reveal that there are few parallels with other sectors in terms of registration, membership, operation and management of credit unions.

CUDA believes credit unions should be omitted from a cross-sectoral approach and from a modified sectoral approach except in so far as provisions relating to the appointment of an administrator or examiner or other matters that may be

common to other sectors. The case for a sectoral approach to credit unions has already been accepted by the Department of Finance and IFSRA. A generic 'one size fits all' approach to the financial services marketplace would not be appropriate for credit unions.

IFSRA's Strategy for 2005 has the high level goal of "*Developing an appropriate regulatory system for credit unions*" through, among other things, "*having a properly differentiated supervisory approach*". This will be achieved by the Registrar of Credit Unions and a dedicated regulatory unit applying legislation, rules and operating principles specific to the Credit Union Movement.

B. Burden of regulation

As stated in the introduction CUDA views the inclusion of Credit Unions under IFSRA's remit in a positive light not least because it serves to underpin one of the key elements of the Movement's competitiveness – reputation.

However Credit unions are extremely diverse in terms of their size and range of activities. This diversity is not currently reflected in Credit Union Act or the regulatory environment. The burden of regulation can be great for small and large credit unions for different reasons. In the case of small credit unions with limited resources, it represents an increasing administrative burden, while in the case of larger credit unions with appropriate expertise, capabilities and resources, it is restricting their ability to grow and compete. In both instances, there may be little risk to the financial stability of the credit union and / or consumer protection issues.

Credit unions are regulated at a micro rather than macro level. For example, credit unions' fields of membership are restricted. There are limits on the amounts an individual member can hold on deposit, withdraw, his/her shareholding and borrowings. There are maximum limits on the interest charged on loans and the percentage of the loan book that can be loaned

beyond five years and ten years. Most importantly, for competition and product innovation, credit unions are not free to introduce new services without the approval of their shareholders and the regulator.

In addition to a Board of Directors, credit unions are obliged to elect or appoint a number of statutory committees and officers to assist the Board with the management of the credit union. These positions are numerous, in many cases voluntary, time-consuming and becoming increasingly difficult to fill.

CUDA credit unions see the 1997 Act as being restrictive in that it appears to take a lowest common denominator approach to the regulation of credit unions. Breaches of the Act constitute offences that can result in fines and/or imprisonment. All of the legislative provisions and more are contained in a set of registered operating rules that bind credit unions and all of their members. The 'Rules' based approach of the Act can be overly prescriptive and restrictive for progressive credit unions in a rapidly changing marketplace.

If regulation is disproportionate to the risks / structures or a one size fits all approach is adopted it may be at the expense of reduced innovation and run the risk of creating a market sameness / convergence to the detriment of genuine consumer choice, access and competition.

CUDA has called for a review of the regulatory / legislative framework under which credit unions currently operate. We welcome recent comments in this regard by the Minister for Finance and IFSRA's reference to "*possible proposals for revisions to the Credit Union Act 1997*" in its recent Strategy document.

C. Role of IFSRA's Registrar of Credit Unions

The role of the Registrar of Credit Unions within IFSRA is to ensure that a proper system of regulation is applied to credit unions. Although the Registrar

of Credit Unions has extensive powers under current legislation, limits can only be changed by Ministerial Order.

Within the context of ensuring the reputation of the Movement as a whole CUDA believes that a risk-based regulatory approach is required. This would govern the number and type of inspections undertaken by the Registry and the operating limits / flexibility that would apply to each credit union.

In line with other sectors, the Registrar of Credit Unions intends to develop credit union 'Codes of Practice' in co-operation with the Consumer Director and in consultation with credit union representative organisations. CUDA welcomes this approach.

The Registrar of Credit Unions is the statutory regulator solely responsible for monitoring and supervision of credit unions. Any duplication or outsourcing of powers reserved to the Registrar, whether through registered rules or otherwise, or indeed the perception of self-regulation by credit unions or an associated body is not acceptable to CUDA.

D. Deficiencies in existing legislation

The following paragraphs highlight some "general" deficiencies in existing credit union legislation – it is not an exhaustive list by any means. CUDA looks forward to interacting on a more comprehensive, detailed and wide ranging basis with both the Department and IFSRA on this topic in 2005.

Structure

Certain requirements in the Credit Union Act relating to the organisational structure of Credit Unions need to be reviewed in the context of the current scale of operations which credit unions encompass and represent.

Membership

The general requirements for membership of a credit union and the rights of non-qualifying members should be reviewed.

General Provisions

Under S.182 of the Act, “After consultation with the Registrar, the Credit Union Advisory Committee and any other bodies appearing to the Minister to be expert or knowledgeable in matters relating to credit unions, the Minister may make regulations that may apply either generally, or by reference to a specified category or categories of credit unions, or to a specified time or times, or during a specified period or periods, or by reference to any other matter as the Minister may consider appropriate”.

In particular, a differentiated approach is required relating to limits on deposits, shares and loans, limitations on lending and the introduction of new services.

To date, the regulatory and legislative approaches have been on the basis of a “one size fits all’ for credit unions. CUDA believes that Ministerial regulations / legislative changes are required to provide a framework for the Registrar of Credit Unions that recognises the diversity of credit unions and applies a risk-based approach to regulation.

Statutory Savings Protection Scheme

The existence of an approved Savings Protection Scheme (SPS) under Section 46 of the 1997 Act has been described by the Registrar of Credit Unions as a “vital component” for the stability of the Credit Union Movement. Although a fund of €90m exists it is neither incorporated nor under independent control and the funds have not been exclusively applied for the protection of members’ savings. The scheme is not an approved scheme and therefore not subject to inspection by IFSRA under Section 46(3) of the 1997 Act. The absence of a statutory scheme with guaranteed protections places credit unions at a disadvantage in the financial market place.

The establishment of such a scheme, **in strict accordance with IFSRA's stated principles**, is an absolute priority and we therefore welcome IFSRA's commitment in this regard in its recently published strategy for 2005. International best practice in this area sees a complete and transparent separation of the operation of Statutory based Savings protection arrangements from the work of Credit Union trade associations or representative bodies. In this regard, CUDA strongly supports IFSRA's requirement for an approved SPS to be independent of Credit Unions and their representative bodies. It also follows that the supervision and monitoring requirements of any approved savings protection scheme for credit unions members in Ireland should rely on the work of IFSRA alone.

CUDA will strongly support any IFSRA initiative / legislative changes required to underpin the introduction of such an approved Savings protection arrangement for Credit Unions in 2005.

CONCLUSIONS

1. CUDA welcomes the inclusion of credit unions under IFSRA's statutory remit. We support IFSRA's Strategy of having a suitably differentiated supervisory approach for credit unions and the development of codes of practice in conjunction with credit union representative organisations.
2. From the prospective of the forthcoming consolidation legislation CUDA believes credit unions should be omitted from any cross-sectoral approach and from a modified sectoral approach except in so far as its provisions can be shown to be common / appropriate to all sectors. A sectoral approach is most appropriate for a unique and diverse Credit Union Movement and this is recognised in the structure of IFSRA through the statutory position of Registrar of Credit Unions.

3. The regulation of credit unions by the Registrar and his team must be in proportion to the risks posed by individual credit unions or groups of credit unions.

4. A revised regulatory approach is required for credit unions, including revisions to the Credit Union Act 1997 and changes to registered rules. Central to this approach are IFSRA and the Registrar of Credit Unions as the sole monitoring and supervisory authority; the introduction of a statutory based independent savings protection arrangement for credit unions and the flexibility to facilitate the capabilities and ambitions of progressive credit unions in delivering a broader and deeper Credit Union service to their members.