Trade and Representative Association
Business Support Services
Monitoring and Supervisory Activities
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Irish League of Credit Unions
IRELAND

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ILCU Submission to the EBA Consultation Paper on the Draft Guidelines (revised) on methods for calculating contributions to deposit guarantee schemes under Directive 2014/49/EU repealing and replacing Guidelines EBA/GL/2015/10

28 October 2022

Dear Sirs,

The Irish League of Credit Unions ("the League") welcomes the opportunity to provide comments to the EBA on its Consultation Paper on the Draft Guidelines (revised) on methods for calculating contributions to deposit guarantee schemes under Directive 2014/49/EU repealing and replacing Guidelines EBA/GL/2015/10.

The League is the trade and representative body for just under 200 credit unions in the Republic of Ireland and we make this submission on behalf of our affiliated credit unions. Credit unions affiliated to the League have a total of 3.17 million members and €14.56 billion in savings (shares and deposits).

We welcome the fact that the Directive recognises that a lower level of contribution can be set for lower risk sectors and support the concept of creating risk-based levies for DGS fund contributions. The application of a lower level of contribution for Irish credit unions can be justified by virtue of the inherently lower risk model of credit unions but also due to other mechanisms and supports which are in place specifically for credit unions in Ireland which would reduce the likelihood and impact of a call on the DGS.

The Central Bank and Credit Institutions (Resolution) Act 2011 established a resolution regime for credit institutions and credit unions in Ireland. The Credit Institutions Resolution Fund (Resolution Fund) was established under this legislation to support resolution actions in the State, and is managed and administered by the Central Bank of Ireland. Credit unions are now the only financial institutions contributing to the Resolution Fund and furthermore have exclusive access to the fund

The purpose of this fund is to provide a source of funding for the resolution of financial instability in, or an imminent serious threat to the financial stability of, credit unions. As such where a credit union is in financial difficulty it is more likely that recourse will be had to this fund and as such this, especially when coupled with the increased supervision by the Registry of Credit Unions, reduces the likelihood of a call on the DGS. The target size of the Resolution Fund is set at €65 million and the intention is that this target should be met by 2025. There is €49 million in the Resolution Fund as at June 2022.

In addition, credit unions in Ireland contribute to a State Stabilisation Scheme which assists credit unions in a situation where the credit union is still viable but its regulatory reserve ratio is between 7.5% and 10% of the total assets of the credit union. The Stabilisation Fund provides financial support to a credit union to restore and facilitate maintenance of a credit union's reserve requirement. Credit unions are the only institution in the state that has such a state stabilisation scheme. Again, the existence of this fund solely for the purpose of stabilising credit unions reduces the likelihood of a call on the DGS and demonstrates that credit unions are a lower risk sector.

The above referenced funds, individually and collectively, provide a support mechanism to credit unions in Ireland. The existence of these funds clearly evidence the lower risk of the credit union vis a vis the DGS. It is noted that the Deposit Guarantee Directive recognises that Institutional Protection Schemes can be taken into account when calculating contributions and the above schemes should be taken into consideration when evaluating the risk profile of credit unions in Ireland in the calculation of the DGS contributions.

In addition to the various support mechanisms available to credit unions which contribute to credit unions lower risk profile there are various other demonstrable reasons to evidence the lower risk nature of credit unions and thus justify, in accordance with the Directive, a lower level of contribution to be applied to the credit union sector in Ireland.

Credit unions are less risky on a per asset basis than large banks because they have less complex operations and because the large sizes of commercial banks present concentration risks to DGS funds. Whereas the success or failure of a single large bank could exhaust the reserves of the DGS fund—the considerably smaller total assets of credit unions (the average asset size in Ireland credit unions is €88m approximately) are divided among over 200 individual credit unions in Ireland that each have a separate balance sheet, independent management and common bond restricting membership to their local community and as such succeed or fail on their own.

Credit unions are fully self-financed, only a handful of credit unions have any borrowings at all, and credit unions do not borrow to lend or for day-to-day expenditure. Total borrowings make up only 0.001% of the total balance sheet.

Credit unions in Ireland are extremely well capitalised and are required to maintain a regulatory reserve ratio (capital) of 10% of total assets. This requirement is far higher than for other financial institutions in that the assets of credit unions are not risk weighted for this calculation. In monetary terms credit unions affiliated to the League have €2.71 billion in capital, up 2% year on year. Credit unions have a buffer of over €968 million in excess capital above requirements, this buffer is also increasing. 58% of credit unions have capital above 15%. It should also be borne in mind that approximately 64% of credit union assets are held in deposits and investments (of which over 68% are held in deposit accounts in banks).

Credit union loan arrears are now at historical lows. During the Covid 19 pandemic, arrears ticked up very slightly but have been falling since. The overall arrears ratio (NPL ratio) is now down to 2.98%, this is a new low. These low arrears ratios would be the envy of other financial institutions. In addition, credit unions have built up provisions for bad debts and despite the economic crisis provisions now exceed total loan arrears by €200 million. So loan arrears are fully covered by loan provisions, and credit unions also have €2.71 billion in capital reserves.

Unlike banks which typically engage in more complex and risky business activities, credit unions have a very simple savings and loans business model and operate under highly prescriptive legislation - the Credit Union Act, 1997 (as amended). The legislative provisions and regulations in relation to investments, lending limits and savings are prescriptive and limited. Credit unions have no exposure to high risk investments such as derivatives with over three quarters of investments in straight forward deposits. Counterparty risk is mitigated by a regulatory requirement to have no more than 20% of investments in any one institution. There are also strict liquidity requirements which credit unions must adhere to. In addition and unlike banks, credit unions do not engage in FX trading, dealing rooms, derivatives trading, leveraged finance etc. The legislative and regulatory restrictions in place reduce a credit unions risks in myriad respects compared to the business activities commercial banks are permitted to engage in.

The categorisation of credit unions as low risk, comparative to the banking sector, is also very clearly evidenced by virtue of the fact that under the Central Bank of Ireland's Probability Risk and Impact SystemTM (PRISMTM) the vast majority of credit unions are in the medium low or low category and no credit union is in the high risk category (which is where the banks are rated).

We also believe that account should be taken of the credit unions' financial inclusion mission and the desirability of diversity in the financial sector, and be able to assign institutions that promote these public policy goals (i.e. credit unions) a lower risk rating in order to further the public good.

Given the above, it is beyond doubt that credit unions are significantly lower risk both in relation to the probability of a call on the DGS and the extent of the impact of a call on the DGS. As such it is clearly justifiable for credit unions to qualify for a significantly lower level of contributions to the DGS.

For the above reasons, we would submit that credit unions (particularly those in Ireland) should be subject to lower contribution rates than currently apply.

Representatives of the League are available to discuss the contents of this submission, or provide further information as required. Any queries on the issue can directed to:

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