



**SUBMISSION FROM**

**THE CREDIT UNION DEVELOPMENT ASSOCIATION**

**IN RESPONSE TO**

**EBA [European Banking Authority]  
Consultation Paper:  
Draft Guidelines on Product Oversight and  
Governance Arrangements for Retail Banking Products**

**9<sup>th</sup> February 2015**

## **Introduction**

CUDA (Credit Union Development Association) is a progressive representative & development association that was formed in 2003 by Ireland's most progressive and leading Credit Unions, in recognition of the real need for progressive credit union leadership and development in an increasingly complex financial environment.

CUDA has a growing membership with 10 owner members and 18 Affinity members. CUDA is the only legally incorporated representative association for Credit Unions in the Republic of Ireland. Its credit union membership has over 250,000 members.

We thank the EBA for the opportunity to comment on the proposed Guidelines on Product Oversight and Governance Arrangements for Retail Banking Products. We would be happy to elaborate further on any points made in this submission, if required. Please do not hesitate to contact us in this regard. Contact details are listed at the end of this submission.

We have consulted with our owner member Credit Unions in relation to this Consultation Paper. We have not responded directly to the questions stated in the Consultation Paper as we provide general commentary in our short Response below.

## General Commentary

CUDA has considered the Paper in detail. We appreciate the regulatory remit of the EBA. We appreciate the need to set standards across the financial industries with regard to product and services. Whilst, in principle, we do not argue with the objective of the draft Guidelines, we are unable to measure the relevance and practicality of such Guidelines for the Credit Union sector.

In Chapter 5.2 Cost-Benefit Analysis / Impact Assessment, the Paper notes that the potential risks to the financial system of widespread misconduct of financial institutions have been identified and analysed in various reports by European and national competent authorities, including reports from the EBA and the Bank of England. According to the Paper, reports identified a widening number and magnitude of incidents of mis-selling of financial products and concerns about insufficient provisions and inadequate disclosure. CUDA queries to what degree such reports focused on the credit unions sector with regard to 1. *Relevance*, and, 2. *Impact*. Indeed, as part of the EBA's 2014 survey to inform the draft guidelines, was adequate reporting and analysis sought by and/or provided to the EBA from member states?

When regulating and supervising policy at national level, the Central Bank of Ireland has recognised a *one size fits all* approach is not always appropriate. There are examples of this. Credit Unions have specific legislative and regulatory provisions with regard to lending and savings products<sup>1</sup>. Furthermore, significant policy determined fit and proper for the main stream banking sector were not deemed relevant or practical for the Irish Credit Union sector. Examples include requirements set down by the Central Bank with regard to mortgage lending such as Consumer Protection Code 2012 (CPC 2012) and the CCMA (Code Conduct on Mortgage Arrears). The impact of imposing such policy already entrenched in the frameworks of many main stream banking sectors can have punitive effect where the relevance or practicality has not being appropriately considered.

Credit Unions are member owned, owner driven and owner focused. Unlike the many manufacturers and distributors which are commercially or shareholder driven, Credit Unions are not for profit. This entrenched member focused and not for profit origins ensure that products and services are designed to meet the interest, objectives and characteristics of their target market – this we will see is a very limited and defined market, and does not give rise to exposure for consumers [members] on a global or national level.

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<sup>1</sup> Resulting from the Credit Union 1997, as amended

Following a reclassification of credit unions under Basel III, the European Commission noted that “*although strictly speaking financial institutions, in the light of the special nature of their business*” a more favourable outflow rate would be applied for deposits made by credit unions (Brussels 10.10.2014 C(2014) 7232). The original proposal contained an extremely negative, albeit unintended, consequence for credit union investment income and we welcome the European Commission and the European Banking Authority recognising this difference. We would ask that this distinction is considered in all areas of policy impacting on the financial market. Given that the EBA have recognised a distinction in the past, CUDA welcomes and supports the draft guidelines provided the impact analysis and relevant reports considered this distinction in order that European Authorities are empowered to study the relevance and practicality of the policy document in question on the sector.

In our view the introduction of the draft guidelines is to restore the confidence of consumers in the financial sector and to help safeguard consumers going forward from irresponsible manufacturing and distribution of products and services. Credit Unions provide basic savings and personal lending products and services, and, whilst diversifying its product and service base is likely to evolve this may occur in a very controlled manner.

The concern emanating from the Paper is that widespread misconduct of financial institutions, in particular the “widening number and magnitude of incidents of mis-selling of financial products. Credit Unions are localised. Unlike Credit Unions in Canada and parts of America, Europe based Credit Unions remain restricted and small. Therefore, the *fall out* of one particular Credit Union regarding conduct failure remains very limited. Due to the localised nature and specific target market the degree of complexity given the market segment to which the products are sold is very minimal.

Credit Unions are not permitted to compete on the open market. Their market is limited to their respective members and their members are restricted by common bond. Typically this amounts to a geographical boundary. The larger Irish Credit Unions would have a membership of approximately 30,000 and some would be as small as 5,000 members. This eliminates consumers [members] from being sold or exposed to exchange rate risks. Market conduct failure has little significance as the products are limited and the market restricted. Scale is not a concern. There is no apparent market-wide retail or wholesale conduct failures.

Aside from the limitation of product and market, other features of the Credit Union model are worth highlighting in our Response and are open to

consideration when factoring in the likely occurrence of retail conduct failure or market conduct failure to the extent or concern as raised in the Paper:

### 1. Interest Rate Cap

Unlike banks, credit unions are subject to rigid interest rate caps. Banks can shoulder the increase in write downs or financial losses by passing on some of the financial loss to future, or indeed existing, consumers in the form of an increase in the price of credit, and other charges, and this *does* need monitoring and supervision. On the opposite scale, under Section 38 of the Credit Union Act 1997, as amended, Credit Unions are bound to offer loans within an upper interest limit of 12% per annum. Other jurisdictions have a similar upper interest rate limitation.<sup>2</sup> The Paper references “excessive interest rates for loans charged to consumers across the banking sector” as a market conduct failure. Due to the statutory limitations, Credit Unions operate within a restricted profit margin, and, are prevented from adopting a risk based pricing for high risk categories. For the consumer [member], this means that excessive interest rates are not incurred.

### 2. Mortgage lending

Mis-selling features strongly in the Paper, including types of mortgages sold to consumers beyond the target market in which they were originally devised. Credit Unions are not prohibited from providing home loans to members. However, such home loans are subject to the very rigid maturity limits contained under credit union legislation<sup>3</sup>. On average a medium sized Credit Union<sup>4</sup> could provide 30 home loans in the duration of a typical loan. The Paper notes the many instances in which inappropriate mortgages were sold to consumers who could not afford them. This whole-scale and large-scale misalignment of product and consumer was not, nor is likely to be, a feature in Credit Union mortgage lending.

Indeed, with regard to lending products, the Irish Insolvency Service of Ireland (ISI)<sup>5</sup> has shown that of the €910million of debt involved in the approximately 1,600 cases currently with the ISI, the majority of which is mortgage debt, only 2% of the overall debt is Credit Union related. This highlights the low exposure for Credit Union members accessing credit products.

### 3. Additional Services

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<sup>2</sup> In the United Kingdom the interest rate cap is at 2% per month (Order 2006 No. 1276)

<sup>3</sup> Section 35(2) of the Credit Union Act 1997, as amended.

<sup>4</sup> Based on a static loan book of €25,000,000

<sup>5</sup> Established in Ireland under the Personal Insolvency Act 2012 to help solve the high level of mortgage and other debt through a number of debt reduction and debt right-off arrangements.

The Paper cautions the banking sector to consider the needs of its customers when designing products. Credit Unions are limited on products and services. Products are designed around their owner members, and, not the other way round.

Furthermore, the ability to provide products and services is not open-ended. In all but a number of prescribed products and services, statutory provisions require a Credit Union to seek approval from the Central Bank of Ireland should the Credit Union propose to offer a new product or service to its members. Approval is provided only on demonstration of a good and robust business case<sup>6</sup>.

#### 4. “External” manufacturers

218 Credit Unions hold dual authorisation in Ireland. This means that they are permitted by the Central Bank of Ireland to act as retail intermediaries on behalf of other manufacturers. However, official statistics show that total income generated from fees and commissions by Credit Unions that are also authorised as retail intermediaries is less than 3% of income in each of these credit unions<sup>7</sup>. Credit Unions are not by nature, distributors of products and services provided by external manufacturers.

Finally, whilst the draft guidelines build on various provisions set out in existing Directives, the relevance and application of such Directives, such as the Capital Requirements Directive, for the Credit Union sector is noteworthy, especially where policy and the current draft guidelines are built upon existing Directives not applicable to the sector. To compound this point, CUDA had sought derogation from provisions of Directive 2014/17/EU (“Directive on Credit Agreements for Consumers relating to Residential Immovable Property or Mortgage Credit Directive”) on the basis that:

1. *The application of the Directive becomes punitive in nature as credit unions are at a transitional stage of development*
2. *Blanket application is not necessarily in the best interests of consumers*
3. *Credit unions are subject to statutory restrictions preventing them competing in the open market*
4. *Provisions of the Directive become redundant where already provided for under credit union, or other, legislation*

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<sup>6</sup> Section 48 of the Credit Union Act 1997, as amended.

<sup>7</sup> Central Bank of Ireland Consultation Paper CP83 August 2013 taken from Credit Union annual returns.

As the high level objective of the guidelines is the protection of consumer from detriment in retail financial markets. CUDA reiterates the sentiment made at Point 2. above: that blanket application of policy is not necessarily in the best interests of consumers.

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We again thank the EBA for the opportunity to part-take in the consultation process and are happy to elaborate on any matters raised in our Response.



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