An Roinn Airgeadais
Department of Finance

Retail Banking Review

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www.gov.ie/finance

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Foreword

The retail banking sector, which is absolutely critical for the functioning of the economy, has been subject to huge changes over the last decade and a half. The number of banks serving the sector reduced from 12 to 3 as banks were amalgamated or closed down and foreign owned entrants exited the Irish retail market. The legacy of the Global Financial Crisis is still being felt in our retail banking sector in the form of higher capital costs and the banks and citizens still dealing with the issues arising from long term mortgage arrears. In this environment there has been significant changes in the global banking landscape, many of which have been driven by the COVID-19 pandemic as well as rapid developments in financial technology.

The seemingly steady state of the Irish retail banking system was disrupted in 2021 as we saw significant bank branch closures, the announcement by NatWest that it was withdrawing from Ireland by closing Ulster Bank, one of the oldest banks serving the Irish economy, and, very shortly thereafter, the announcement that KBC, which had a presence in Ireland for more than 40 years, was also leaving the market.

I decided that the time had come for a major review of the retail banking sector and I published the comprehensive terms of reference (ToR) last November. In the period since, as outlined in the Introduction to the Review, the Review Team has commissioned and published an informative consumer survey, hosted a Retail Banking Dialogue, run a public consultation process and engaged with many stakeholders directly as well with entities like the Central Bank of Ireland and the Competition and Consumer Protection Commission. This has all been synthesised into a comprehensive report that:

- Describes the retail banking landscape and the disruptive forces for change affecting it, especially digitalisation, which is often referred to as fintech, and
- Identifies issues that we are facing today such as:
    - The uncontrolled reduction in our access to cash and to our traditional ways of accessing financial services without sufficient development of the new services, especially when issues arise,
    - A number of oversights and gaps in consumer protection and financial inclusion,
    - Gaps in our regulatory landscape such as in relation to parts of our SME lending not being subject to regulation, and
    - The need to pay more attention to competition as we face into a period when the retail banking market becomes more concentrated and additional competition is becoming more dependent on players who are more reliant on market funding.

The Review concludes that the trends we are already seeing and the issues arising from those trends will only grow if no action is taken. However, the Review is clear that further change is coming and we cannot reverse or stop these changes. So the Review Team has developed a wide ranging set of recommendations to address the issues and, critically, to put in place measures that will help us to navigate the further changes that are coming in a controlled, fair and equitable way.

The Review Team, in accordance with the deadline specified in the ToR, submitted the draft Review to me in November 2022. Having examined the Review in detail, I brought the Review to Government on the 29th of November 2022 to seek its approval to publish the Review and to implement its recommendations in line with the timelines suggested in it.

Following consideration of the Review, Government approved the decisions I sought and, as a result, the recommendations contained in the Review are now Government policy.

Implementation of the recommendations will place a burden on the Department of Finance and the Central Bank, requiring the deployment of significant resources. Delivering many of the recommendations will also require strong collaboration between both organisations, which they both have demonstrated many times in the past. Other recommendations will require implementation by other State agencies, such as the Competition and Consumer Protection Commission (CCPC), Government departments and other relevant stakeholders.

Within this latter group, one set of stakeholders stands out as having the most to do and the most responsibility, namely the retail banking sector and the entities within it. It is important that they ensure the interest of consumers are a priority in their organisations and seek to work together, where possible, to deliver the best outcomes for the economy and citizens.

I would like to thank the Review Team for its hard work.

Executive Summary

Background

A stable and viable retail banking sector is essential for a modern economy to support the wellbeing of society as a whole. In his speech at the Retail Banking Dialogue, Minister for Finance Paschal Donohoe TD stated that 'as a society, and as an economy, we need a functioning banking system that helps households and businesses achieve their financial, economic and social needs.'[1]

The key products and services provided by the retail banking sector include: the acceptance of deposits to meet the savings needs of consumers; the provision of loans, including mortgages and business loans; and enabling payment for goods and services.

The retail banking sector has undergone transformational change in the past two decades. Much of this change has been driven by the international and domestic response to the Global Financial Crisis (GFC), which had severe consequences for banks across the world. Banks in a number of countries, including in Ireland, required both liquidity and funding support to enable them to continue operating.

In the initial years following recapitalisation, the Irish banks faced material challenges, including managing large portfolios of non-performing loans (NPLs). Since then, significant progress has been made in the area of NPLs, albeit further work is necessary. The sector has also, up to recently, been operating in a prolonged period of low and negative interest rates.

These two factors have had a negative impact on the traditional banks' profitability, which has lagged behind European peers. [2]

Developments in technology have driven significant change in the retail banking sector. The entrance of digital banks and non-banks is providing consumers and SMEs with greater access via digital distribution channels, as well as greater provider and product choice, which is welcome.

New entrants have enabled a shift in the behaviour of consumers, who traditionally used their bank as a one-stop-shop for all their banking products and services. While the vast majority of consumers still use traditional banks, there is an increasing trend for consumers to also choose a number of additional providers to meet their different needs.

[1] https://www.gov.ie/en/speech/fd941-retail-banking-review-dialogue-minister-donohoe-keynote-speech/
[2] Following the departures of KBC and Ulster Bank the domestic banks will comprise AIB, Bank of Ireland and PTSB, referred to throughout the report as 'the traditional banks'.

The decision in 2021 by KBC and Ulster Bank to leave the market has led to further change and disruption as c. 1.25 million personal and business customers switch their accounts.[3] Following these departures the number of traditional banks in Ireland will have decreased from the pre-GFC number of 12 to 3. This leaves Ireland in an unusual position vis-à-vis smaller European states, as all our traditional banks are domestically headquartered and managed.

Establishment of Retail Banking Review

As a result of the departures and other changes occurring in retail banking, in November 2021 the Minister for Finance published the Terms of Reference (Appendix 6) for a broad-ranging review of the retail banking sector in Ireland. Over the last year, a team within the Department of Finance ('the Department') has conducted a detailed assessment of the sector and engaged with different stakeholders.

This Report is the outcome of the Review Team's work, and includes a range of policy recommendations addressed to the State, its agencies, regulatory bodies, as well as the retail banking sector. The recommendations are to ensure an appropriate policy and regulatory landscape and to help guide the sector in meeting the needs of society and the economy in the coming five to ten years.

As in other areas of economic activity, the provision of banking services on a commercial basis requires the providers of such services to generate an acceptable commercial return. No firm can survive in the long-term unless it generates a sufficient return for its owners and investors, in addition to having sufficient resources to maintain and grow its business and withstand different economic cycles. Retail banking is no different, and due to its importance to the economy, it is subject to regulation.

The need to generate a commercial return must be balanced by the wider objective of supporting citizens and the broader economy. This balance has been considered by the Review Team throughout its work, and underpins the recommendations.

Key Findings

The key findings of the Review are outlined below.

IRISH RETAIL BANKING LANDSCAPE OVER THE NEXT 5-10 YEARS

It is the view of the Review Team that the Irish retail banking sector in the coming years will be served by the three traditional banks, credit unions, An Post, digital banks and a number of non-banks. The traditional banks are expected to retain their universal product offerings, digital banks are likely to expand their product ranges (as their licences permit them to provide

[3] https://www.centralbank.ie/statistics/data-and-analysis/credit-and-banking-statistics/account-migration-statistics

products and services not currently offered by them in Ireland), while non-banks are likely to focus on particular products and/or particular segments of the market.

During this period the sector must also develop and expand the credit products available to support consumers and SMEs make the necessary investments to reduce their carbon footprints and contribute to Ireland meeting its 2030 and 2050 climate targets.

The sector will continue to be fragmented, with consumers obtaining products and services from a range of providers, some of which will be providing products or services via passporting from another EU or EEA Member State. This is a relatively new development in the Irish retail banking sector, but one which the Review Team expects will continue.

Additionally, the fact no new entrant has come forward to take over the operations of KBC and Ulster Bank, and previous departures of other foreign owned traditional banks suggests policy formation for the retail banking sector should not presuppose the entry of a new large retail bank, even if such an event would be welcome.

LEVEL OF COMPETITION

Following the departure of two traditional banks, the Irish market will have lost two significant competitors, however the Review Team believes that despite the level of concentration, and subject to continued strong regulatory oversight, sufficient competition will remain in the short to medium term. However, as non-banks generally have a greater dependency on wholesale markets for funding, their levels of activity and product offerings are more likely to follow the economic cycle. Thus, the market will see an expansion and contraction of competition at its margins at different points of the economic cycle.

Given the concentrated nature of the retail banking sector, the Review Team believes it is important that the level of competition is monitored, and that certain measures be implemented to facilitate new entrants.

It will be important for citizens and the economy that the two relevant authorities, the Central Bank of Ireland ('the Central Bank') and the Competition and Consumer Protection Commission (CCPC), continue to work closely together on issues that are common to their respective roles. The two authorities should build on existing arrangements and establish closer coordination to share perspectives, information, and experience of the orderly functioning of markets, consumer protection and competition in the retail banking sector.

To facilitate new entrants, or existing providers seeking to expand their retail banking product offerings, the Review Team has recommended certain measures that would help a new entrant build market share with minimal frictions. These include reforming the Switching Code[4]

[4] https://www.centralbank.ie/docs/default-source/regulation/consumer-protection/45-gns-4-2-7-code-of-conduct-o.pdf?sfvrsn=1b59d71d_6

(taking into account the lessons learned from the current Ulster Bank/KBC migration), seeking to resolve IBAN discrimination, and for the sector to promote and facilitate the greater use of Open Banking within the Irish retail banking sector.

Credit unions have a strong and trusted brand, they are present in communities throughout the country, and have been developing their product offering. The credit unions are already a significant player in consumer credit, and they are making inroads in the current account, mortgages and SME segments of the market. These developments, coupled with their collectively strong levels of capital and deposit bases, leads the Review Team to believe that credit unions could play a greater role in the provision of retail banking products and services in the coming years.

The Review Team considers that in addition to implementing the changes enabled by the legislation currently being progressed, the credit union sector and its leadership should develop a strategic plan to deliver business model changes that would enable the sector to safely and sustainably provide a universal product offering to all credit union members. The Review Team understands the Department and the Central Bank will engage constructively, developing new legislation, if required.

With its strong brand and significant community presence across the country, An Post is already working in partnership with several firms in the retail banking sector to provide critical retail banking products and services in a number of areas. There is scope for An Post to further expand its offerings in consumer and SME retail financial services, in partnership, and on a commercial basis with other firms.

ACCESS TO CASH & BANKING SERVICES

Mainly due to technological developments, the way consumers and SMEs engage with and access banking services has changed rapidly in recent years. This trend was accelerated as a result of the COVID-19 pandemic. While the use of cash and visits to bank branches have been in decline in Ireland and elsewhere for some time, the Review Team notes an European Central Bank (ECB) survey found a majority of people want to have the option to pay in cash, even if some have a preference for digital as a means of payment.

The high cost of providing cash services, as well as the move to a more digitalised banking model has incentivised banks to move away from the direct provision of cash services. However, there continues to be, and will likely always be, an enduring societal demand for cash. In this regard, the Government and the Central Bank, in accordance with the ECB's Cash Strategy, have a fundamental responsibility, together with the banking sector, to ensure the smooth supply of cash and access to cash for consumers and SMEs. Government policy should therefore support the development and maintenance of a sustainable and resilient cash system for as long as cash is needed.

It is important that future reductions in the cash infrastructure do not outpace the expectations or needs of society. To achieve this objective, the Review Team believes a legislative framework should be put in place to manage any further decline in the cash infrastructure in a fair, transparent and equitable manner. The framework should be on a legislative basis that, after consultation with relevant stakeholders, will set criteria for the provision of cash services and enable the cash system evolve in a controlled manner.

The objective of this framework must not be to reverse what has occurred or seek to maintain cash usage at its current level but rather to manage further decline in an orderly way. It is important future changes in the cash infrastructure do not outpace the expectations or needs of society.

The Review Team has noted that in addition to bank provided ATMs and cash counter services, access to cash is facilitated by ATMs located in shops and other settings, cashback provided by retailers, and agency arrangements such as those currently in existence with An Post.

It will be important that industry works together to determine how access to cash develops further. This should be a key factor in the development of a framework that works for customers.

The Review Team has noted the effective operation of the cash system relies on a small number of Cash-in-Transit (CIT) firms and a high proportion of ATMs are owned and operated by unregulated non-bank providers, also known as Independent ATM Deployers (IADs). CIT firms and IADs are of critical importance to the distribution of and access to cash across the country, and currently neither are subject to authorisation or supervision by the Central Bank. The Review Team recommends that both are brought within the regulatory perimeter of the Central Bank.

The Review Team recommends a National Payment Strategy be developed. Work should start in early 2023, and the work should be completed in 2024. This strategy should set out a roadmap for the future evolution of the entire payments system. The strategy should take into account developments in digital payments, and guide how future changes should be made to access to cash criteria and other issues.

Regardless of the pace of further change, it is important to support consumers and SMEs in their transition to a more digitally-based retail banking products, as well as the likely further reduction in the use of cash in the coming years. The Review Team is of the opinion the developments in the sector have outpaced the capacity of some consumers and SMEs to make this transition to digital. To support these ongoing developments, the Review Team recommends the Department should participate fully in the financial literacy stream of the Government's Adult Literacy for Life Strategy and ensure there is a coordinated and integrated approach that leverages all of the State's existing work on financial literacy.

SME CREDIT

SMEs are an integral part of the economy, and access to retail banking products and services is critical for their operation. The recommendations of the Review Team with regard to competition and access to cash are equally relevant for SMEs.

The increasing and diverse number of credit providers to SMEs from the non-bank sector has been a welcome development in recent years. However, given the impact on the funding model of some non-banks from rising interest rates and tighter capital market conditions, it will be important that the Department, in conjunction with others such as the Department of Enterprise, Trade & Employment work with the SBCI, Enterprise Ireland and other agencies to support SMEs, leveraging European Investment Fund monies where possible.

The Review Team also highlights that a portion of SME credit is advanced by firms who do not require authorisation by the Central Bank. SMEs borrowing from unregulated firms do not benefit from protections in the Central Bank's SME Regulations.[5] This situation results in an un-level playing field for the traditional banks, credit unions and regulated non-banks. The Review Team recommends, following consultation with relevant stakeholders, this situation be addressed through legislation so that providers of credit to SMEs are authorised and supervised by the Central Bank.

CONSUMER PROTECTION

The framework for consumer protection has been enhanced significantly over recent years driven by European and domestic legislative changes, as well as developments in codes issued by the Central Bank. Domestically, the introduction of new legislation has extended protections regarding credit provided by High Cost Credit Providers (HCCPs, formerly known as licenced moneylenders), credit provided under Hire Purchase/Personal Contract Plans and credit commonly described as 'Buy Now Pay Later'. The Central Bank's codes have been extended and updated on a regular basis, and the launch of a comprehensive review of the Consumer Protection Code (CP-Code) will be a further catalyst to ensure a comprehensive consumer protection framework operates in Ireland.

While these measures are welcome, the first line of consumer protection must always rest with the providers of retail banking products and services, as they have the most control over ensuring the continuing protection of consumers. The way a firm engages with its customers, and importantly, how firms resolve customer issues, are determined by the extent to which the firm has an appropriate customer-centric culture, and the consequent level of confidence and trust customers have in the firm.

[5] Where funding is provided by an unregulated entity under an SBCI scheme, a term of participation in an SBCI scheme is that the lender must comply with the SME Regulations.

In this regard, the establishment of the Irish Banking Culture Board by the traditional banks represented a positive step in the process of assisting the industry to regain public trust. The forthcoming Individual Accountability Framework legislation, which includes a Senior Executive Accountability Regime, will create a framework to facilitate the embedding of cultural change and ensure greater individual accountability.

The retail banking sector must play a key role in supporting its customers in an evolving retail banking environment. The response of industry to the COVID-19 pandemic, including the provision of payment breaks to customers, and the measures taken by the traditional banks to support customers impacted by the departure of KBC and Ulster Bank are examples of how the sector can support current and prospective customers.

The sector must continue to build on these type of consumer-focused initiatives. In particular, it must give greater consideration to customers' expectations and requirements as it devises strategies to support them in the roll-out of digital enabled products and services, especially those who are more at risk, including the vulnerable.

In the area of consumer protection, building on existing work by the State and the retail banking sector, the Review Team has made a series of recommendations it believes will help improve the experience of consumers and SMEs, especially in a time of continued significant change. These include changes in approach if the traditional banks are considering a change in the services they provide in branches, setting out customer service standards via new customer charters, and also making it clear to consumers who are engaging with firms passporting into Ireland which European ombudsman would deal with any future complaints.

The Review Team also believes a number of these recommendations should be implemented via amendments to the CP-Code prior to 2024, due to the ongoing pace of change underway in the retail banking market.

In advance of any changes being made to the CP-Code, the Review Team calls on the retail banking sector to work together or individually, as appropriate, to implement the actions set out in this report on a voluntary basis.

MORTGAGE MARKET

The traditional banks are the main providers of mortgage lending, and following the departure of KBC and Ulster Bank, the market share of the remaining banks will, at least initially, increase further. Despite the dominance of the traditional banks, non-bank lenders have grown their share of new mortgage lending in a relatively short period, and in 2021 they held a 13% market share of new mortgage lending.

The non-banks provided fixed rates that had terms that were longer than previously available in Ireland, but have recently been impacted by the increased cost of funding in wholesale markets. The €1bn in funding available from BOI to each of the two Retail Credit Firms (RCFs)

as part of the CCPC approval of the bank's acquisition of certain assets and liabilities of KBC Ireland will help support these providers and is a welcome development.

The rising interest rate environment has also resulted in an increase in the number of consumers who are switching their mortgage, or fixing the interest rate on their existing mortgage. For example, in Q3 2022 non-purchase mortgage activity, which includes switching and top-ups totalled €1.3bn, an increase of 175.8% year on year.[6]

While this increase in switching is encouraging, the Review Team believes it is important that the Department, the CCPC and the Central Bank continue to focus on levels of switching in the mortgage market, and where possible to introduce measures to make switching easier.

The Review Team has proposed a number of recommendations in mortgage switching, and in addition the increased use of Open Banking could represent a potential option to improve the mortgage switching process.

The Review Team also believes that mortgage lenders could play a stronger role in identifying and developing new mortgage products or innovations that aid consumers' by providing greater product choice. The Review Team notes the CCPC has required BOI to make a €1 million fund available for distribution to companies involved in developing innovations in the mortgage market. The Review Team calls on eligible firms to utilise these funds and also calls on the other providers in the sector to contribute to this initiative.

In the context of mortgages, it is also important the issue of Long Term Mortgage Arrears (LTMA) remains a key focus. While there has been significant progress over recent years to address LTMA, and the numbers have declined significantly, this should not result in complacency. The Review Team believes the recommendation by the IMF for a co-ordinated approach to the resolution of LTMA should be actioned by the relevant agencies and Government departments, to include input from the Department.

FRICTIONS IN THE RETAIL BANKING MARKET

It is important to identify and resolve, where possible, any frictions that inhibit providers from entering the Irish retail banking sector, as this would help increase levels of competition and choice for consumers and SMEs. Also, it is important there is a level playing field for the traditional banks when competing with other providers based in Ireland, or providing retail banking products and services into Ireland from another EU or EEA Member State. One such friction identified by the Review Team is the remuneration restrictions placed on the traditional banks as part of the bank recapitalisation arrangements.

[6] https://bpfi.ie/publications/bpfi-mortgage-drawdowns-q3-2022/

In the intervening years, new requirements regarding banks' remuneration policies have been introduced at EU level. These requirements align remuneration policy with sound risk management, and aim to ensure appropriate risk taking and avoid short-termism in decision making by senior management. As the State restrictions only apply to the three traditional banks, there is the potential for their customers to be disadvantaged if the impacted banks cannot recruit and retain staff with the skillsets necessary to develop and provide good products and service. In this regard the three impacted banks compete for talent in the wider banking sector and other parts of the economy, including the technology sector.

However, the level of support provided previously by the State and its citizens to the Irish banking system was significant and resulted in considerable hardships for many.

Notwithstanding this point, given the operational challenges and the need to attract staff that will help these banks provide effective service and products to their customers, the Review Team recommends that the remuneration restrictions for the traditional banks be amended.

This would be achieved by amending the full ban on variable pay and replacing it with a limit of up to €20,000, where variable pay would be permissible. In addition the prohibition on the traditional banks providing standard employee benefits should be lifted. The €20,000 limit would align with the threshold above which variable pay is subject to the 'super tax' of 89%, which would remain in place.

Recognising that the state is no longer a shareholder in BOI, the Review Team also recommends that the maximum pay cap of €500,000 for an individual is removed. With regard to AIB and PTSB, the pay cap should be removed in the future when the state's shareholding in them is at an appropriate level.

Conclusion

The Irish retail banking sector has undergone significant change over the last 15 years. Due to actions taken by State, and the sector itself, the Irish financial system is now much stronger. From a financial stability perspective, the capital, funding and liquidity positions of the traditional banks have strengthened significantly. They are subject to far greater regulatory requirements as well as a much stronger supervisory regime. The traditional banks have also taken steps to deal with the mistakes of the past.

The sector has experienced a period of significant change, and this will continue in the medium term. Given the external environment and the ongoing transition occurring in retail banking, it will be important the sector is agile and forward looking. This will enable it to take advantage of the opportunities presented by continuing change in the coming years, as well as ensuring it is not blind-sided by new risks that may arise.

The Review Team believes it is important for providers in the Irish retail banking sector, where appropriate, to increase their level of collaboration, within the bounds of competition law, to lower costs and improve services to customers. This would be particularly helpful in the provision of retail banking products and services into less densely populated areas.

Looking forward, the Review Team believes the Irish retail banking sector can support consumers, SMEs and the economy and ensure the provision of retail banking products and services in an efficient and competitive manner.

The Review Team believes the recommendations within this Report, listed below, will help to achieve this objective. Also the further initiatives and suggested measures addressed to the retail banking sector, will be key to help guide better outcomes for consumers and SMEs.

Recommendations by Chapter

The Retail Banking Review Team recommends:

5. Competition

5.1 With regard to its authorisations and approvals functions, the Central Bank should:

- continue to review its authorisation and approvals processes to identify how these might be improved. This should reflect the importance of a continued flow of high quality new entrants to the financial services markets, while also recognising the importance of gatekeeping activities in mitigating risks to protect consumers and the economy.
- provide guidance for firms on its authorisation and approvals processes to enhance clarity regarding its expectations, processes and timelines (including factoring in any pre-authorisation engagement);
- review the reporting of its authorisation activities. In particular, the Central Bank should enhance reporting of the overall timelines of firms going through authorisation and approvals processes; and
- continue to enhance its strategy and implementation to ensure that its regulatory approach is consistent with realising the benefits of innovation in financial services while ensuring risks are managed and mitigated. In this context, the Central Bank should conduct a detailed review of the Innovation Hub, including peer comparisons, to expand its impact and functionality. Consideration should be given to the types and benefits of regulatory sandboxes adopted in other countries.

5.2 Taking into account the legislative amendments in the forthcoming Credit Union (Amendment) Bill 2022, the credit union sector and its leadership should develop a strategic plan that enables the sector to safely and sustainably provide a universal product and service offering, which is community based, and which is offered to all credit union members, directly or on a referral basis.

Such a strategic plan should demonstrate how credit unions can:

- Scale their business model in a viable manner in key product areas such as mortgages and SME lending;
- Invest in expertise, systems, controls and processes such that the sector can deliver standard products and services across all credit unions, in a manner that manages risks arising and continues to protect members' savings; and
- Provide the option of in-branch services for members of all credit unions.

Where new or amended legislation is required to achieve a universal product offering and associated business model transformation, the Department of Finance (with guidance and technical advice from the Central Bank) should consider the necessary legislative changes.

5.3 In line with its view and its mandate, the Central Bank should:

- In completing its Annual Performance Statement, include an assessment of how the exercise of its functions is consistent with the orderly and proper functioning of domestic financial markets; and
- assess how existing domestic regulation impacts competition within domestic financial markets, recognising its importance to the orderly and proper functioning of those markets.

5.4 The Department of Finance should prepare heads of a bill in 2023 to amend S.50 of the Central Bank (Supervision and Enforcement) Act 2013 to require the Central Bank to carry out and publish assessments of the costs and benefits of regulations it proposes to make under S.48 of the 2013 Act, where appropriate. The assessments are to consider the potential impacts on consumers and fair and sustainable competition, amongst other issues.

5.5 The Department of Finance should review the relevant legislation to identify actions, consistent with provisions governing data collection and use in relevant EU Regulations and Directives, to facilitate increased sharing of information between the Central Bank and the Competition and Consumer Protection Commission across all relevant areas of their respective remits.

5.6 The Competition and Consumer Protection Commission and the Central Bank should build on existing arrangements and establish closer coordination to share perspectives, information and experience on the orderly functioning of markets, consumer protection and competition in the retail banking sector.

6. Climate

6.1 As a matter of priority, the retail banking sector should consider how best to expand its products and services so that it provides a competitive and effective financial offering to consumers and SMEs to assist in the transition to a lower carbon future.

7. Access to Cash

7.1 The Department of Finance should develop Access to Cash legislation, and prepare heads of a bill in 2023 to:

- Require banks that meet objective criteria to provide reasonable access to cash. "Reasonable access to cash" criteria will be defined in consultation with the Central Bank and other stakeholders and the initial objective of the legislation will be to preserve access at December 2022 levels; and
- Provide that the criteria can be changed by the Minister for Finance by regulation, based on research and advice from the Central Bank. This will allow for the further evolution of the cash infrastructure to be managed in a fair, orderly, transparent and equitable manner for all stakeholders.

7.2 Pending development of this Access to Cash legislation, the banks should seek to preserve consumers' and business' access to cash services at December 2022 levels.

7.3 The Department of Finance should prepare heads of a bill in 2023 to require ATM operators to be authorised and supervised by the Central Bank.

7.4 The Department of Finance should prepare heads of a bill in 2023 to provide the Central Bank with responsibility and powers to protect the resilience of the cash system including the authorisation and supervision of cash-in-transit firms in respect of their cash handling activities and related financial services.

7.5 The Department of Finance should lead on the preparation of a new National Payments Strategy to be ready in 2024. The strategy should set out a roadmap for the future evolution of the entire payments system, taking account of developments in digital payments, the use of cheques and other issues, and guide how future changes should be made to the legislative Access to Cash criteria. The Strategy should be informed by, and aligned with, the retail payment strategies of both the EU Commission and the Eurosystem. The Strategy should also consider and consult on whether:

- To legislate pre-emptively to give the Minister for Finance the power to require certain classes of firms, sectors or sub-sectors to accept or facilitate (to an appropriate level) the acceptance of cash; and
- If it should be Government policy that public bodies should accept or facilitate the acceptance of cash for the payment of goods, services, taxes, levies, fees or charges.

8. Access to Branches

8.1 While complying with competition law requirements, the retail banking sector should increase its levels of collaboration, wherever possible, to reduce costs and improve/retain customer service levels. Potential areas include:

- Shared banking hubs in locations where all branches have closed; and
- Developing utility entities in areas such as ATM provision and operation.

8.2 The Central Bank should, in its review of the Consumer Protection Code and, unless otherwise stated, in advance of the completion of its Consumer Protection Code review:

- Require banks to submit robust, board approved, assessments to the Central Bank when they are planning to significantly alter the services provided through branches or when planning to close a branch. These assessments should examine the impact on customers, the suitability of alternative service provision arrangements, and the plans for migrating customers to them, especially at-risk customers. Such assessments, excluding commercially sensitive information, should be published by the relevant bank.
- Require ex-post assessments by banks, to include a survey of impacted customers, nine to 15 months after the change or closure and a requirement to rectify material issues.
- Increase the minimum notice period required to four months (currently one) for significant banking service changes (e.g. going cashless) and to six months (currently two) for branch closures and credit institutions leaving the market.
- Require, in the revised Consumer Protection Code, all providers of retail banking products and services to set out and publish customer charters, incorporating service standards. In advance of changes that may ultimately be made to the Consumer Protection Code, the Review Team recommends that all providers of retail banking products and services implement this recommendation on a voluntary basis.

9. Mortgages

9.1 The Department of Finance should work with the Central Bank in 2023 to identify measures and initiatives to build consumer and SME knowledge and confidence in the switching process for mortgages and other retail banking products, including taking actions that make switching easier, and that address impediments and gaps identified in the process. This work will be informed by the wider switching research being undertaken for the Department of Finance by the ESRI.

9.2	The Central Bank should, as part of its review of the Consumer Protection Code, consider enhancing requirements on how regulated firms provide information on alternative mortgage products to their customers to improve the take-up by mortgage holders of cheaper options which may be available to them. This should be addressed in a standalone section of the Consumer Protection Code.
9.3	The retail banking sector should review their existing mortgage product suite to identify opportunities to enhance and expand it for the benefit of their customers, in particular where this could help reduce the borrower's overall cost of credit.
9.4	The Department of Finance should consult with mortgage lenders and the Central Bank to determine if lenders can provide increased transparency in relation to the composition of variable mortgage pricing.
9.5	Implementation of the IMF recommendation that the resolution of long term mortgage arrears needs to be considered and addressed in a coordinated way by various agencies, including the Department of Finance, the Central Bank, the Department of Justice, and the Insolvency Service of Ireland in consultation with other relevant agencies. The Department of Finance should, together with all the other relevant bodies, take this recommendation forward.
10. SME Credit	
10.1	The retail banking sector reviews its strategies and delivery models for SME credit, making amendments where required to ensure good customer service standards and to facilitate effective engagement by SMEs with skilled staff, either remotely or in-person, as appropriate.
10.2	The Department of Finance should continue to commission the Credit Demand Survey on an annual basis.
10.3	The Department of Finance should continue to work with other Government Departments and the SBCI to identify SME credit market failures or gaps and to develop risk sharing schemes to address them. Where possible, this should be done in conjunction with the European Investment Fund.
10.4	Following consultation with stakeholders, the Department of Finance should prepare legislation to require providers of credit to SMEs to be authorised and supervised by the Central Bank, so that all SME borrowers benefit from the protections of the Central Bank's SME Regulations.
10.5	The Central Bank should review and amend the SME Regulations to take account of legislative changes and developments in the revised Consumer Protection Code, particularly digital/online matters, automated decision making and customer charters

and service standards. The Central Bank should also review the regulations applicable to guarantees issued by, or on behalf of, SME borrowers.

11. Consumer Credit

11.1 The Department of Finance should commission an annual survey of consumers' experiences and perceptions of the retail banking market based on the consumer survey commissioned for the Retail Banking Review.

11.2 The operation of the Central Credit Register should be amended, following engagement with relevant stakeholders, to:

- Reduce the reporting threshold for credit agreements from €500 to €200 and the consultation obligation threshold from €2,000 to €1,000; and
- Introduce a new lower fee for Central Credit Register consultations for low value loans (i.e., loans of less than €1,000, in line with the proposed changes to the obligatory consultation threshold) to facilitate smaller loans, particularly by credit unions.

The Department of Finance should draft legislation, if the proposed amendments require it.

12. Current and Savings Accounts

12.1 The Central Bank should conduct a review of the Switching Code for payment accounts as soon as possible after the current mass migration of accounts is largely concluded. The review should incorporate input from the sector and other stakeholders regarding lessons from the mass migration. The review should also consider requiring the establishment of a switching service in accordance with the Payment Accounts Directive, including examining the feasibility of automatic or manual routing of credit and debit transfers for a set period after an account has switched.

13. Consumer Protection and Financial Literacy

13.1 The Department of Finance should rationalise and simplify consumer protection legislation with the objective of eliminating overlapping provisions. This process should take account of the transposition of the forthcoming revision of the Consumer Credit Directive.

13.2 In line with its statutory mandate, the Central Bank should continue to prioritise the interests of consumers in terms of enhancements to the regulatory framework (supported with evidence-based findings and research, as appropriate) and through the execution of its supervisory role. As part of the review of the Consumer Protection Code, the Central Bank should assess how its integrated mandate across

financial stability, prudential and conduct regulation can be further utilised to ensure the ultimate goal of protecting consumers.

13.3 The Central Bank should, in advance of its completion of its Consumer Protection Code review, require each institution serving the retail banking market to set out clearly to its customers which ombudsman/Alternative Dispute Resolution service will deal with complaints, where the customer does not accept the decision of the provider's internal complaints process. This information should be provided to the consumer as part of the pre-contractual information obligations and at the commencement of a complaints process.

13.4 The Department of Finance should seek to ensure access to appropriate ombudsman/Alternative Dispute Resolution services for customers of passporting institutions is satisfactorily addressed at EU level.

13.5 With regard to financial literacy and digital financial literacy:

- the Department of Finance should:
  - engage with and participate fully in the financial literacy stream of the Adult Literacy for Life Strategy; and
  - seek to ensure that all stakeholders work together so that Ireland is compliant with the OECD High Level Principles on Financial Consumer Protection and the Recommendation on financial literacy.
- The retail banking sector should:
  - build on the work already done by the BPFI and the Irish Banking Culture Board to ensure that its offerings are appropriate to cater for the needs of adults at risk of harm or abuse and empower them to safely manage their own money and financial affairs. The sector should become more responsive to the needs of these 'vulnerable' customers and harness the opportunities that advancements in technology provides to assist them.

14. Staffing

14.1 The retail banking sector should work with the Institute of Banking to consider the development of a Financial Services Skills Framework to build the skills and competencies needed for the future and sustainable development of the retail banking sector.

14.2 The pay restrictions should be amended by:

- Permitting variable pay per employee of up to €20,000 per annum;
- Allowing the provision of standard non-pay benefits for all employees; and
- Solely for Bank of Ireland, removing the maximum pay cap of €500,000 for an individual.

1.Introduction and methodology

In the period since the Global Financial Crisis (GFC), the Irish retail banking sector has undergone significant upheaval and change. While much of this change, which is ongoing, stemmed directly from the impact of the GFC, it is also attributable to technological and digital development that has changed the way all businesses work. As a result of financial technology, the provision of retail banking products and services at scale no longer necessitates having branch networks and this is also reflected in the traditional banks cutting back their branch networks. By 2014, most of the foreign owned traditional banks had withdrawn from Ireland and the sector had reached, what appeared to be, a steady state with five traditional banks providing financial services on a nationwide basis. Three of them, AIB, BOI and PTSB, were domestically owned banks, while Ulster Bank and KBC had UK and Belgian owners respectively.

However, in 2021, both Ulster Bank and KBC announced they were leaving the Irish market and, separately, BOI announced its decision to close 88 of its branches. In light of this, the Minister for Finance, Paschal Donohoe TD decided that the Department should conduct a review of the retail banking sector in Ireland. The Terms of Reference of the Retail Banking Review (ToR) were published on 23 November 2021.[7] The focus of the Retail Banking Review (the Review) is retail banking products and services which are defined as the provision of current and saving accounts, consumer and Small and Medium-sized Enterprise (SME) credit, and mortgages. The Review considered all the firms offering these products to, or servicing these products for, consumers and SMEs including the traditional banks, digital banks, credit unions, non-banks which include retail credit firms, credit servicing firms, payment institutions, e-money institutions, unregulated providers to SMEs and high cost credit providers (HCCPs, formerly licensed moneylenders).

1.1. Methodology

The Review was conducted by a dedicated team in Department of Finance, led by a Principal Officer working with four staff from the Department and two staff seconded from the Central Bank. In the course of the Review, the Review Team:

- Commissioned and published a Consumer Survey,[8] setting out consumers' experience and perceptions of the retail banking sector in Ireland. The survey was conducted by Behaviour and Attitudes through face-to-face interviews with a sample of 1,500 individuals. The survey informed the analysis carried out in the Review.

[7] https://www.gov.ie/en/consultation/8bbea-retail-banking-review-public-consultation/
[8] https://www.gov.ie/en/organisation-information/3c122-retail-banking-review/#consumer-survey-results

- Organised a Retail Banking Sector Dialogue ('the Dialogue') in Tullamore, Co. Offaly on the 16th of May 2022. The Dialogue, which was attended by over 100 participants representing over 60 organisations, included plenary sessions along with breakout sessions focusing on consumers, SMEs and the retail banking model. The views and analysis expressed at the Dialogue informed the work and analysis of the Review Team.
- Conducted a Public Consultation process ('the Public Consultation'), which ran from the launch of the consultation document on the 16th of May until the 8th of July 2022. In total 102 submissions were received. These submissions were reviewed and, where the submissions came within the ToR, taken into account and addressed as appropriate in the Review. It is intended to publish the submissions shortly.
- Commissioned an international comparative analysis, carried out by Deloitte covering seven countries, which may be found at https://www.gov.ie/en/organisation-information/3c122-retail-banking-review/
- Met with various stakeholders throughout the process. Meetings took place with sector and union representatives, public agencies, and organisations representing a wide range of interests.
- Liaised with, received information and analysis from and engaged with the Central Bank, the CCPC and a range of relevant Government departments[9] on the content of the Review and the recommendations it makes.
- Worked closely with colleagues in the Department on the information and analysis used in the Review and on the drafting of recommendations in it.

In the course of its work, the Review Team sought to take a balanced approach to the measures it considered to address the issues identified during the process. Two key considerations that influenced the approach of the Review Team were the recognition that the retail banking sector is:

- Absolutely critical to the functioning of the economy; and
- A commercial sector whose profits are necessary for the accumulation and acquisition of the capital and funding that is needed to provide further credit

The views and analysis in the Report are, unless otherwise attributed, the responsibility of the Review Team.

1.2. Next steps

The Report, including 34 policy recommendations, was submitted to the Minister for Finance in mid-November 2022. Following consideration, the Minister brought the finalised Report to Government, which approved its publication and the implementation of the policy

[9] Department of Enterprise, Trade and Employment, Department of Further and Higher Education, Research, Innovation and Science and the Department of Justice.

recommendations made in it. As Government policy, implementation will follow the established and required procedures. For instance, in the case of legislative actions, the Department will prepare heads of bills to be submitted to Government for approval to draft the legislation in question.

This phase of preparation will, where appropriate, involve engagement with relevant stakeholders and relevant agencies. The regulatory impact of proposals will be considered and regulatory impact analysis statements will be prepared. Any proposed legislation will follow the normal parliamentary process, including pre-legislative scrutiny process in the Oireachtas. The ECB will, where required, be consulted on the proposed legislation. It will also take account of EU regulatory and legislative developments.

Recommendations that have been made to regulators, Government agencies, the retail banking sector and others will be a matter for them to consider.

Please note that in addition to all the listed recommendations, which may be found grouped by chapter in the Executive Summary and by theme in Appendix 2, there are a number of initiatives and suggested measures also included in each of the chapters, which are directed at various stakeholders in the sector. The Review Team calls on the all stakeholders, particularly the retail banking sector, to action these initiatives.

ACKNOWLEDGEMENTS

The Review Team wishes to acknowledge the kind assistance of Mary O'Dea - Chief Executive of the Institute of Banking, who chaired the Dialogue and was the rapporteur for the retail banking model breakout session, Maeve Dineen - Chair of the Financial Services and Pensions Ombudsman's Council, who was rapporteur for the consumer breakout session and Conor O'Toole, ESRI, who was rapporteur for the SME breakout session.

We also thank everybody who participated in the Consumer Survey, attended the Dialogue, responded to the Public Consultation, as well as all the stakeholders who met with the Review Team over the course of the work. The input and information received from the Central Bank, CCPC and Government departments is also greatly appreciated. We also express our thanks to Jimmy Larsen and his team at Behaviour & Attitudes and Adam Kissane and his team at Deloitte for their input. Finally, the Review Team acknowledges the invaluable assistance from colleagues in the Department of Finance.

RETAIL BANKING REVIEW TEAM

The members of the Review Team led by John Palmer were:

Barry Creighton	Geraldine Hannon	Paul Keogh
Sorcha Keogh	Colm Roche	Michael Smyth

2. Retail banking sector landscape

The decision of Ulster Bank and KBC to leave the Irish market has led many to ask if Irish consumers and SMEs can be appropriately served by the providers of retail banking products and services that remain in the market. The GFC caused many of the traditional banks to leave the market, and the imminent departure of Ulster Bank and KBC means that the traditional banking sector will become even more concentrated.

However, new providers have entered the market to avail of market opportunities they identified. This has provided consumers and SMEs with more choice. However, as with any other market or economy of similar size to Ireland, it will always only ever support a certain level of economic activity, which will limit the number of providers that can operate commercially in our market. From an Irish perspective, we have recent experience of having a large number of providers in the retail banking sector not leading to optimal outcomes.

2.1. Market Size

With a population of 5.1 million, the size of the Irish market is small by international standards. Forecasts for 2022 has Gross Domestic Product (GDP) at €499bn and modified Gross National Income (GNI*) at €261bn[10] (with the latter being more reflective of the domestic economy). There are c. 272,000 SMEs operating in Ireland representing 66.4% of total private sector employment and 43.6% of total turnover.[11] The dimensions of the key product offerings of the different category of firms operating in the retail banking sector are set out in Table 1.

Table 1 - Key product offering by category of firm as at 31 December 2021

Category of firm	Product	€bn
Traditional banks	Deposits	€228bn
	Loans	€176bn
	Of which to Irish residents	€137bn
	- Mortgages	€90bn
	- SME	€18bn
	- Consumer	€8bn
Non-banks	Mortgages	€22bn
	SME	€4bn
Credit unions	Deposits	€17bn
	Loans - 90% of which is consumer credit	€5bn

Source: Bank annual reports; Central Bank

[10] https://www.gov.ie/en/publication/04fef-budget-publications/
[11] https://www.cso.ie/en/releasesandpublications/ep/p-bii/businessinireland2019/smallandmediumenterprises/

2.2. The impact of the Global Financial Crisis

The GFC resulted in several banks in foreign ownership leaving the Irish retail market. The number of banks operating in Ireland was reduced further by actions taken by the State. This included amalgamations and closures of banks and led to a smaller, but more stable banking system. Internationally, similar actions were taken by governments to address failings in their banking markets. State interventions in Ireland and elsewhere were motivated by a recognition that the banks play a pivotal role in supporting economic activity.

Alongside the immediate measures taken to stabilise banking systems across the globe, over the decade since the GFC there was wide-ranging reform of the global financial system. This included a material strengthening of banking regulation. In the Eurozone, the Single Supervisory Mechanism (SSM)[12] was established to directly supervise Europe's largest banks (currently comprises c. 110 banks, including AIB and BOI). In Ireland domestic reforms included significant changes to the legislation related to the Central Bank such as the Central Bank (Supervision & Enforcement) Act 2013, a strengthening of the CP-Code and the introduction of the Code of Conduct on Mortgage Arrears (CCMA). The post-GFC programme of reform is largely complete, however some aspects still require actions by legislators and regulators, and these are discussed further in the chapter on Change.

In Ireland, to address issues regarding the solvency and liquidity of the Irish banks, unprecedented actions were necessary to safeguard the banking system. In addition to recapitalising the banks, the Government issued a guarantee which covered all the deposits and debts of six banks.[13] Emergency liquidity assistance was also made available from the monetary authorities, including the ECB. The Deposit Guarantee Scheme (DGS) was expanded to a limit of €100,000 and the credit unions were included.

The total recapitalisation of the domestic banks amounted to €64.1bn, with €34.7bn being invested in Anglo Irish Bank and INBS (IBRC) and €29.4bn in AIB, BOI and PTSB - the three traditional banks that remain in operation today.

The long-standing policy of the Government is to return the three remaining banks into private ownership, while achieving value for the taxpayer. In this regard, the Minister for Finance, Paschal Donohoe recently commented:

> *'It continues to be this Government's belief that banking in the main is an activity that should be provided by the private sector and that taxpayer*

[12] The Single Supervisory Mechanism refers to the system of banking supervision in Europe. It comprises the ECB and the national supervisory authorities of the participating countries: https://www.bankingsupervision.europa.eu/about/thessm/html/index.en.html

[13] AIB, Anglo Irish Bank, BOI, EBS, INBS and IL&P (Permanent TSB)

> *funds which were used to rescue the banks should be recovered and used for more productive purposes.'*

To date, €21.1bn of the investment in the three remaining banks has been recovered in cash by way of disposals, investment income and liability guarantee fees. As part of this activity, the State has fully disposed of its investment in BOI. The remaining investments in AIB and PTSB are currently valued at c. €5.4bn leaving a shortfall of c. €2.9bn.

During 2021 and 2022 the Department has been active in delivering on the Government's policy which, in addition to fully exiting BOI, has seen a reduction in the State's investment in AIB from 71.1% to 57%. The State's investment in PTSB recently reduced from 74.9% to 62.4% following NatWest's acquisition in the bank, representing a non-cash consideration as part of the transaction that saw PTSB acquire certain loan portfolios of Ulster Bank.

The investment in IBRC is largely a sunk cost with a net €1.1bn recovered to date.

Table 2 - Summary of the State's investment in the banks – November 2022

	AIB	BOI	PTSB	Sub-total	IBRC	Total
	€bn	€bn	€bn	€bn	€bn	€bn
Gross invested	€20.7bn	€4.7bn	€4.0bn	€29.4bn	€34.7bn	€64.1bn
Sale/redemption proceeds	€8.0bn	€4.4bn	€1.9bn	€14.3bn	€0.0bn	€14.3bn
Investment income	€1.8bn	€0.8bn	€0.1bn	€2.7bn	€1.7bn	€4.4bn
CIFS/ELG - net	€1.8bn	€1.5bn	€0.7bn	€4.0bn	(€0.6bn)	€3.4bn
Net cash position - In/(out)	(€9.1bn)	€2.0bn	(€1.3bn)	(€8.4bn)	(€33.6bn)	(€42.0bn)
Market value of equity stakes	€4.8bn	€0.0bn	€0.6bn	€5.4bn	€0.0bn	€5.4bn
Net position - including valuations	(€4.3bn)	€2.0bn	(€0.7bn)	(€3.0bn)	(€33.6bn)	(€36.6bn)

Source: Department of Finance

As part of the State's recapitalisation of the Irish banks, certain remuneration restrictions were introduced for staff working in the banks that were recapitalised by the State. These restrictions are still in place today and are discussed in the chapter on Staffing.[14]

2.3. Current Providers

In the recent past, retail banking products and services in Ireland were provided mainly by the traditional banks through extensive branch networks. Historically, the traditional banks played a key role in helping consumers and SMEs achieve their financial, economic and social needs through safeguarding people's savings, providing credit to consumers and SMEs, maintaining the flow of cash through society and ensuring good and appropriate access to retail banking products and services to all in society, including the vulnerable. Through a network of branches, and other channels including digital and online, the three traditional banks that remain in the Irish market will continue to provide important support to consumers and SMEs.

As well as the traditional banks, there are now other significant providers in the Irish market who are playing an increasingly important role. The credit unions and An Post both offer retail banking products and services through their extensive community based networks, with An Post also offering services through franchise post offices.

In recent years, changing regulation and developments in technology have enabled more diverse providers to enter the retail banking market. New providers, including digital banks and non-banks, reach their target customers using various channels including broker channels or directly via digital platforms. These channels represent a much lower cost of entry to the Irish market, compared to establishing a network of branches, which historically would have been a prerequisite to gaining market share.

Despite changes to the range of firms providing retail banking products and services, the traditional banks continue to maintain a strong and dominant market share in many areas, including deposit taking and lending, although in recent years non-banks have been increasing their lending activity, particularly in the mortgage and SME sectors. Digital banks are also expanding their customer bases, with a strong initial focus on the provision of payment accounts. An overview of the retail banking landscape that is within the scope of this Review is as follows:

- Following the departure of Ulster Bank and KBC, there will be three traditional banks (AIB, BOI, PTSB) with 438 branches providing a wide range of retail banking products and services, including cash services, credit (consumer, mortgage, SME), account and payments services as well as other services outside of the scope of this Review, such as investment and insurance services.

[14] The restrictions are in place for staff working in AIB, BOI and PTSB.

- There are three digital banks (Bunq, N26, Revolut) all providing current accounts, whilst one offers credit to consumers. The digital banks have no branch network.
- There are 204 credit unions, operating from over 400 locations all providing savings account products and consumer credit, with a growing number developing a capability to provide current account and mortgage lending products, as well as expanding into the SME sector.
- An Post has a network of 912 post offices providing a range of retail banking products and services to consumers, including cash/cheque lodgements, cash withdrawals, current accounts, credit cards and consumer credit,[15] as well as access to State Savings.
- At 31 December 2021, there were 18 authorised retail credit firms (RCFs),[16] ten of whom are actively originating credit. The business models of these 18 firms vary significantly, with some originating mortgages, SME loans, credit cards and car finance, while others act as credit servicers.
- Separately, there are also 21 authorised (three transitionally) credit servicing firms (CSFs). These firms service loan portfolios, principally mortgages. However, they cannot advance credit.
- There were 63 non-bank lenders to Irish SMEs in 2019 and 2020.[17] Some of these lenders are regulated as RCFs as they also lend to consumers.
- There are 32 HCCPs authorised by the Central Bank. [18] These were formerly known as licensed moneylenders.
- There has been a marked increase in the number of Payment Institutions and Electronic-Money Institutions (PI/EMI) in Ireland, particularly since a new Directive[19] was introduced in 2018 and in the aftermath of Brexit. These providers primarily enable digital and card payments. The Irish PI/EMI sector currently comprises c. 40 firms operating under licences granted by the Central Bank, however, many of these firms' operations are pan-European, rather than domestically focused.

While no new traditional banks have been authorised in Ireland since the GFC, European Union (EU) and European Economic Area (EEA) authorised banks can notify of their intention to passport cross-border and thereby offer services to consumers and SMEs in other countries within the EU. The digital banks Bunq, N26 and Revolut, who are headquartered and authorised by regulators in The Netherlands, Germany and Lithuania respectively, all operate in Ireland on a passporting basis, and collectively are reported to have built an Irish customer base of circa two million. Initially focusing solely on providing payment services, one of these digital banks has already expanded its product range to its Irish customers by providing credit.

[15] An Post provide credit cards and consumer credit as an agent for Avant Money
[16] http://registers.centralbank.ie/DownloadsPage.aspx
[17] https://www.centralbank.ie/statistics/statistical-publications/behind-the-data/the-role-of-non-bank-lenders-in-financing-irish-smes
[18] Central Bank of Ireland Moneylender Register as of 10 October 2022, https://registers.centralbank.ie/DownloadsPage.aspx
[19] Payment Services Directive 2: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex%3A32015L2366

Each of these digital banks, and in accordance with their licence, could offer a wider range of products to Irish consumers should they choose to do so.

In recent years, there has also been an increase in the number of non-banks operating in the mortgage market, who have been growing their share of new business. Recent research show these firms increasing their share of new business from c.5% in 2020 to c.13% in 2021.[20]

Notwithstanding the growth in new entrants to the market, the continued scale of the traditional banks in the provision of retail banking products and services gives rise to considerations regarding the extent of competition and consumer choice in Irish retail banking offerings. These issues are considered in detail within later chapters of this Report.

A key feature of the Irish retail banking sector, highlighted by the Minister for Finance at the Dialogue, is that Ireland is unusual when compared to other small European jurisdictions in that the remaining Irish traditional banks are headquartered and managed in Ireland. In contrast, the position in our peer European countries is that banks are generally subsidiaries of larger foreign-owned firms.

2.4. Business Model Comparisons

The Review Team compared and contrasted the business models of the different types of firms operating in the retail banking sector. Firms were grouped on the basis that they were deemed to be a traditional bank, digital bank, non-bank or credit unions. Traditional banks comprise AIB, BOI, KBC, PTSB and Ulster Bank; digital banks comprise N26, Bunq and Revolut; and non-banks comprise An Post, retail credit firms (RCFs), HCCPs and a number of unregulated firms that solely provide lending to SMEs.

Some of the key business model differences between provider types are:

Product offering

The traditional banks offer the full suite of retail banking products and services, including mortgage, SME and consumer lending, deposit accounts and payment services. To date digital banks have focused primarily on payments, while non-banks mainly offer lending products, often specialising in a particular product or smaller product range, or lending to a particular sector. The credit unions provide deposit account services, while their lending offering focuses mainly on unsecured consumer loans, with modest levels of mortgages and SME credit. An increasing number of credit unions also offer current accounts. An Post, in addition to providing current accounts, also provides deposit gathering through State savings

[20] https://www.centralbank.ie/docs/default-source/publications/financial-stability-notes/non-bank-mortgage-lending-in-ireland-recent-developments-and-macroprudential-considerations.pdf?sfvrsn=f0ab911d_8?

on behalf of the NTMA, consumer credit as agent for an international bank as well as cash services to the customers of some of the traditional banks.

Channel of distribution

The traditional banks, credit unions and An Post operate country wide physical branch networks, as well as digital or online platforms. For mortgage lending the traditional banks are increasingly using broker channels. In contrast, the non-banks have a heavy concentration on the broker channel, particularly for mortgages, with the digital banks exclusively utilising their digital platforms.

Regulation

Firms authorised and regulated by the Central Bank must ensure compliance with all applicable legislation, codes, guidelines and obligations on an ongoing basis. The Central Bank seeks to ensure that the financial system is resilient and trustworthy, that it sustainably services the needs of the economy and its consumers, and is one in which firms and individuals adhere to a culture of fairness and high standards. In this regard, the Central Bank expects the boards and senior management of all regulated firms to ensure their firms are in compliance, on an ongoing basis, with all their regulatory requirements, including conditions imposed at authorisation.

Regulatory requirements are stronger for deposit takers, which comprises the traditional banks, digital banks and credit unions, where full prudential and conduct of business regulation applies. Non-banks are subject to conduct of business regulation but, as non-deposit takers, they are not subject to prudential capital and liquidity requirements. An Post is authorised by the Minister for Finance for the provision of the banking services it offers. Unregulated firms that serve the SME credit market do not, as the description suggests, require authorisation and are not subject to the Central Bank's conduct of business rules, although the Strategic Banking Corporation of Ireland (SBCI) does require the unregulated firms it deals with to comply with them. Unregulated firms that advance credit are, however, subject to the Credit Reporting Act 2013.

Funding

The traditional banks funding model is based on a mix of customer deposits and wholesale funding, with a heavy bias towards the former. This is important as customer deposits are more stable ('stickier') in times of stress. The non-banks cannot accept customer deposits and many of these operators finance themselves through wholesale markets via securitisation and debt issuance.[21] The credit unions are almost wholly funded by on-demand deposits from their members.

[21] The exception is Avant which is funded by its parent, Bankinter.

Capital

The traditional banks and digital banks, as deposit takers, are subject to prudential regulation and must meet the requirements of the revised Capital Requirements Directive IV (CRDIV) and the Capital Requirements Regulation (CRR). CRDIV and the CRR were introduced in 2013 in response to the GFC which exposed weaknesses in banks' capital and liquidity resources. More recently, the implementation of CRDV further enhanced these measures, including strengthening banks resilience to interest rate risk. The credit unions are subject to prudential regulation under a tailored legislative and a regulatory framework developed by the Central Bank. They are exempted from CRD and CRR. The non-banks operating in the Irish retail banking system are not subject to CRR or CRD requirements.

3. Change in the retail banking sector

The retail banking sector is experiencing significant change, with many complex factors disrupting the traditional retail banking model. Some of the driving factors are new, such as digitalisation. Other factors, like competition, have always been drivers of change but the nature of these competitive drivers is now different, meaning the traditional banks have to adapt rapidly so that they can continue to compete in a market where customer expectations are changing, and where greater choice is available.

3.1. Forces driving change

At the Dialogue in May, Mary O'Dea, CEO of the Institute of Banking, outlined the forces that are driving change in the retail banking sector. These are illustrated in Figure 1 and summarised briefly in Table 3.

Figure 1 - Forces of change in retail banking in Ireland

Source: Institute of Banking

The impact of these drivers on the retail banking sector, consumers and SMEs is discussed in the Report. For example, in the chapters on Access to Cash and Access to Bank Services, decisions by some traditional banks to reduce their costs by reducing the number of branches or the types of services provided at branches are impacting on consumers' and SMEs' ability to access basic retail banking products and services, including access to their own cash. In the chapter on Climate, as well as in the chapters on Mortgages, SME Credit and Consumer Credit, the Report outlines how the retail banking sector must adapt and innovate to support consumers and SMEs transition to a more sustainable future.

Table 3 -The Forces of Change in retail banking in Ireland	
Overhang from the crisis	• Substantial increase in capital requirements. • ECB quantitative easing and prolonged low interest rates. • State ownership restrictions. • Trust and culture.
Market Dislocation	• Ulster Bank and KBC leaving the market, with impact for 1 million customers and 100 branches. • Estimated €5bn capital leaving the State. • Davy and Goodbody returned to bank ownership.
Profitability	• Banks need to generate capital to reinvest in supporting consumers, businesses and economic activity. • Profitability of Irish banks has been amongst lowest in Europe (dependency on interest income; capital levels; high cost base). • All banks have cost reduction programmes. • Developing new products (e.g. green mortgages, digital products)
Customer needs and preferences	• Demanding a more compelling personalised digital experience as leading BigTech has taught them to expect. • Speed in decisions – but anti money laundering (AML) can slow things. • For consumers, advice for key life financial decisions. • For SMEs, industry knowledge expected and relationship banking valued.
Digital	• Digital transformation continues at pace (accelerated by COVID-19). • Current and future forces include cloud computing; open networks and standardised platforms.
Regulation	• Individual Accountability Framework (IAF) and Senior Executive Accountability Regime (SEAR) legislation. • Major changes since the GFC include SSM, ECB competent authority, AIB, BOI and Ulster Bank designated significant institutions, Fitness & Probity, capital requirements regulation/directive.
People & Talent	• Banking needs to attract and retain talented employees. • Skills, proficiency, professionalism are key to success. • Leaders play a key role executing strategy and creating the right culture. • Remuneration challenges, as well as competition for talent.
Climate Change	• Banks drive capital to green purposes, facilitate funding, innovative green product design, support customer's transition. • Environmental, social, and governance (ESG) reporting rules – banks must measure progress against goals.

Source: Institute of Banking

In the remainder of this chapter, specific focus is given to imminent change in the legislative and regulatory landscape, which will in part address the post-GFC programme of reform that remains to be completed. In addition, this chapter provides a macro level overview of technology driven change in the retail banking sector given the significant impact that developments in financial and digital technology are having on the sector, as well as on consumers and SMEs.

In the course of its work, the Review Team did not have an objective to stop change from happening, particularly as much of the change that is happening is delivering good outcomes

for consumers and SMEs. Furthermore, much of the change cannot be stopped. However, what was a key focus of the Review Team was identifying the impact of change on consumers and SMEs, and where possible, to recommend measures be taken to manage that change to ensure consumers and SMEs remain protected and included within the retail banking sector, and that they retain continued good access to the retail banking products and services they need.

3.2. Legislative and regulatory driven change

A review[22] of behaviour and culture published by the Central Bank in 2018 identified cultural failings in the five traditional banks serving retail customers.[23] In addition to requiring institution specific actions to address the findings, the Central Bank's review also proposed the introduction of an Individual Accountability Framework (IAF) in Ireland that would apply to banks and other regulated firms in the retail banking sector, as well as the staff working in them.

The Department has worked closely with the Central Bank to introduce such a framework. This resulted in the Central Bank (Individual Accountability Framework) Bill 2022 being published on 28 July. The purpose of this Bill is to provide for greater levels of accountability in the financial services sector. It clarifies the standards of behaviour expected of individuals and firms in the sector, and should help raise these standards in practice. The most significant measures in the Bill are designed to improve individual behaviour and the overall culture in the financial sector including in individual firms.

Better standards of behaviour in financial institutions should achieve better outcomes for consumers. An improved culture in the running and management of financial services firms offers significant benefits in preventing improper behaviour by individuals and organisations, improving trust in the financial services sector and delivering better outcomes for customers.

Better standards of behaviour in financial institutions should achieve better outcomes for consumers

The Bill will allow the Central Bank to use its supervisory tools to ensure that firms are well run and, where necessary, to deal appropriately with individuals who contravene financial services law.

[22] https://www.centralbank.ie/publication/behaviour-and-culture-report
[23] AIB, BOI, KBC, Permanent TSB and Ulster Bank

The Minister for Finance consulted the ECB on the Bill. The ECB stated that it '*strongly welcomes the measures … regarding the individual responsibilities of senior persons, including management board members and key function holders.*'

The Bill will provide for the:

- Introduction of a Senior Executive Accountability Regime (SEAR) for management in specific sectors (credit institutions, investment firms, insurance undertakings in short those which have a customer focus) which places obligations on firms and senior individuals within them to set out clearly where responsibility and decision-making lies;
- Introduction of Conduct Standards for individuals and all regulated financial services firms to provide for statutory powers to set and impose binding and enforceable obligations on all Regulated Financial Service Providers (RFSPs) and relevant individuals working within them with respect to expected standards of conduct;
- An enhanced Fitness & Probity Regime which includes provisions to enhance the Fitness & Probity regime to ensure the effective operation of the regime and the ability of the regime to support the Central Bank's proposed individual accountability framework and the conduct standards for individuals and firms;
- Breaking the 'Participation Link' to allow the Central Bank to take action against either a firm or an individual where a contravention of financial services legislation has been proven.

Second Stage of the Bill in the Dáil took place on 18-19 October 2022 and Committee Stage is expected soon.

3.3. Technology driven change

The term 'digital finance' is often used to describe the impact of new technologies on the financial services industry. It includes a variety of products, applications, processes and business models that have transformed the traditional way of providing banking and financial services. While technological innovation in finance is not new, investment in new technologies has substantially increased in recent years and the pace of innovation is significant.

Consumer and SMEs increasingly interact with their bank using mobile technology. They make payments, transfer money and make investments using a variety of new tools that were not available a few years ago. Artificial intelligence, social networks, machine learning, mobile applications, distributed ledger technology, cloud computing and big data analytics have given rise to new services and business models by established financial institutions and new market entrants.

The issue of financial and digital technology was considered by the OECD in a 2018 report[24] that noted the important role advances in telecommunications and computing technology play in improving quality and processing speeds, as well as helping lower information and transaction costs. These developments impact both providers and users of financial products and services.

Interestingly, the OECD noted that in the context of retail clients, product needs remain largely unchanged, comprising 'some type of current account, loans to fund large purchases and investments, financial advice and for remittance capabilities and money transfers' and what is changing 'from the viewpoint of end-users, is how the needs are met.'

An overview of the technologies that are key to innovation in financial services is provided in Appendix 3**,** but including big data analytics, cloud computing and storage, artificial intelligence and biometric technologies. For example, within financial services:

- Big data can be used to develop more granular pricing strategies (due to more broadly based assessments of individual customers' risk profiles), tailor promotional materials and enhancing internal risk management (for example, improved fraud detection).
- Cloud computing and storage increases financial institutions' capacity to collect and analyse data, which in turn supports the use of data analytics in both customer facing and internally-focused activities.

Digital technologies are enabling innovation in retail banking financial services, as follows:

- Payments. Innovation in payments is not new, and represents the most basic application of digital technologies. This started with physical cards and has now advanced to instant payments that facilitate electronic retail payments in real time and can make funds available for use by the recipient in less than 10 seconds.
- Advice and planning. Digital technologies underpin developments in advice and planning across a myriad of activities. Uses include supporting consumers with budgeting, keeping track of their spending, and helping consumers to save. Digital platforms can also help compare financial products, through the use of comparison platforms. Digital platforms also provide a means of financial education.
- Lending and funding. Digital technology has facilitated the evolution of new lending and funding models to make credit accessible to consumers and SMEs that traditionally may have had difficulties accessing credit via traditional channels. Furthermore, big data has also provided additional information to support credit assessment by lenders. In this regard, credit scoring models are now incorporating non-traditional variables, such as social networks, to refine scores to better represent an individual's risk characteristics.

[24] OECD 2018: Financial Markets, Insurance and Pensions Digitalisation and Finance: https://www.oecd.org/competition/financial-markets-insurance-and-pensions-2018.htm this section draws heavily on this report.

- Cybersecurity. Digital technology is both a source of risk and an enabler of greater security in digital delivery of financial services. For example, more robust data encryption is providing better security, while biometric technology can enhance identify verification and authentication. Improved data analytics capabilities provides the capacity for increased identification of irregular patterns and to pinpoint fraud. Nonetheless, consumers regularly cite concerns regarding online fraud and misuse of personal information as reasons for their cautious approach to digital banking services.
- Operations. Improvements in technology have greatly enhanced the effectiveness and efficiency of operational processes, as well as reducing operational costs, as manual processes are automated. More sophisticated uses are increasingly possible, for example, supporting credit decisioning and customer due diligence compliance.
- Communications. Technology is also influencing how financial institutions communicate with their customers and how products are marketed. For example, online advertisements can be targeted as technology draws conclusions from people's online behaviour and browsing habits.

While technology, once deployed effectively, can deliver significant operational efficiencies, in the context of retail banking services, two key considerations are:

- Accessibility – while it can be positive for customers who found branch-based banking a challenge, digital banking is not for everybody and financial exclusion is a key concern. The transition away from full-service, well-resourced branches is presenting challenges for individuals who lack the connectivity and / or the technical skills or knowledge to engage digitally.
- Retail banking business model – historically the larger the bank (in terms of customers and balance sheet), the larger its branch network and cost base, whereas in a digital context, while the fixed costs associated with technology are significant, marginal costs are typically far lower and therefore scaling up profit generating activities is significantly more beneficial from an earnings perspective.

The positive and negative aspects of speed, automation and privacy and transparency are also relevant.

While outside the scope of this Review, a related matter on the subject of digitalisation is the potential for Central Bank Digital Currencies. In October 2020, the ECB published a report on a digital currency[25], which included examining the idea of a 'digital euro'. The digital euro would be a central bank liability, offered in digital form, for use by citizens and businesses for their retail payments. The ECB is currently in an investigation phase which started in October 2021 and is expected to conclude in October 2023. While we await the outcome of this work, it is clear that a digital euro, if launched, will have an impact on retail banking that will require

[25] https://www.ecb.europa.eu/euro/html/digitaleuro-report.en.html

careful examination. Separately, the European Commission's work plan for 2023[26] includes a policy objective entitled, 'strengthening the role of the euro' which includes a legislative proposal/impact assessment of a digital euro.

3.4. Impact on the sector

TRADITIONAL BANKS

Technological innovation has allowed traditional banks to reduce operating costs, reduce staff numbers, reduce the size and scale of their branch and ATM networks, all of which has been beneficial from a cost perspective. However, implementing such extensive and fundamental change has proven challenging, and has required substantial and ongoing IT investment.

Digital transformation has also required traditional banks to change the profile of skills required at all levels of their organisations, as the sources of competitive advantage are ever-increasingly influenced by exploitation of the digital enablers mentioned above.

Impediments to fully leveraging the benefits that should accrue from their technology investments, coupled with the need for further enhancements to their end to end IT systems, mean the traditional banks have yet to fully implement digital transformation. As a result the traditional banks are being challenged to compete effectively with newer providers who have not had to migrate from legacy systems or to re-invent their business models/delivery channels.

Given the full service nature of the traditional banks' consumer offerings, work to re-engineer fully effective digitally enabled end-to-end processes, while ensuring high standards of customer service delivery is ongoing and has yet to meet the expectations of some customers. This could partly explain why digital savvy customers continue to visit branches.

A key challenge for the traditional banks is responding to the rapid changes in retail banking delivery

Also, technology enabled innovation requires ongoing investment as technology continues to evolve and therefore all providers, including traditional banks, are faced with the need for regular investment and further cycles of change implementation. It is difficult to envisage a return to the historic delivery model of retail banking products and services, which was based largely on relationship banking, in-person branch delivery, large branch and ATM networks and a model where individuals and SME generally used a single bank as a 'one stop shop' for their banking services.

[26] https://eur-lex.europa.eu/resource.html?uri=cellar%3A413d324d-4fc3-11ed-92ed-01aa75ed71a1.0001.02/DOC_2&format=PDF

A key challenge for the traditional banks is responding to the rapid changes in retail banking delivery from firms whose business models are founded on creativity and innovation and who, enabled by state of the art technology, can deploy new products and enhanced product features to the market at speed.

DIGITAL BANKS

Digital banks are new firms with business models based on digital technology delivered to customers via mobile applications. Those currently operating in Ireland have a narrower product offering (for example none offer mortgages and their focus is on payments rather than deposits or lending), and while they are making inroads into the market it is too early to determine the extent to which they will take market share from the traditional banks and become customers' primary bank. The digital banks could potentially become customers' preferred provider for certain products/services, such as payments and foreign exchange due to ease and speed of delivery, plus lower cost.

If they are to become the 'one stop shop' they will need to expand their product ranges. Their key source of competitive advantage is their ability to leverage state of the art technology to deliver core banking products digitally. This results in swift delivery, attractively priced products and user-friendly add on features (e.g. budgeting, monitoring spending). In substance, there are no material differences between digital and traditional banks core products, and the traditional banks are also innovating to develop user-friendly apps and online services.

Relative to the traditional banks, digital banks have significantly lower cost bases and their resourcing mix has a greater focus on management and staff with technological skills. As their businesses are mostly in the development phase, their success to date is being measured in customer numbers and ability to raise funding in the private equity markets.

All the digital banks operating in Ireland are in private ownership and it remains to be seen how their investors monetise their investments in these ambitious ventures. As digital banks expand their product range, advances into the provision of credit will mean funding and capital requirements become relevant for them. To operate in the medium to long-term, building sustainable levels of profitability will be important.

NON-BANKS

Combined, the non-banks provide credit products such as mortgages, consumer credit, hire purchase (HP), leasing, real estate financing and invoice discounting. The non-banks generally have lower cost bases and in relative terms their more niche focus means staff typically have strong subject matter expertise. Thanks to their use of digitally enabled innovations to offer enhanced products, services or delivery methodologies to customers (consumers and SMEs), some non-banks are challenging the market position of the traditional banks and, to a lesser extent, the credit unions (particularly in the area of smaller personal

loans). Mortgage lenders primarily use the broker channel. The non-bank providers of retail banking products and services generally provide a smaller suite of products, which often means their systems can be more streamlined. In addition, some newer entities are not impacted by legacy IT infrastructure, and as such IT investment and deployment has not been as big a factor as it has been for the traditional banks.

3.5. Impact on customers

The pace and scale of change has had a material impact on all users of retail banking products and services. As far back as 2016, Eurostat reported that almost 60% of European internet users used online services for internet banking.[27] In addition, in 2015 it was reported that for most European countries, digital servicing was overtaking branch servicing.[28] COVID-19 accelerated this migration further, as customers were forced to shift to online banking due to worldwide lockdowns. The European banking sector saw an increase of 23% in customers using digital banking services for the first time.[29]

Similarly, with regards to cash and contactless payments, the COVID-19 pandemic brought about significant changes in the use of cash. The Bank of International Settlements (BIS) highlighted in their 2020 annual report that the use of contactless payments almost doubled during the onset of the pandemic in developed economies. The Central Bank payment statistics show similar trends.

In relation to customers migrating away from accessing banking services via a branch, in its 2021 report on the Future of Retail Banking in Ireland,[30] the BPFI commented:

> *'Over the counter transactions in Irish retail bank branches have fallen by over 45% in the past three years. In contrast, there has been an immense rise in online and mobile banking activity, with overall digital payments rising by a significant 65% during the same period.'*

The transition to digital is a global phenomenon and is reflective of the evolution of banking throughout the developed world. Changes have both positive and negative impacts for bank customers, some of which are outlined below:

- ✓ Improved access as customers can access products and services remotely on a 24 hour basis.

[27] Archive: Internet access and use statistics - households and individuals - 2016 edition: https://ec.europa.eu/eurostat/statistics-explained/index.php?title=Category:Archive_-_digital_economy_and_society
[28] https://www.bankingsupervision.europa.eu/press/speeches/date/2018/html/ssm.sp180606.en.html
[29] https://www.bankingsupervision.europa.eu/press/speeches/date/2021/html/ssm.sp210921~78d06f2393.en.html
[30] https://bpfi.ie/publications/bpfi-ey-the-future-of-retail-banking-in-ireland-report/

- ✓ In some instances innovation and competition from new providers has positively influenced product pricing.
- ✓ Add-on services such as budgeting and spending tools are beneficial for financial management, as are comparison websites.
- ✓ Remote access facilitates better financial inclusion for those members of society who could not easily access a branch.
- ✓ For certain products and services, automated processes result in speedier delivery – e.g. instant payments.
- ✓ New providers of credit for consumers such as Buy Now Pay Later (BNPL) have the potential to be a positive force in the market, however ensuring that these products are not a mechanism for over-indebtedness is an important consideration.
- ✗ Digital access to finance can require consumers and SMEs to develop new technical skills and expose them to new risks, including cyber risk, which must be considered in the context of consumer protection, financial inclusion and financial literacy.
- ✗ Reductions in the number of branches / services provided in branches have negatively impacted customers who do not / cannot access services digitally and have resulted in longer journeys to the nearest alternative branch, or are potentially leading to financial exclusion. This was clearly evidenced in the public reaction to AIB's proposal to remove cash services from 70 of its branches, notwithstanding the fact that similar services were to be provided by local post offices.
- ✗ The reduction in access to and use of cash is a concern for consumers and small businesses, many of whom are reluctant to migrate fully to non-cash payment methods. In addition, cash is a critical component to resilience of the system as it is the main fall-back in the event of significant system outages.
- ✗ Some consumers, including some SMEs, find branch services in the traditional bank branches have been reduced and they would prefer to engage directly with a suitably qualified member of staff, rather than the branch staff directing customers to make contact with centralised call centres.
- ✗ Continuous implementation of technological innovations presents challenges for consumers who need to stay on top of such changes to ensure the services they are availing of can be used safely and effectively.

3.6. Open banking potential

Open Banking allows consumers to share account information and make payments through regulated Third Party Providers (TPPs).[31] Open banking in the EU is enabled by the Payment Services Directive (PSD2), which allows banks to open up access to customer payment accounts to two new categories of third party payment services providers:

- Payment Initiation Service Providers (PISPs)
- Account Information Service Providers (AISPs)[32]

Access is via an Application Programming Interface (API) and requires the customer to consent to the third party accessing their details and is not automatic. PSD2 requires that all such third-party payment services providers be authorised and regulated by the relevant authorities.[33]

Under the European Commission Digital Finance Strategy, the PSD2 is viewed as an important step towards the sharing and use of customer-permissioned data by banks and third party providers to create new services.[34]

PSD2 laid the ground for open banking, opening up access to customers' payment accounts data and enabling third-party information and financial service providers to reuse this data with the customer's agreement: the general purpose of this data re-use was to offer competing financial services or information services, such as comparison tools and data aggregation across several providers.[35]

Open finance, while similar to open banking, is broader and goes beyond the scope of payments account data. In relation to open finance, the European Commission's digital finance strategy noted that open finance has the potential to lead to better financial products, better targeted advice and improved access for customers, in addition to greater efficiency in business-to-business transactions.

The Commission launched a review in 2022 to gather evidence on the application and impact of PSD2, and to inform the Commission's work on open finance.[36] The Digital Finance Strategy notes that a balanced regulatory framework for the sharing of data on financial products will support the financial sector in fully embracing data driven finance, and effectively protect data subjects, who must have full control over their data.[37] By 2024, the EU should have an open

[31] Irish Retail Payment Forum meeting 18 February 2019: https://www.centralbank.ie/financial-system/payments-and-securities-settlements/irish-retail-payments-forum/meetings-of-the-irpf
[32] https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32015L2366&from=EN
[33] https://www.ecb.europa.eu/paym/intro/mip-online/2018/html/1803_revisedpsd.en.html
[34] https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:52020DC0591&rid=3
[35] https://ec.europa.eu/info/sites/default/files/business_economy_euro/banking_and_finance/documents/2022-psd2-review-open-finance-consultation-document_en.pdf
[36] https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/13331-Payment-services-review-of-EU-rules/public-consultation_en
[37] https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:52020DC0591&rid=3

finance framework in place, in line with the EU Data Strategy, the upcoming Data Act, and Digital Services Act. This will be coordinated with the review of the Payment Services Directive.[38] As of November 2022 there were five Account Information Service Providers and 23 Payment Institutions registered with the Central Bank.[39]

Uptake of open banking in Ireland has been slow due to a number of factors including the impact of legacy systems, challenges around harmonising of APIs and the relatively lower number of third-party providers operating here.

3.7. Impacts for financial stability, consumer protection and competition

FINANCIAL STABILITY

From a financial stability perspective, concentration risk is reduced when the market is served by a greater number of more diverse providers. Accordingly, the emergence of new competitors in the retail banking sector is generally a welcome development, albeit the positive impact is counter-balanced by the imminent departures of KBC and Ulster Bank.

While greater use of technology has certain advantages, as already outlined, sole dependency on technology-enabled banking brings risk, as no system is failure-proof. Minimising the impact of systems failures, should they occur, is a key regulatory requirement on regulated firms and their service providers – strong resiliency and effective fall-back mechanisms are areas of focus.

A further consideration in the context of financial stability is the continued provision of retail banking products and services through the economic cycle. While recognising that credit supply generally contracts in response to a more challenging economic environment, this is impacted further where lenders raise funding in the wholesale markets, as typically these markets respond rapidly to changes in economic sentiment. In this regard, where a firm's funding model is based on access to market finance, raising debt is likely to be more challenging in times of market stress, and therefore providers who rely on such funding may find it difficult to obtain new funds or refinance existing finance during an economic downturn. This could impact on their ability to fund existing lending (e.g. long-term mortgages) or to continue to provide credit to creditworthy customers.

An over-reliance on non-domestic providers of retail banking products and services could also have implications for financial stability

[38] https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52020DC0591&from=EN
[39] https://registers.centralbank.ie/DownloadsPage.aspx

An over-reliance on non-domestic providers of retail banking products and services could also have implications for financial stability, as the impact of decisions to fundamentally change how they participate in the market or, in extremis, a decision to leave the market may not give due consideration to the consequences for the users of retail banking products and services in Ireland and the Irish economy.

The extent to which the overall market is dependent on technology also has potential financial stability implications, as should an outage occur across the main providers of banking products and services for an extended period of time, it would be almost impossible for the economy to function effectively.

CONSUMER PROTECTION

Developments in technology in the retail banking sector have largely been positive – providing greater choice and more modern delivery with the growth in digital banking. Key concerns regarding the disruptive forces of technology are:

- Financial exclusion of those who choose not to, or who cannot effectively access digital services.
- Greater complexity in accessing services as many processes are not as consumer friendly as is required by some consumers.
- Poor customer outcomes due to inadequate supporting customer service where issues arise.
- Increased digital security risk as customers migrate more of their banking activity to digital channels.
- Customer data – ownership, usage and potential privacy issues.
- Algorithmic decision-making, where errors or biases go undetected (e.g. inaccurate risk profiling) which could cause detriment to consumers.

COMPETITION

New competitors have brought innovation to the Irish market, particularly in terms of digital payments and increased choice for SMEs seeking credit. While it is too early to determine what the result of the current transition within the Irish retail banking sector will be, it is clear that digital delivery continues to grow. As evidenced by the number of customers Revolut has attracted in a relatively short period of time, there is demand within the Irish market for innovative products and services.[40]

The challenge for newer providers is the dominant position of the traditional banks, generally very low switching levels and the fact that the traditional banks continue to challenge strongly to retain their market shares. A cohort of the newer providers are likely to remain in the Irish

[40] Per recent press coverage Revolut has 2 million Irish customers.

market and it is expected that additional providers will enter (noting that passporting within the EU provides easy access to the market for EU and EEA authorised firms).

Competition in the retail banking sector is addressed in more detail in the chapter on Competition.

4. The traditional banks in Ireland

As outlined in the chapter on Forces of Change, developments in technology and regulation have enabled transformation in how retail banking products and services are delivered, as well as innovations in product features and the types of firms providing products and services. Arising from these changes, as well as an increasing role by the credit unions and An Post, there is a growing trend whereby consumers and SMEs are placing less reliance on the traditional banking model, whereby their bank is a 'one stop shop' for all their banking needs. Despite the new and welcome competition from non-banks and digital banks, and the innovations and greater customer choice they provide, the traditional banks remain the dominant providers of retail banking products and services in Ireland and the Review Team expects this will continue to be the case for at least the next decade.

In the context of the number of traditional banks now reducing to three, as commercial firms, it is important they are profitable, viable and have sufficient capital so that they can continue to meet the needs of all stakeholders, including consumers and SMEs. To support the economy through different economic cycles, all banks must generate sufficient profits so they have the capital necessary to support credit growth, fund ongoing investment in the business (e.g. IT enhancements, including digitalisation), and ensure an appropriate return for investors, through dividends and share price appreciation. In addition, a strong track record in delivering attractive shareholder returns, either through share price and/or paying dividends, is an integral part of the investment case for any bank, should it need to raise fresh capital from the market.

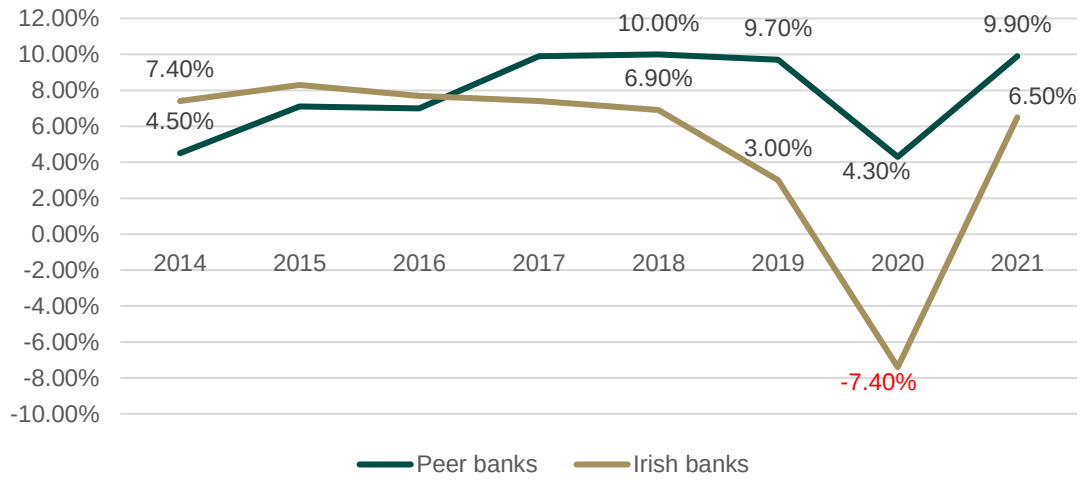
It is important that banks are profitable, viable and have sufficient capital so that they can continue to meet the needs of all stakeholders, including consumers and SMEs

4.1. Profitability

Since the GFC, sustained progress has been made to repair and restore the financial positions' of the traditional banks. They have much stronger capital positions and more stable funding models. While the traditional banks returned to profit a number of years ago, returns are still below expected norms. In 2021, the aggregate return on equity (ROE)[41] for the three remaining traditional banks of 6.5% was below shareholder expectations, which is generally regarded as being 10%+. In addition, ROE underperformed European peer banks for the same period, which was close to 10%.

[41] ROE is calculated as Profit after Tax/Average Shareholders' Funds

Figure 2 - Return on equity – Irish traditional banks versus European peer banks



Source: Department of Finance calculations from banks' annual reports.
Irish banks included are AIB, BOI and PTSB

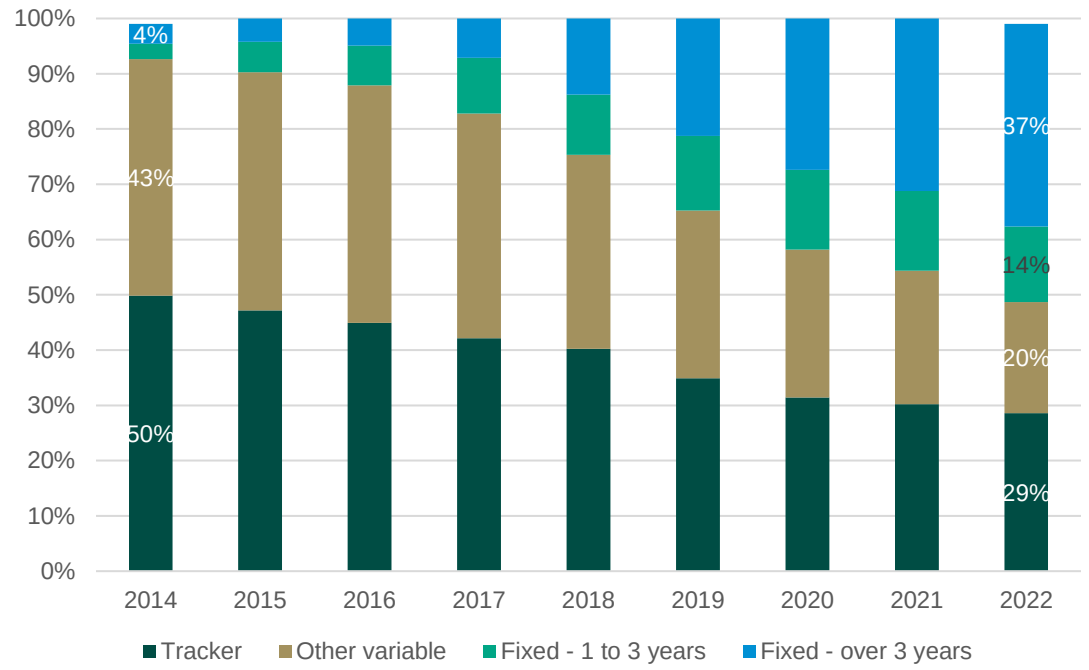
STRUCTURAL FACTORS

There are a number of structural factors which go a long way towards explaining the underperformance of the Irish traditional banks.[42]

- The low/negative interest rate environment over the past decade adversely affected the banks' net interest income. Although the interest rate environment impacted all banks in the Eurozone, it was particularly acute for Irish banks due to their greater reliance on interest income as a percentage of total income, coupled with lower returns on tracker mortgage portfolios which, although reducing, still represent a significant percentage of total outstanding mortgage balances at end 2021 (Figure 3). In 2021, aggregated non-interest income for AIB, BOI and PTSB accounted for c. 25% of total income, compared to c. 39% for European peer banks (Figure 4).

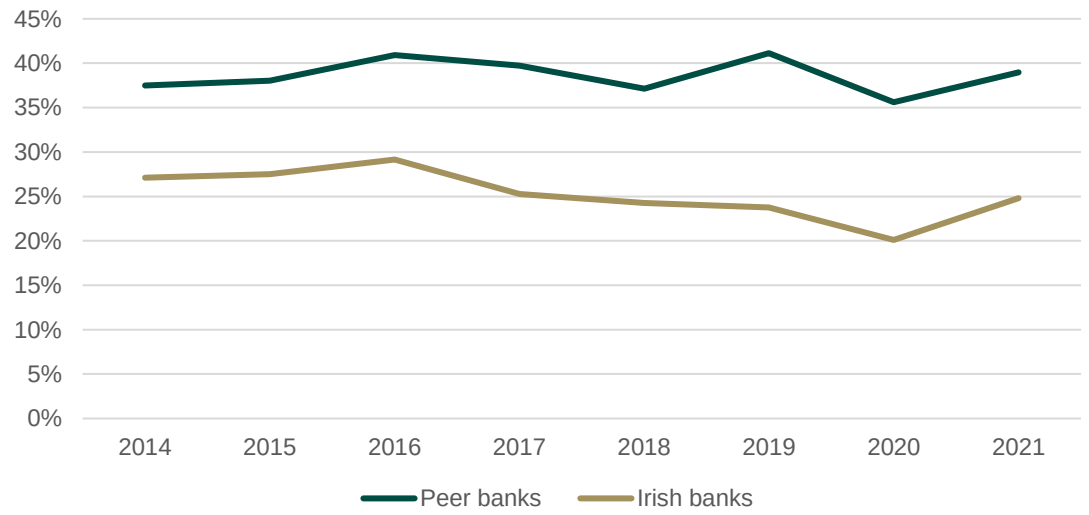
[42] In calculating ROE, the impact of the low interest rate environment and the cost base is reflected in the numerator – or, Profit after Tax. The impact of the higher capital levels is reflected in the denominator – or, Average Shareholders' Funds.

Figure 3 - Composition of the traditional banks' mortgage balances



Source: Central Bank

Figure 4 - Non-interest income ratio – Irish banks versus European peer banks

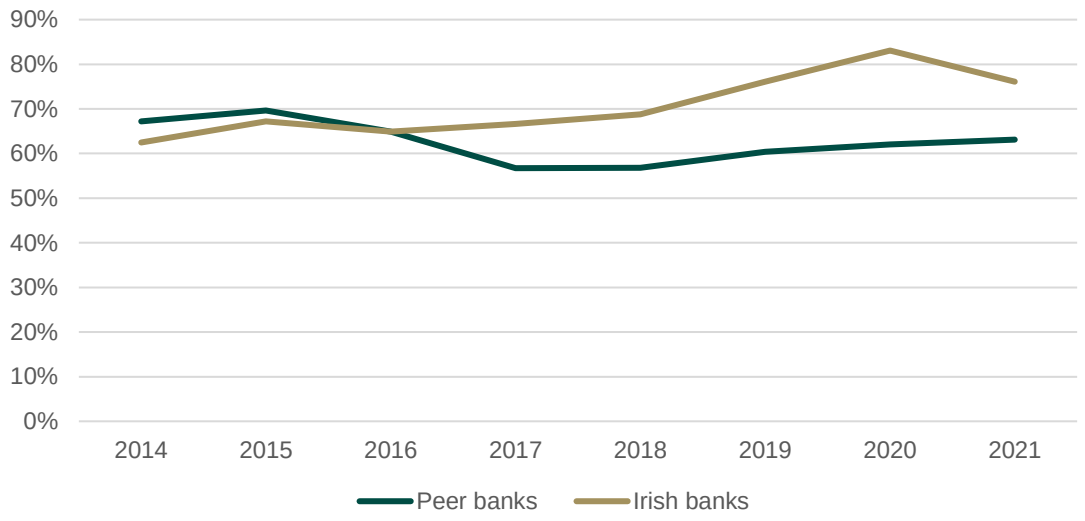


Source: Department of Finance calculations from banks' annual reports.
Irish banks included are AIB, BOI and PTSB

- Irish banks, like peers across Europe, have had a strong focus on reducing operating costs in order to improve profits. Cost saving initiatives have included reducing

headcount, rationalising head office functions, scaling back branch networks, greater use of automation/streamlining operations, and in more recent years, increased use of digital technology. However, compared to European peers, Irish banks' cost income ratios are high, due to the higher pro-rata cost base of the Irish banks. Banking is a scale business with significant fixed costs including infrastructure, digital investment, regulatory costs and levies. Arising from the modest size of the Irish market, and the deleveraging since the GFC that has reduced banks' balance sheets, costs are shared over a smaller pool of assets, which in turn generate lower revenues.

Figure 5 - Cost to income ratios – Irish banks versus European peer banks



Source: Department of Finance calculations from banks' annual reports.
Irish banks included are AIB, BOI and PTSB

- Due to the higher risk levels associated with their loan portfolios, relative to European peers, Irish banks are required to hold relatively higher levels of regulatory capital. Factors that determine regulatory capital include the likelihood of default, and the likely losses when a loan defaults. For Irish lending, likely losses are influenced by the loss experience associated with pre-GFC lending; and the longer timeframe in resolving distressed debt, including collateral recovery.

RECENT DEVELOPMENTS

There are a number of recent developments that should support the banks to achieve sustainable levels of profitability in the coming years and thereby strengthen their ongoing viability. The main influencing factors are:

- The acquisitions of the Ulster Bank and KBC portfolios will improve efficiency and scale of the three remaining banks. For AIB and BOI, the acquisitions of Goodbody

Stockbrokers and Davy Group will contribute further, in addition to providing diversification away from interest income.

- Following a period of relatively static balance sheets, organic loan growth has also been in evidence, led mainly by strong mortgage demand. Notwithstanding the more challenging external environment, continued growth in the mortgage market is expected.
- The return to a more normalised interest rate regime is expected to generate a material growth in income.[43]

Notwithstanding the positive impact of these developments, given the more challenging external environment and the ongoing transition occurring in retail banking it is important that the sector, including the banks, is agile and forward looking. Taking advantage of opportunities that arise must also be balanced with ensuring the sector is not blind-sided by emerging new risks.

4.2. Funding and liquidity

The traditional banks are funded by a mix of customer deposits and funds raised in the wholesale markets (including debt issuance and securitisation). While it is good for a bank to fund itself utilising a mix of funding sources, it is important that there is a heavy bias towards customer deposits, which are regarded as more stable (or 'stickier') in times of market stress. Banks internationally, as well as some in Ireland, encountered difficulties in this regard at the outset of the GFC due to an over-reliance on wholesale markets. This contributed to the exceptional State support for the covered banks[44] including emergency liquidity assistance in the form of funding from the monetary authorities, and liability guarantees from the Irish State.

Following the failure of many banks to adequately measure, manage and control their liquidity risk in the lead-up to the GFC, the regulatory authorities introduced two liquidity standards as part of post-GFC reforms - the Liquidity Coverage Ratio (LCR), and the Net Stable Funding Ratio (NSFR). These ratios were introduced to ensure banks could meet their short term liquidity requirements and were funding their lending activities with more stable sources of funding on an ongoing basis.

For both of these liquidity metrics, banks are required to maintain a ratio of no less than 100%. Table 4 shows that at 31 December 2021 each of the three remaining Irish banks held liquidity positions well in excess of the minimum requirements.

[43] In its recent Financial Stability Report, the Central Bank commented that "Potential interest rate increases, while potentially leading to repayment challenges for some borrowers, are on net expected to be beneficial for bank profitability, primarily through lending margins."
https://www.centralbank.ie/docs/default-source/publications/financial-stability-review/financial-stability/financial-stability-review-2022-i.pdf?sfvrsn=3e74961d_5

[44] The covered banks were AIB, Anglo Irish Bank, BOI, EBS, INBS and IL&P (PTSB).

Table 4 - Banks - liquidity ratios as at 31 December 2021			
	Liquidity Coverage Ratio	Net Stable Funding Ratio	Loan-to-Deposit Ratio
AIB	203%	160%	61%
BOI	181%	144%	82%
PTSB	274%	170%	75%
Regulatory requirement	>=100%	>=100%	n/a
Source: Banks annual report			

Although there is no regulatory requirement to maintain a loan-to-deposit ratio (LDR) at a certain level, this metric is a common indicator that helps assess how banks are funding their lending activities. The LDR relates to the total loans granted by a bank as a percentage of total deposits which are regarded as a stable funding source.

As part of the EC-ECB-IMF bail-out agreement a sustainable LDR for the aggregate domestic banking system was assessed as being no more than 122.5%.[45] In recent years, due mainly to strong growth in deposits and modest growth in loan portfolios, the traditional banks ended 2021 comfortably within this ratio.

4.3. Capital

A key aspect of the measures taken in response to the financial crisis was the establishment of a robust framework for setting minimum capital requirements for banks. Capital is a key ingredient for safe and sound banks. Banks take on risks and may suffer losses if the risks materialise. To stay safe and protect depositors' funds, banks have to be able to absorb such losses and keep going in good times and bad. That's what bank capital is used for.[46]

Minimum capital requirements are set for a number of metrics including Common Equity Tier 1 (CET1), Tier 1, and Total Capital, with different types of capital qualifying for inclusion under each metric. In addition, banks are required to maintain a minimum Leverage Ratio of 3%.[47]

Minimum capital requirements are set by the regulator as part of a bank's annual Supervisory Review Evaluation Process (SREP). In terms of the ability of the banks to absorb shocks or

[45] The LDR at the time of agreeing the Financial Measures Programme was c.180%
[46] https://www.bankingsupervision.europa.eu/about/ssmexplained/html/hold_capital.en.html
[47] **Appendix 4** provides more detail in relation to the different components which are included in a bank's capital requirements.

unexpected losses, each of the three banks comfortably exceed the regulatory capital minima (see Table 5). Notwithstanding this, in its recent Financial Stability Review, the Central Bank commented in relation to capital that 'headroom is expected to decline in the coming years due to portfolio transfers arising from the exit of two retail banks.'[48]

Table 5 - Banks' Capital Ratios – 31 December 2021

	AIB		BOI		PTSB	
	Actual	Minimum Required	Actual	Minimum required	Actual	Minimum required
CET1	19.2%	10.2%	17.0%	9.77%	16.9%	8.94%
Total capital	24.2%	15.01%	22.3%	14.25%	21.8%	13.95%
Leverage ratio	8.6%	3.0%	6.6%	3.0%	7.1%	3.0%

Source: Bank disclosures.
Minimum required ratios for Common equity tier 1 and Total capital are before Pillar 2 Guidance (P2G) which is not disclosed by the banks, in line with regulatory preference.

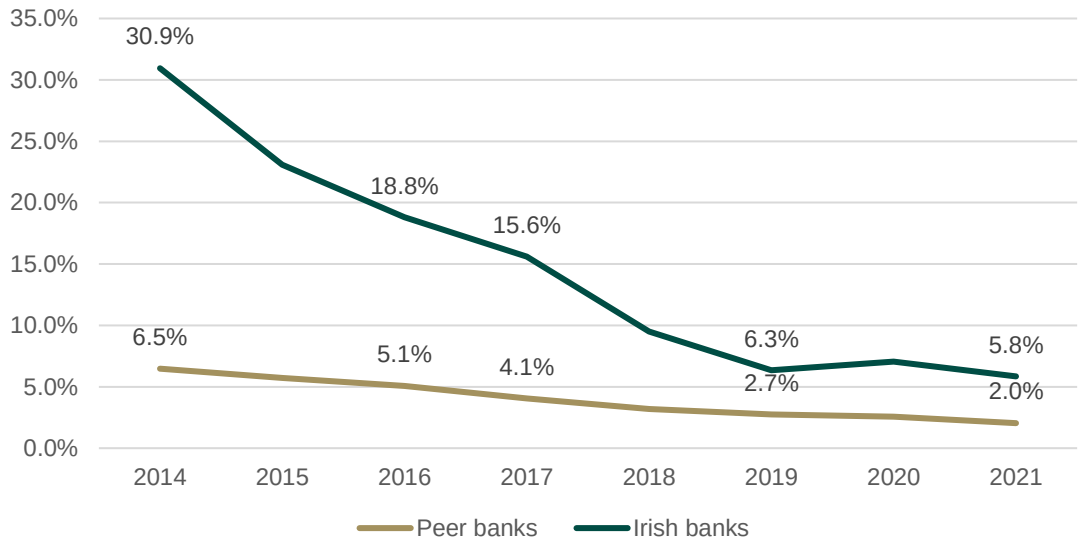
The larger banks in Europe participate in a stress test carried out by the European Banking Authority (EBA)[49] once every two years. Although the stress test does not define a pass/fail threshold, it is an important input for the requirement to hold additional capital – the Pillar 2 assessment – as part of the annual SREP. AIB and BOI were included in the most recent test that took place in 2021. The test assesses the impact of a very severe stress scenario on the participating banks' CET1 capital and leverage ratios over a three year period. Commenting on the results of the stress tests, the Central Bank stated that while they 'highlighted vulnerabilities for Irish banks, the results are broadly consistent with the findings of the Central Bank's own forward looking assessment of Irish banking resilience that the Irish banking system has sufficient loss-absorbing capital to absorb material adverse shocks.'[50]

4.4. Non-performing loans (NPLs)

Since the GFC, the traditional banks have made significant progress in reducing the NPL ratio to a more sustainable level. As at 31 December 2021, the weighted average NPL ratio for the traditional banks stood at 5.8%,[51] compared to a peak of 32% in 2013.[52] The progress in reducing NPLs to the current level reflects a supportive economic environment, as well as measures taken by the banks to resolve or restructure problem loans, together with a number of loan portfolio sales.

[48] https://www.centralbank.ie/publication/financial-stability-review/financial-stability-review-2022-i
[49] The test comprised 50 banks from across the European Union and EEA, which make up 70% of the EU banking sector assets.
[50] https://www.centralbank.ie/publication/financial-stability-review/financial-stability-review-2021-ii
[51] The retail banks comprise AIB, BOI, KBC, PTSB and Ulster Bank.
[52] https://www.centralbank.ie/news-media/press-releases/non-performing-loans-dg-ed-sibley21Sept2017

Figure 6 - Combined NPL ratio for the Irish banks



Source: Central Bank
Department of Finance calculations from banks' annual reports.
Irish banks included are AIB, BOI and PTSB

However, the weighted average NPL ratio of 5.8% at end-2021 for the Irish banks is still above the average for European peer banks, which stood at 2.0% (Figure 6). In its recent Financial Sector Stability Assessment of Ireland, the IMF commented as follows on the matter:

> *'The NPLs of retail banks remain above the EU average and these weigh on profitability, including via high risk weights. While much progress has been made in reducing bank NPLs since the GFC, progress has slowed down recently. Very long-term mortgage arrears (LTMA), some more than a decade, persist. A push to clear the final stock is needed, as well as steps to improve insolvency and collateral recovery procedures to see a meaningful drop in risk weights that are contributing to higher interest rates in Ireland than in EA peers.'*

LTMA is discussed in more detail in the chapter on Mortgages.

4.5. Outlook

In terms of the outlook for the traditional banks, as outlined above, much has been achieved in terms of profitability, capital, liquidity, cost management and business transformation. In the coming years profitability is likely to improve further due to a normalised interest rate

environment, scale economies from acquisitions, and further growth in loan portfolios. The banks have reasonable headroom on their regulatory capital and liquidity requirements, and due to multi-year investment and cost-saving programmes they have addressed many of the business model and IT risks that emerged in the years following GFC.

In terms of credit risk, loan portfolios are originated under more stringent credit policies and underwriting standards, NPL portfolios have been managed down significantly, and NPL ratios are tracking towards European norms albeit they have a way to go.

However, challenges remain in the context of newer, agile competitors, the requirement to meet customers' expectations regarding high standards of product and service delivery, addressing residual NPLs, particularly LTMA, and the less-benign external environment that has emerged during 2022. The latter is likely to lead to a deterioration in credit quality, with consequential impacts on future levels of loan loss provisions, and the need for experienced credit and relationship banking staff to engage directly with customers facing repayment challenges.

While the banks appear well-placed as they come into 2023, continued focus on business activities and risk management, and remaining alert to the ever-changing environment are necessary if they are to generate the levels of sustainable profits required to assure their viability in the medium to long-term.

5. Competition

Effective competition in retail banking markets is good for consumers and SMEs. It can result in providers competing on price and innovation, which can help bring down the cost of retail banking products and services as well as provide more choice due to new and better products being introduced to the market. Effective competition can also drive improved customer service standards as it ensures that consumers who are unhappy with the service that they are receiving can switch to an alternative provider.

Competition can also be important from a financial stability perspective. If there are many smaller firms operating in the market offering products and services, the failure of any one smaller firm may have less of an impact on the economy, as they may not need to be bailed out as happened to bigger firms during the GFC. However, it is important there is a balance as bigger and stronger firms can have a better ability to absorb shocks.

In this chapter, the Review Team outlines its general assessment of competition in the retail banking sector in Ireland. For each of the products that are being considered as part of the Review, namely mortgages, SME credit, consumer credit, current accounts and deposit accounts, specific competition issues relating to those products are discussed in the relevant chapter in this Report.

5.1. Concentration

The retail banking sector in Ireland was already concentrated before the departure of Ulster Bank and KBC, whilst new competition in the market is increasingly fragmented.

Non-banks have entered the mortgage and consumer credit markets and digital banks have entered the current accounts market, though the digital banks have started to enter the consumer credit market. An Post and some credit unions offer current accounts, whilst An Post also offers credit to consumers. Many credit unions now offer mortgages and SME lending. These developments have resulted in a more fragmented competition landscape. No full-service bank has entered the Irish retail banking market in the past 15 years, whereas there have been multiple departures.

The entry of digital banks and non-banks into the retail banking markets, as opposed to full-service banks, means that customers may not be going to a single provider for all of their retail banking needs. Increasingly, consumers and SMEs are developing secondary relationships with the digital banks and non-banks.

The concentration level in a market does not in itself tell how well competition is functioning in that market, but it does provide an indication. Based on the most commonly used metric, the Herfindahl-Hirschman Index (HHI), Ireland's mortgage and primary personal current accounts

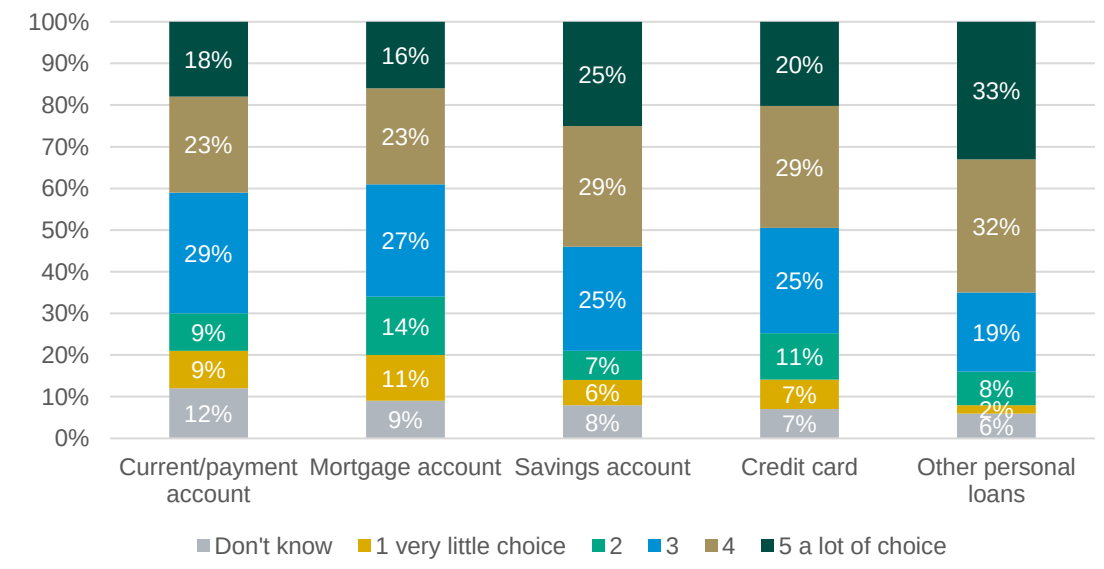
both have HHIs of around 2,600, which are well above the 2,000 that denotes a highly concentrated market.[53]

In the Public Consultation, the Review Team asked the question: 'Following the departure of Ulster Bank and KBC, do you consider that the level of competition in the retail banking sector will be appropriate and sustainable, bearing in mind population and market size in Ireland.'

Of those that responded, almost nine in ten said the level of competition was not appropriate and sustainable and just over one in ten said that it was. Where reasons were provided for their answers, most respondents focused on the fact that following the departure of KBC and Ulster Bank there will only be three full-service banks left in the Irish market.

The Consumer Survey points to less concern around concentration. The Consumer Survey asked how consumers rate product choice in each of the products under consideration. The responses varied from product to product, with the perception being that choice is more limited in mortgages and current accounts, whereas there is greater choice in other products such as personal loans, credit cards and savings accounts (see Figure 7).

Figure 7 - Perception of consumer choice in the market among product holders



Source: Department of Finance, Consumer Survey

The International Comparison outlines how Ireland, with five though soon to be three traditional banks, has fewer such banks than other countries. The UK has 67, Portugal 31, Canada 30, the Netherlands 20, New Zealand and Finland each have 13 and Lithuania has

[53] https://www.ccpc.ie/business/mergers/guidance-on-mergers/guidelines-for-merger-analysis/

12. However, in all these countries between two and five traditional banks dominate the retail banking sector, which is comparable to the situation in Ireland.

The departure of Ulster Bank and KBC from the Irish market provided the opportunity for a full-service bank to enter the market through an acquisition of an existing business or the purchase of the departing banks' assets. The fact no new entrant has come forward to take over the operations of these two banks and the departure of other foreign owned traditional banks since the GFC suggests policy formation for the retail banking sector should not presuppose the entry of a new large retail bank, even if such an event would be welcome.

Going forward, it is likely that the Irish retail banking sector will be served by the three traditional banks, a number of non-banks (including An Post), credit unions and digital banks. The scale of the activities of these different categories of providers is likely to differ from product segment to product segment. In addition, compared to the past, a number of providers (especially digital banks) are passporting services into Ireland from another EU/EEA Member State, all without having a physical branch presence.

With the market so concentrated, it is critically important that there continues to be effective competition between the existing providers in the market. The Review Team considered actions that could be taken to improve competition between the existing providers in the market, such as in the area of switching. These considerations are discussed further below.

5.2. Consumer choice

Within the range of providers that offer retail banking products and services in the Irish market, the Review Team considered the level of choice that exists for the products and services that are within scope of the Review, namely current and savings accounts, mortgages, SME credit and consumer credit.

In completing its assessment, the Review Team asked stakeholders, via the Public Consultation, whether there is an acceptable level of choice in the Irish market in relation to the range of providers, as well as the range of products they offer.

Whilst these issues are commented upon within the relevant product chapter of this Report, in summary the Review Team's assessment indicates the following:

Current accounts – the range of providers has increased beyond the traditional banks, offering more choice. There was evidence of product innovation that provides better outcomes for consumers. Product differentiation and innovation has tended to focus on a few key areas, principally the mobile app, ability to use instant payments, cost, as well as the speed and ease of opening an account.

Savings accounts – the choice of provider is narrow, however this is normal in all markets as regulatory restrictions only allow firms with a full banking licence and credit unions to hold deposits. Irish depositors also have the option to place their deposits with the State Savings schemes either directly or via the Post Office. With respect to product choice, as the traditional banks and credit unions both hold excess deposits, and considering the low interest rate environment that has prevailed for a decade, there has been no incentive for them to compete by developing or offering innovative and attractive product features, including competitive deposit interest rates. Rates available on State Savings also reduced over the decade, reflecting the trends in interest rates across the Eurozone.

Mortgages – the range of providers has increased beyond the traditional banks, offering more choice. There was evidence of innovation in the area of long-term fixed rates (more so in the non-banks) and green mortgages (solely in the traditional banks). There is evidence of more product choice in other jurisdictions, and the Review Team considers that lenders in Ireland could review mortgage offerings in these other jurisdictions and give consideration to further innovations in their existing product suite.

SME credit – there is significant choice of provider, though only the traditional banks offer the full suite of products to SMEs. Overall, there is a wide choice of both provider and product, and there is no objective evidence to suggest that the products and services that SMEs need are not available in the market. For SMEs who need an overdraft facility, the choice is however narrower and is limited to the traditional banks, though the credit unions may potentially expand their current account offering to businesses over time.

Consumer credit – there is a range of lenders supplying the different segments of the consumer credit market from credit cards, hire purchase and personal contract plans (PCPs), personal loans and BNPL. Similar to the SME credit market, there are a number of traditional bank, credit union and non-bank lenders providing products in each of the segments except for overdrafts. Low value loans are predominantly provided by credit unions and HCCPs.

5.3. Barriers to entry

In considering how levels of competition could be improved within the Irish market, the Review Team considered whether there were actual or perceived barriers to entry that may impede prospective entrants from establishing in Ireland, providing more choice for consumers and SMEs, whilst also recognising that financial services, and banking in particular, is a heavily regulated sector.

To inform its view, the Review Team asked, via the Public Consultation, whether there were ‘actual or potential barriers to entry that are resulting in less competition both in terms of product availability and product price.’ Of those that responded, circa seven in ten suggested barriers to entry existed, with the remainder suggesting they did not. The feedback obtained

primarily attributed the barriers to entry to low levels of profitability in the sector, the scale of the Irish market, the difficulties in recovering collateral, regulation, low switching rates and the dominance of the traditional banks.

As new entrants would enhance effective competition, it is important that inappropriate barriers to entry are addressed where they exist, and where it is possible, remove or address them. However, there are certain barriers, such as the relative small size of the Irish market compared to other jurisdictions that cannot be changed.

The Review Team also recognises that the reasons for regulating the sector are well-founded and broadly reflect international standards and best practice. The Review Team believes that the focus in these circumstances should be to ensure that prudent and efficient access to our market is provided to firms that identify a market opportunity they want to serve, who meet the regulatory requirements, and having gained access, that they have the opportunity to build scale through gaining market share from new opportunities as well as efficient switching processes.

The Review Team notes that the CCPC has required commitments from BOI in relation to its purchase of KBC's assets. These measures include a requirement that BOI make €1 billion available to some non-bank mortgage lenders to increase their funding capacity and a €1 million fund for distribution to companies involved in developing innovations in the mortgage market.[54] The Review Team calls on the relevant providers in the retail banking sector to utilise these funds.

SIZE AND SCALE OF THE IRISH MARKET

The size of the Irish market is small by international standards. Ireland has a population of 5.1 million and a forecast 2022[55] GDP of €499 billion, although the GNI figure of €261 billion is more representative of the domestic economy. Whilst both the population and the economy are growing and have a positive outlook, the simple reality is that for an economy of Ireland's size, there is a limit to the economic activity that can be created, and which providers of retail banking products and services can serve. The business models of potential and different entrants will vary, and for some they will depend on an ability

Whilst both the population and the economy are growing and have a positive outlook, the simple reality is that for an economy of Ireland's size, there is a limit to the economic activity that can be created

[54] https://www.ccpc.ie/business/ccpc-requires-commitments-from-boi-to-acquire-kbc-ireland-assets/
[55] https://www.gov.ie/en/publication/04fef-budget-publications/

to build to a significant scale and market share. Ireland may offer this opportunity to some firms, but for others, the commercial potential of the Irish market will simply be too small.

This is not to underplay the attractiveness of Ireland's market. There are opportunities in Ireland that firms have already identified, and in recent years, these firms have established or trade in Ireland and have built market share. In addition, Ireland has developed as a leading hub for international financial services firms and many have chosen to be authorised in Ireland, providing them with the licence they need to serve the Irish market should they want to.

EU passporting rules also allow firms that have an authorisation obtained within the EU or the EEA to sell their products or services to consumers in Ireland. However there are more firms authorised in Ireland than are choosing to serve the Irish market, and there are thousands of firms authorised in other EU jurisdictions that are choosing not to passport into the Irish market, even though there are no regulatory barriers.

In these circumstances, where the size of the market cannot be changed, there is a need to ensure that other barriers to entry are removed or managed efficiently, enabling firms that meet regulatory standards to efficiently enter our market, and when they are in our market, that they can build scale, including through efficient account switching processes.

REGULATION

It is sometimes suggested that regulation can act as a barrier to entry to firms wanting to enter the financial services market. However, the experience in Ireland, and which is similar throughout the developed world, is that firms offering financial services to consumers and SMEs can cause detriment to such customers where, for example, the customer is not made fully aware of the underlying risk in a product, or where products are mis-sold. In addition, excessive risk taking by large firms can cause financial stability issues such as those that materialised in Ireland and elsewhere during the GFC.

Banks are more regulated than other sectors as governments and regulators require them to maintain high levels of capital and meet high standards in order to protect deposits and the fact that larger banks can pose a threat to financial stability

For this reason, governments and central banks regulate financial services. Given the global and cross-border nature of many financial services, and lessons from the GFC, key elements of regulation have been determined at international level, including direction provided by the G7 and the G20 and work at the BIS, via the Basel Committee on Banking Supervision. Typically, sectors that pose the most risk are more regulated than sectors that pose less risk, and sectors that do not pose a risk to consumers, SMEs or financial stability, are not regulated at all. It is for this reason, for example, that banks are more regulated than other sectors as governments and regulators require them to maintain

high levels of capital and meet high standards in order to protect the deposits they hold on behalf of their customers and the fact that larger banks can pose a threat to national and sometimes international financial stability.

From a competition perspective, it is important that when governments or regulators decide to regulate, that the new regulation is proportionate to the risk it aims to manage, that it is applied equally to firms that are engaging in the same type of activity, and that the authorisation processes that are in place do not restrict access to markets where the firm meets the required regulatory standards.

Feedback obtained through some of the Public Consultation submissions suggested that the length of time, as well as the complexity of the authorisation processes in the Central Bank could act as a barrier to entry. In the Review Team's engagement with the Central Bank on this issue, the Central Bank outlined how they seek to ensure the entry of firms in an orderly way, supported by 'effective engagement and clear and efficient processes.' They outlined their important role in assuring consumers that 'regulated financial service providers and the individuals overseeing and managing firms meet applicable regulatory standards,' and outlined how this is 'key to promoting high levels of trust and confidence in the financial system.' Whilst restrained by confidentiality issues from discussing individual cases, the Central Bank outlined how licence applications can be progressed efficiently when the licence application itself meets the required standard, and when questions the Central Bank may raise are responded to quickly and adequately by the applicant firm.

In addition to its processes, the Central Bank outlined how its *Innovation Hub*, among other things, provides an ability for firms who are considering applying for a licence to discuss authorisation processes and to receive an informal view on how regulation might apply to their business. It also provides the Central Bank 'with early intelligence on innovations, especially where those innovations are developed outside of the regulatory perimeter.'[56]

Feedback was obtained as part of the Public Consultation that fintech providers and other firms could benefit by an expansion of the *Innovation Hub* to include a regulatory sandbox, which is a tool used by certain other regulators to facilitate companies enter their market in a safe and controlled way. A regulatory sandbox would enable firms test innovative financial products or new business models in line with a plan that is agreed with the regulator, who will monitor performance and ensure that all regulatory requirements are complied with.

Proportionate regulation

In the context of the more concentrated market that has already been discussed, it is important that the Central Bank continues to play a key role in ensuring good access to our market for

[56] https://www.centralbank.ie/docs/default-source/regulation/innovation-hub/innovation-hub-2021-update.pdf?sfvrsn=2

firms who have identified a market opportunity, which the firm believes it can satisfy, once such firms meet the required regulatory standards.

As already outlined, this must mean that good firms have frictionless access to our market when they meet the required regulatory standards, but it also means that financial regulators consider the costs and benefits of new or existing regulation in order to ensure it is proportionate, and does not inappropriately impact the proper and efficient functioning of the market, including its impact on competition. The assessment of the regulatory impacts - which takes account of the costs and benefits and considers potential unintended consequences - is a key aspect of good regulation.

Level playing field

If firms are competing in a market, posing the same risks to consumers and SMEs, and/or financial stability, it is appropriate that these firms are regulated in the same or similar manner. As regulation comes at a cost to those firms that are regulated, the application of regulation to some and not others within the same sector may confer a competitive advantage to firms that are not regulated.

In the course of its work, the Review Team considered whether regulation was being applied in a similar manner across the firms that provide products within the scope of the ToR. As outlined in the chapter on SME Credit, all non-banks offering credit to SMEs are not regulated in the same way, and the Review Team has made a Recommendation that this is changed so that a level playing field is established.

The Review Team recommends that:

Recommendation 5-1

With regard to its authorisations and approvals functions, the Central Bank should:

- continue to review its authorisation and approvals processes to identify how these might be improved. This should reflect the importance of a continued flow of high quality new entrants to the financial services markets, while also recognising the importance of gatekeeping activities in mitigating risks to protect consumers and the economy.
- provide guidance for firms on its authorisation and approvals processes to enhance clarity regarding its expectations, processes and timelines (including factoring in any pre-authorisation engagement);
- review the reporting of its authorisation activities. In particular, the Central Bank should enhance reporting of the overall timelines of firms going through authorisation and approvals processes; and
- continue to enhance its strategy and implementation to ensure that its regulatory approach is consistent with realising the benefits of innovation in financial services while ensuring risks are managed and mitigated. In this context, the Central Bank should conduct a detailed review of the Innovation Hub, including peer comparisons, to expand its impact and functionality. Consideration should be given to the types and benefits of regulatory sandboxes adopted in other countries.

SWITCHING

Well-functioning competitive markets depend on consumers being able to switch service providers, and between products, with relative ease. Where barriers to switching exist, such as complicated or time-consuming processes, consumers and SMEs will be deterred from switching. This can impede their access to the products and services that better suit their needs.

Low levels of switching, for whatever reason, can also act as a barrier to entry to providers who are considering entering a market. Low switching levels may lead the prospective new entrant to believe they cannot build scale in a timescale that merits entering the market.

Historically, switching levels in Ireland have been low, across the wide range of retail banking products. For instance, between 2014 and 2021, only 1.32% of current account holders switched providers.[57] In mortgages, in 2021 6.9% of mortgage holders switched providers[58] (these numbers may not be representative of a typical year as this was the year the Ulster Bank and KBC announced they were leaving the market). Further, the rising interest rate environment is likely to act as a further catalyst for switching. According to BPFI, in Q3 2022 non-purchase mortgage activity, which includes switching and top-ups totalled €1.3bn, an increase of 175.8% year on year.[59]

These historic low levels of switching are despite a number of initiatives by the Department, the Central Bank as well as the CCPC to boost switching levels.[60]

Over the next few months, as tens of thousands of people and businesses move their accounts from Ulster Bank and KBC, the lessons that will be learned will be valuable to inform the development of future initiatives to improve switching levels, including any issues that could be considered as part of the Central Bank's current review of the CP-Code.

IBAN portability is also considered to be an effective method to encourage switching, and this issue is discussed further in the chapter on Current & Savings Accounts.

As discussed later in the chapter on Mortgages, the Department commissioned the ESRI to conduct a three stage study of switching in financial services. The third stage involves a large scale field study of initiatives designed to aid the switching process, and is due to conclude in H1 2023. The Review Team recommends that the Department uses the insights gained in its work with the ESRI to work with the Central Bank to make the switching process across retail

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[57] Data provided by the Central Bank
[58] Data provided by the Central Bank
[59] https://bpfi.ie/publications/bpfi-mortgage-drawdowns-q3-2022/
[60] The Department established "Switch your bank": https://www.switchyourbank.ie/. The Central Bank introduced the Switching Code in 2016 and the CCPC set up the Money Tools comparison service. In addition, significant research has been undertaken to better understand the behavioural factors influencing low switching levels

banking products and services easier and to build consumer and SME confidence in the switching process.

COST OF SETTING UP A BANK

The cost of setting up a full service bank is expensive. There are minimum capital costs, IT infrastructure costs, staff costs, compliance/regulatory costs and premises costs, and historically, to access the market a bank required an extensive branch network. The cost of setting up a bank, and operating a bank, will always be higher than the cost of establishing and operating a non-bank, simply due to the fact that higher capital and regulatory standards are required of banks to ensure the deposits of its customers are protected.

However, in recent years it is evident that providers do not need to establish directly in Ireland, nor do they require a physical presence such as a branch network in order to compete and build market share.

Europe's single market and advances in technology have facilitated digital banks, such as Revolut, N26 and Bunq, enter the Irish market and offer digital current account products without any physical branch network. These digital banks are reported to have built a customer base of over two million, providing competition for the traditional banks and more choice for consumers and SMEs. Passporting rules mean these digital banks, or any other authorised provider of retail banking products and services to which passporting rules apply, can enter the Irish market at relative low cost, as they do not need a physical presence (either premises or staff) in Ireland. What is also evident is that once they have established a customer base in Ireland, some of these providers are beginning to expand their product range. For example, as a licenced credit institution in Lithuania, Revolut has recently commenced offering credit to Irish consumers.

Providers do not need to establish directly in Ireland, nor do they require a physical presence such as a branch network in order to compete and build market share

In addition, non-banks have grown their presence and provide an important source of choice for customers, most particularly in consumer, mortgage and SME credit sectors. These non-banks are mainly authorised as RCFs. Where a provider only lends to SMEs, authorisation is not required, however many SME lenders are regulated due to other activities they undertake that do require authorisation, such as lending to consumers. The non-banks have built scale through broker/third party channels, rather than via a physical branch infrastructure.

IRISH LEGAL SYSTEM

As retail banking products and services are mainly provided to customers under a contract arrangement, firms entering a market will consider how the legal system works in a country. Firms tend to want to operate in a legal system they are familiar with, as well as favouring legal systems that deliver timely, certain and predictable outcomes.

The Irish legal system, like the UK system, is based on common law, where precedent, as determined by a court, is a key factor in how legislation and regulation are interpreted and applied. Accordingly, in many situations courts decide cases by following the principles laid down in earlier cases and written judgments. The EU civil law tradition is different from that in common law jurisdictions, such as Ireland. The EU tradition is based exclusively on written codes. There are no principles which are based on case law and precedent and it is sometimes viewed as less complex. While UK firms are familiar with the Irish legal system and how it operates, the material differences between codified law jurisdictions and the Irish system are a factor that firms based in codified law jurisdictions must consider as part of their assessments of whether or not to enter the Irish market.

Legal certainty and timescale to recover collateral are also considerations in assessing the attractiveness of a market. In Ireland, when a borrower defaults under a mortgage contract the time taken to recover collateral through the judicial process is longer relative to other EU countries. In the Public Consultation, the Review Team asked whether there was an appropriate balance between the rights of a borrower who is in financial difficulty compared to the contractual rights of a lender. Of the responses received, circa one third suggested there is an appropriate balance and two thirds suggested there is not. The feedback obtained provided no clear messages.

Legal certainty and timescale to recover collateral are also considerations in assessing the attractiveness of a market

As is discussed later in the chapter on Mortgages, the IMF Financial Sector Assessment Program (FSAP)[61] states that persistence of long term mortgage arrears (LTMA) “pose a challenge to the effectiveness of the overall system for debt resolution and creditors’ rights,” and creates uncertainty on how lenders can recover their collateral when a borrower defaults. The IMF recommended the adoption of a coordinated, multi-agency strategy for resolving LTMA. The State has accepted the FSAP recommendations.

In the chapter on Consumer Protection, the issue of complex consumer protection legislation that has been developed and amended over time is discussed. This issue was raised in a material submission received in response to the Public Consultation, which highlighted that this added legislative complexity can act as a barrier to entry. It is recommended that the

[61] https://www.imf.org/en/Publications/CR/Issues/2022/07/07/Ireland-Financial-System-Stability-Assessment-520469

Department should rationalise and simplify consumer credit legislation, taking account of the transposition in the coming years of the forthcoming EU Directive on consumer credit.

OTHER BARRIERS TO ENTRY

Data inequality and Open Banking

The CCPC has noted that the traditional banks have substantial loan portfolios, and other products such as current accounts, personal loans and credit cards which provide them with access to large volumes of customer data such as customer history of loan payments, income and property valuations. This can help the traditional banks to better assess risk when lending, which can allow the traditional banks to charge lower prices for credit. Thus giving them a competitive advantage over new entrants without the access to such data and as such can act as a barrier to entry.

One of the principal aims of regulation that was introduced in 2018[62] was to encourage the development of 'open banking'. As outlined in the chapter on Forces of Change, open banking is the process of enabling third-party payment service and financial service providers to access consumer banking information such as transactions and payment history. The FSAP notes that 'take-up of the opportunities afforded by open banking has been slow in Ireland,' and highlights a number of possible explanations including 'issues faced by incumbent retail banks in upgrading legacy systems; a relative absence of third-party providers operating in Ireland (i.e. the entities that may directly access payment service users' online payment accounts with their explicit consent) compared to elsewhere in Europe; and a general lack of interest among Irish consumers.'

Take-up of the opportunities afforded by open banking has been slow in Ireland

The EBA and others are working to address issues that are limiting the adoption of open banking so that barriers are removed. Feedback received by the Department during the Review noted that within the market the provision of payment history information is inconsistent (as low as 90 days), insufficient (e.g. customer name not provided), and in some cases technology issues have been experienced making it necessary to make multiple attempts to successfully retrieve information. These issues impede the effective operation of open banking. Clarity regarding minimum standards and mandatory implementation of the minimum requirements are issues that require action by the European authorities. The Review Team understands that the upcoming review of PSD2 is expected to review the issue of minimum standards in open banking.

[62] PSD2

In addition to acquiring customer information via the open banking gateway, the availability of credit scoring information to new entrants is also a means of addressing data inequality between existing providers and new entrants. Currently there is no provider in the Irish market that calculates and makes credit scores available to lenders. To provide credit scoring in the market would require a firm to gather information on borrowers, usually but not always, from their loan applications and credit bureaux, including data such as the applicant's monthly income, outstanding debt, financial assets, how long the applicant has been in the same job, whether the applicant has defaulted on a previous loan, and owns or rents a property.

It is likely that it would take several years for a provider to gather and analyse a sufficient amount of data to generate credit scores. Credit bureaux exist in other countries and can facilitate new market entrants who can use their readymade bank of data to inform their risk assessment processes. In some jurisdictions, for example the USA, credit scores are an integral part of the credit underwriting process.

Having considered the matter, the Review Team considers it is questionable if the introduction of credit scoring, via a credit bureau or otherwise, would facilitate greater competition in the provision of consumer credit in the Irish market. In the course of its work, the Review Team did not identify any market failure which the introduction of credit scoring would address. The Review Team considers that the Central Credit Register (CCR) and information available to credit providers through the open banking channel, once current issues are addressed, are a viable suitable alternatives to a credit scoring system.

IBAN discrimination

IBAN discrimination occurs when direct debit originators, employers or other firms taking or making payments directly to/from a current account do not accept instructions because the nominated account has a non-Irish IBAN. This may discourage passporting firms who do not have an Irish IBAN from setting up in Ireland, as they could consider the discrimination limits the attractiveness of their product to potential Irish customers. In Ireland, all of the traditional banks, the credit unions, An Post and digital bank Bunq have Irish IBANs. Digital banks, N26 and Revolut have German and Lithuanian IBANs respectively.

The Consumer Survey identified that the vast majority of consumers have their main current account with the traditional banks, as opposed to the digital banks. 1% of respondents reported they have their main account with Revolut. It is not clear whether IBAN discrimination is influencing consumers' decisions regarding choice of primary current account provider but it is a reasonable thesis.

As IBAN discrimination is an issue that is not unique to Ireland, the Department and the Central Bank are engaging and taking steps to address this issue, including amending the relevant

regulation[63] to give the Central Bank additional powers to act against firms that are engaging in IBAN discrimination, irrespective of whether or not the firms are regulated.

The Bank Levy

The Bank Levy ("the Levy") was initially introduced for the three-year period from 2014 to 2016 with the purpose of enabling the banking sector to contribute to economic recovery. The Levy was extended twice, first to 2021 and then to 2022.[64] The second extension also provided that those banks that are in the process of winding up their retail banking operations here (i.e. Ulster Bank & KBC) would be exempted from the Levy, whilst those banks still subject to it (primarily AIB, BOI & PTSB) would only be expected to pay what they had paid in 2021, i.e. a total of €87 million. As announced in Budget 2023 it is intended to extend the Levy for a further year to end-2023, on the same basis as that which has applied in 2022.

The Levy is calculated using a Deposit Interest Retention Tax (DIRT) based formula, using 2019 as a base year. The structure of the Levy means it only applies to banks that are paying interest on customer accounts in the base year, and primarily applies to those institutions that have a physical operation in Ireland.

If the Levy is not amended, any new entrant to the Irish retail banking market would be exempt from it placing the traditional banks, in particular, at a disadvantage to those new retail banking providers.

The actual existence of the Levy could also act as disincentive for a new entrant into the Irish market in case it is amended and it is also potentially an incentive to avoiding paying interest on customer accounts.

The Levy could be reformed to level the playing field for the traditional banks, but this would require broadening the scope of the firms caught under it. While this would deal with level playing field issues, it would still remain as a dis-incentive to provide retail banking products and services into Ireland, whether via passporting of services or physically establishing an operation.

[63] https://www.irishstatutebook.ie/eli/2013/si/132/made/en/print#
[64] During the period between 2014 and 2021, the State has raised €1.2bn from the Bank Levy.

5.4. Options for greater competition

In the course of the Review there were calls for the State to introduce more competition into the retail banking sector. The Review Team explored whether it would be desirable to do this in the following ways:

- Through a local public/community banking structure such as via a Sparkassen-like model.
- Through the credit union network.
- Through an expansion of the role of the An Post network.

LOCAL PUBLIC BANKING AND CREDIT UNIONS

A potential avenue to introduce further competition in the retail banking sector would be for the State to directly introduce new competitors of scale to the market. The Review Team received 15 submissions to the Public Consultation whose primary recommendation was that the State establish a network of regional or local public banks.

In 2018, the Department of Finance and the Department of Rural and Community Development jointly published a report investigating the feasibility of establishing a network of local public banks based on the Sparkassen model, as proposed by Irish Rural Link, particularly to provide SME credit.[65] Following on from this, the Department commissioned a report from Indecon International Economic Consultants titled *Evaluation of Concept of Community Banking in Ireland*[66] (the Indecon Report). These reports found no business or economic case for the establishment of a new state-owned public banking network.

The Review Team recognises that developments since the Indecon Report was published at the end of 2019 may warrant a reconsideration of the local public banking concept in Ireland. However, the Review Team has reached the conclusion that the recent decisions by Ulster Bank and KBC to leave the market do not change the conclusions previously reached for the following reasons:

- While there have been closures of bank branches and a limited number of credit union branches, there is still extensive local provision of retail banking products and services through the three remaining traditional banks, the credit union networks as well as the services available through An Post;
- The Review Team considers that the establishment of a local public banking network could displace the credit union network. The credit union network already provides retail banking products and services at a community level, which is a core tenet of what is proposed under a public banking model;

[65] https://www.gov.ie/en/publication/14fce4-local-public-banking-in-ireland/
[66] https://www.gov.ie/en/press-release/3f7624-minister-donohoe-publishes-independent-external-evaluation-on-local-/

- The Review Team did not identify any market failures in the retail banking sector, and accordingly, the establishment of a state-owned local public banking network could fall foul of EU state-aid rules;
- A state-owned local public banking network would come at a significant cost to the Exchequer, take years to establish and to obtain regulatory approval and, thereafter, is unlikely to achieve sufficient scale to be an effective competitive force in the retail banking markets for many years, if ever; and,
- The presence of further State involvement in the retail banking sector through the establishment of a local public banking network could act as a deterrent to potential new entrants that may wish to enter the Irish retail banking market.

Traditionally, credit unions were active in the provision of deposit accounts and small value personal credit, but, in recent years, some credit unions have expanded their product range to include current accounts, mortgages, higher value personal credit and SME credit. The range of products provided by individual credit unions within the sector is heterogeneous and, as each credit union is a standalone entity, members cannot use locations interchangeably.

To date, the provision of current accounts is a relatively small but growing product offering. The provision of mortgages and SME credit is also growing from a low base. A key issue in developing and launching new products, is the fact that each credit union is an independent entity and capacity to deliver is generally constrained by size. To create a stronger product offering, some credit unions have entered into collaborative ventures whereby the costs of certain activities are shared, such as product development, IT and back office functions. The growth in the provision of current accounts has been greatly aided by two such collaborations. However, there are many credit unions who continue to maintain a narrower product range, comprising savings accounts and consumer loans.

Forthcoming legislation[67] will permit credit unions to refer members to another credit union with a wider product offering. The legislation also introduces other reforms, including the introduction of corporate credit unions, whose members consist of other credit unions. This will allow credit unions to further collaborate and enable them to compete more effectively.

However, it is the view of the Review Team that this should only be the beginning of reform in the credit union sector. Credit unions already have the key assets needed to bring further competition into the retail banking market. These are a nationwide network with strong roots in every community, significant capital reserves and liquidity in the form of strong and stable deposits. This means they are not dependent on the wholesale market for liquidity funding to provide credit.

Furthermore, the expansion of the capabilities of the credit union network would not fall foul of EU state-aid rules, it would not come at a significant Exchequer cost and it has an existing

[67] The Credit Union (Amendment) Bill 2022

network of branches. Furthermore, it would not involve significant State involvement in the sector and as such it would not act as a deterrent to potential new entrants to the Irish retail banking market.

The Review Team concluded that the credit union sector, building on the policy proposals approved by the Government in July, should be given the opportunity to transform into a community based provider of universal retail banking products and services. In this role, the Review Team believes that the sector has the capacity to provide additional competition, at scale. However, this transformation will require strong leadership and collaboration within the sector to implement the significant business model change required to deliver scale efficiencies, leverage the necessary expertise in a cost effective manner and to develop greater standardisation across the product range.

The credit union sector should be given the opportunity to transform into a community based provider of universal retail banking products and services

While Government should be prepared to act where appropriate, it is also incumbent on all of those working in the sector to be ambitious and to embrace transformational business model change as a matter of urgency.

The Central Bank has advised the Review Team that the regulatory framework is not a barrier to credit union commercial progression. The Central Bank's strategic priorities include a focus on continued engagement with credit unions on effective implementation of the existing regulatory framework and support towards prudent credit union business model transition. This includes assessment of applications for increased house and business lending, current accounts and provision of additional services.

Transformation will require strong leadership and collaboration within the sector to implement the significant business model change required

The lending framework for credit unions was updated in 2020. The Central Bank has undertaken to perform and publish an analysis on credit union sector lending in 2023 - three years post-commencement of the 2020 amendments. This is in order to assess and analyse the actual impact that those changes to the lending regulations have had on the activity of the credit unions, and to inform any decisions on the need for future change.

The Review Team understands the Department and Central Bank will engage constructively through the stakeholder roundtable and with the Credit Union Advisory Committee (CUAC) to give further consideration to the sector's legislative and regulatory framework as the wider financial services policy framework develops. Should the delivery of a universal product

offering and associated business model changes require further legislation, the Government should consider it.

Opportunities for the credit union sector in the mortgage and SME markets are also outlined in the Mortgage and SME chapters of this Report.

The Review Team recommends:

Recommendation 5-2

Taking into account the legislative amendments in the forthcoming Credit Union (Amendment) Bill 2022, the credit union sector and its leadership should develop a strategic plan that enables the sector to safely and sustainably provide a universal product and service offering, which is community based, and which is offered to all credit union members, directly or on a referral basis.

Such a strategic plan should demonstrate how credit unions can:

- Scale their business model in a viable manner in key product areas such as mortgages and SME lending;
- Invest in expertise, systems, controls and processes such that the sector can deliver standard products and services across all credit unions, in a manner that manages risks arising and continues to protect members' savings; and
- Provide the option of in-branch services for members of all credit unions.

Where new or amended legislation is required to achieve a universal product offering and associated business model transformation, the Department of Finance (with guidance and technical advice from the Central Bank) should consider the necessary legislative changes.

POST OFFICES

An Post also provides a range of retail banking products and services to consumers through its network of 912 post offices across the country. Most of the retail banking products and services offered by An Post are provided on an agency basis, including State savings and consumer credit.[68] However, An Post itself also offers current accounts to consumers. In providing these retail banking products, An Post is another community based competitor, and offers consumers and SMEs with choice and services at a local level through its national network of branches.

An Post can continue to develop and expand its retail banking offering, and should ensure that all the products and services it provides add to the commercial viability of the company

The Review Team considers that An Post can continue to develop and expand its retail banking offering, and where it does, it should ensure that all the products and services it provides add to the commercial viability of

[68] An Post supplies State Savings deposits on behalf of the NTMA and acts as a credit intermediary for of Avantcard.

the company. In addition, the Review Team is of the view that An Post should seek Central Bank approval for those services which it regulates prior to seeking the authorization of the Minister for Finance under section 67 of the Postal and Telecommunications Act 1983.

5.5. Central Bank functions & powers

In the context of a more concentrated Irish retail banking sector it is important to ensure that going forward there continues to be effective competition among the remaining providers.

There were some calls in the course of the Review to confer a secondary competition mandate on the Central Bank. In a number of cases, other countries have given financial regulators a role in promoting competition in their jurisdictions. According to a BIS report on the universe of supervisory mandates, giving bank supervisory authorities statutory competition mandates is not widespread globally, and generally not seen as common in the EU.[69] However, the UK's Prudential Regulation Authority (PRA) and Financial Conduct Authority (FCA) and the Australian Prudential Regulation Authority (APRA), among others, each consider competition when they are performing their functions. In addition, some sectoral regulators in Ireland also have competition functions including the Commission for Communications Regulation (ComReg), the Commission for Regulation of Utilities (CRU) and the Legal Services Regulatory Authority (LSRA).

Between 2003 and 2010 the Central Bank and the Financial Services Regulatory Authority of Ireland had a mandate to 'promote the development within the State of the financial services industry but in such a way as not to affect the objective of the Bank[70] in contributing to the stability of the State's financial system' as well as to ensure the safety and soundness of the financial system. However, this dual mandate was considered to have been a conflict of interest in light of the banking crisis in Ireland and was not replicated in the Central Bank Reform Act 2010, which reestablished the Central Bank as a unitary structure.[71]

During the Review, the Review Team has consulted with the Central Bank on the calls to confer it with a secondary competition mandate. In response, the Central Bank has highlighted that the Central Bank Act 1942 already requires it to perform its functions and exercise its powers, in a way that is consistent with the orderly and proper functioning of financial markets.[72] In the Central Bank's view, an effective functioning market includes appropriate levels of competition, fair and transparent price formation, and provides consumers with access to the products they need.

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[69] See Table 1 of BIS (2021) "FSI Insights on policy implementation No 30 The universe of supervisory mandates – total eclipse of the core?": https://www.bis.org/fsi/publ/insights30.pdf
[70] Bank was defined as Central Bank and the Financial Services Regulatory Authority of Ireland
[71] https://inquiries.oireachtas.ie/banking/evidence/the-irish-banking-crisis-regulatory-financial-stability-policy-2003-2008/
[72] Section 6A(2)(b) of the Central Bank Act 1942 : https://www.centralbank.ie/fns/legislation

The Review Team notes that the Central Bank has other legislative requirements to have regard to promotion of fair competition in financial markets when making codes of practice[73] and the promotion of fair competition between credit institutions when exercising its powers in relation to customer charges.[74]

However, the examination of Central Bank legislation in relation to competition has highlighted a lacuna that should be addressed. As noted above, when making codes of practice under the 1989 Act, the Central Bank has to have regard to fair competition. Since the enactment of the Central Bank (Supervision and Enforcement) Act 2013, the Central Bank mainly uses the regulation making powers under section 48 of that Act instead of section 117 of the 1989 Act. The latter is only used for amendments to existing codes.

For example, the revised CP-Code will in fact be one or more regulations under section 48 of the 2013 Act. The lacuna is that section 50 of the 2013 Act, which sets out matters that the Central Bank has to have regard to when making section 48 regulations does not include any reference to competition or the impact on consumers.

Consequently, and to align the 2013 Act with the 1989 Act, the Review Team recommends that the Central Bank should be required to carry out and publish assessments of the costs and benefits of proposed regulations, which consider the potential impact on consumers and fair and sustainable competition, amongst other issues.

An effective functioning market includes appropriate levels of competition

In line with its view and its mandate, the Review Team also recommends that the Central Bank should:

- In completing its Annual Performance Statement include an assessment of how the exercise of its functions is consistent with the orderly and proper functioning of domestic financial markets, and
- Assess how existing domestic regulation impacts competition within domestic financial markets, recognising its importance to the orderly and proper functioning of those markets.

The Review Team welcomes and agrees with the Central Bank's interpretation that an effective functioning market includes appropriate levels of competition. This is important and taken together with its other legislative requirements in relation to making codes of practice and considering customer charges along with the proposed amendment to the 2013 Act outlined above, the Review Team is satisfied that the Central Bank does and will take fair competition into account when performing its functions and exercising its powers.

[73] S.117 of the Central; Bank Act 1989 https://www.irishstatutebook.ie/eli/1989/act/16/enacted/en/html
[74] S.149 of the Consumer Credit Act 1995 https://www.irishstatutebook.ie/eli/1995/act/24/enacted/en/html

The Review Team believes the proposed changes outlined above will help further enhance the way the Central Bank exercises its powers and perform its functions in this area. *The Review Team recommends:*

Recommendation 5-3

In line with its view and its mandate, the Central Bank should:

- In completing its Annual Performance Statement, include an assessment of how the exercise of its functions is consistent with the orderly and proper functioning of domestic financial markets; and
- assess how existing domestic regulation impacts competition within domestic financial markets, recognising its importance to the orderly and proper functioning of those markets.

Recommendation 5-4

The Department of Finance should prepare heads of a bill in 2023 to amend S.50 of the Central Bank (Supervision and Enforcement) Act 2013 to require the Central Bank to carry out and publish assessments of the costs and benefits of regulations it proposes to make under S.48 of the 2013 Act, where appropriate. The assessments are to consider the potential impacts on consumers and fair and sustainable competition, amongst other issues.

The Review Team believes, in the context of a more concentrated market for retail banking products and services, it is important that it continues to be competitive

Given the CCPC's role in the enforcement of competition law and promotion of competition, an important additional support for citizens and the economy will be that it and the Central Bank, the two relevant authorities, continue to work closely together. The CCPC and the Central Bank should build on existing arrangements and establish closer coordination to share perspectives, information and experience of the orderly functioning of markets, consumer protection and competition in the retail banking sector. The co-operation between the CCPC and the Central Bank could facilitate further joint work in the areas.

In this context and after consultation with both authorities, the ability to share detailed market data between the Central Bank and the CCPC needs to be clarified. To this end, the Review Team recommends that the existing legislative provisions in relation to data sharing are reviewed to identify actions to facilitate, subject to complying with European law, increased information sharing.

The Review Team recommends:

Recommendation 5-5

The Department of Finance should review the relevant legislation to identify actions, consistent with provisions governing data collection and use in relevant EU Regulations and Directives, to facilitate increased sharing of information between the Central Bank and the

Competition and Consumer Protection Commission across all relevant areas of their respective remits

Recommendation 5-6

The Competition and Consumer Protection Commission and the Central Bank should build on existing arrangements and establish closer coordination to share perspectives, information and experience on the orderly functioning of markets, consumer protection and competition in the retail banking sector.

6. Climate and the retail banking sector

> *"The current changes in the planet's climate are transforming the world."*[75]

The ToR included consideration of the key role the retail banking sector will play in the provision of sustainable credit to the economy, and how the banking system can best support economic activity. Whilst an assessment of how the retail banking sector is performing against climate objectives is not within the scope of the Review, the Review Team did consider climate specifically in relation to the retail banking products and services that are within the scope of the Review, principally SME credit and mortgages. An important consideration in this regard was whether the retail banking sector is providing appropriate support and funding to consumers and SMEs to enable them meet the Government's climate objectives, as well as wider EU/ECB requirements.

6.1. EU Strategy

The EU focus on climate includes the publication in July 2021 of a renewed 'Strategy for Financing the Transition to a Sustainable Economy.' The strategy sets out a comprehensive set of actions and it includes specific reference to green loans and mortgages for retail customers. While the EU market for green retail loans and mortgages is developing, the EU Taxonomy[76] will serve as a reference point for lenders who wish to finance "green lending" as practices regarding green loan classification across the EU currently vary.

The EU Strategy aims to move banking to a more inclusive sustainable finance framework, with a particular aim of allowing households and SMEs access sustainable finance. In this respect, the EU Strategy highlights the need to develop measures to support the provision of green loans and mortgages to increase the levels of retrofitting, switching to electric vehicles, and other decarbonisation changes. It also identifies the need to increase individual financial literacy, and to provide clear, harmonised information to the consumer to help them make informed choices.

6.2. Government Climate Action Plan

The Irish Government launched its Climate Action Plan in November 2021,[77] stating at the time:

[75] Climate Action Plan 2021https://www.gov.ie/en/campaigns/2f87c-climate-action-plan-2021/
[76] https://finance.ec.europa.eu/system/files/2021-04/sustainable-finance-taxonomy-faq_en.pdf
[77] https://www.gov.ie/en/publication/6223e-climate-action-plan-2021/

> *'The Climate Action Plan 2021 provides a detailed plan for taking decisive action to achieve a 51% reduction in overall greenhouse gas emissions by 2030 and setting us on a path to reach net-zero emissions by no later than 2050, as committed to in the Programme for Government and set out in the Climate Act 2021. It will put Ireland on a more sustainable path; cut emissions; create a cleaner, greener economy and society; and protect us from the devastating consequences of climate change. It is a huge opportunity to create new jobs and grow businesses in areas like offshore wind; cutting-edge agriculture; and retrofitting, making our homes warmer and safer.'*

In June 2021, the IMF estimated that meeting Ireland's emission reduction target would require significant investment of close to €20 billion annually for the coming 10 years, of which about one-third would be public capital spending. Clearly further funding is required, coming from a mix of further State supports, personal and business savings, as well as loans from commercial lenders. Of note is a finding from a survey that 50% of consumers who have improved, or plan to improve their home energy efficiency rely on savings.[78]

With regard to State supports, there is a comprehensive range of grants and supports available to consumers and businesses including retrofitting and electric vehicles, administered through the Sustainable Energy Authority of Ireland (SEAI). In addition, to promote the provision of retail credit, the SBCI recently introduced a €150m SME Energy Efficiency Scheme. Work is also progressing on the development of a €500m residential retrofit guaranteed credit scheme. It will be delivered by the SBCI on behalf of the Department of Environment, Climate and Communications (DECC) with the aid of a counter guarantee from the European Investment Fund.

6.3. Retail banking sector role

The retail banking sector has an important role to play in helping Ireland achieve its climate action targets. The role of the banks was acknowledged by the BPFI and the Institute of Bankers (IoB) in their submissions to the Public Consultation. The IoB stated 'Banks have a critical role in supporting the economy achieve this huge transition which includes:

- Effectively driving capital to green purposes, supporting consumers and businesses
- Facilitating funding

[78] https://bpfi.ie/publications/bpfi-sustainable-finance-report/

- Innovating in the design and creation of sustainable finance products
- Promoting financial inclusion and literacy.'

Through their sustainability reporting, the traditional banks have outlined the measures they are taking to address climate change, setting out the volumes of 'green' lending that has already been advanced, as well as future targets. The BPFI has stated that 'most banks have set a target of aligning customer lending portfolios across all sectors to net zero emissions by 2040,' and noted that 'some banks have made significant progress in this regard where close to 20% of all new lending is done using green products.'[79] It is also reported that rating agencies rate the Irish banks quite well under the broader environmental, social and governance factors,[80] which includes climate action.

From a financial stability and business model resilience perspective, banks must progressively transition their loan portfolios to net zero emissions. In the 2022 FSAP, the IMF highlighted that 'the Irish banking system's exposure to climate risk is moderate, but material.'[81] Furthermore, the ECB's Single Supervisory Mechanism (SSM) recently conducted a climate related stress test on banks in the EU (including the larger Irish banks). The findings from the stress test highlighted that, despite some progress, many deficiencies, data gaps and inconsistencies remain across the banks. The results mean that many banks do not yet sufficiently incorporate climate risk into internal models and stress testing frameworks. In addition, many banks appear to lack clearly defined long-term strategies for credit allocation policies that reflect transition paths. Against this background, banks are expected to make substantial progress in the coming years in terms of stress test capabilities and long-term strategic planning e.g. with regard to green transition plans and targets.

6.4. Public Consultation findings

In the Public Consultation the Review Team asked if the retail banking sector was providing consumers and SMEs with appropriate support and funding to transition to carbon neutral. Of those who responded, almost eight in ten indicated the sector was not providing enough support. The dominant comment in this regard was that was that placing 'green' in front of a product name is not enough to promote the transition to a green economy. The responses did not provide any insights into what measures the banking sector could take to address this issue.

Placing 'green' in front of a product name is not enough to promote the transition to a green economy

[79] https://bpfi.ie/publications/bpfi-ey-the-future-of-retail-banking-in-ireland-report/
[80] https://www.goodbody.ie/docs/default-source/morning-wrap/morning-wrap-2021-q4/mmw-22-sept-2021.pdf?sfvrsn=22753e19_2
[81] https://www.imf.org/en/Publications/CR/Issues/2022/07/07/Ireland-Financial-System-Stability-Assessment-520469

As outlined in the chapter on Consumer Credit, the findings of a European-wide consumer survey included that, whilst consumers are increasingly willing to make sustainable choices, they will only be incentivised to take out green loans if they are competitive and affordable. This survey also suggested that 'green loans' are not widely offered.[82]

As outlined in the chapter on SME Credit Ireland's SMEs rank behind EU peers in the area of climate action. The 2021 European Investment Bank (EIB) Investment Survey found that 15% of Irish firms had already invested in tackling the impacts of weather events and reducing their carbon emissions, relative to 40% for their EU peers.

6.5. Actions for the retail banking sector

The availability of innovative, competitive and effective financial products and services to consumers and SMEs to assist in the transition to a low carbon future is critical. While the retail banking sector is already engaged in the process, further actions by the sector are required to complement the current suite of private sector products, public funding and subsidies. In this regard, although consumers and SMEs have made progress in making their properties more energy efficient, as well as purchasing eco-friendly cars and commercial vehicles, a material increase in momentum is required to support Ireland to meet its 2030 and 2050 targets.

Further actions by the sector are required to complement the current suite of private sector products, public funding and subsidies

The Review Team notes much public commentary regarding the challenges encountered by consumers in pre-funding the full costs of home retrofits and energy upgrades, particularly where a significant portion of the cost is eligible for SEAI grants. While recognising the need for commercial lenders to operate within risk appetites and credit policy parameters, the Review Team suggests that all relevant stakeholders engage to explore solutions regarding how consumers could be supported to bridge grant payments, and thereby enable them commence the envisaged works.

Furthermore, the Review Team calls on all providers of credit within the retail banking sector to expand their range of products available to support green investments by consumers and SMEs. In this regard, creative approaches to structuring loans with the aim of aligning the monthly repayment, insofar as possible, with the energy cost saving that will accrue to the consumer or SME could be considered. Lenders could also consider if opportunities exist within their existing mortgage books to proactively engage with consumers on possible re-mortgaging opportunities to fund retrofitting where there is adequate LTV headroom, and subject to normal and prudent underwriting standards.

[82] https://www.beuc.eu/sites/default/files/publications/beuc-x-2021-076_affordable_green_loans.pdf

The Review Team recommends that:

Recommendation 6-1

As a matter of priority, the retail banking sector should consider how best to expand its products and services so that is provides a competitive and effective financial offering to consumers and SMEs to assist in the transition to a lower carbon future.

7. Access to cash

7.1. Background

Cash is a critical component of the payments system and, as noted by the ECB 'the economy requires a certain amount of available cash to function'.[83] In Ireland, the National Payments Plan ('the NPP'),[84] which was published in 2013, sought to improve the take up of electronic payments in Ireland in order to drive 'improved cost competitiveness, greater security, convenience, consumer choice and reduced financial exclusion.[85] The NPP sought to double the number of electronic payments per capita by 2015, leading to a reduction in cash and cheque usage to the EU average, as well as making the Irish cash cycle[86] as efficient as possible, while also serving the needs of consumers and SMEs. The NPP noted that while Ireland would not move to being a cashless society, it would transition to a 'less-cash' society.

The economy requires a certain amount of available cash to function

In the last decade, key objectives of the NPP have been achieved - Ireland now has a more sophisticated electronic payments system and much greater usage of electronic payment methods. While it remains an important element of the payments system, cash usage has declined. Since 2015 the number of ATM transaction declined by 46%,[87] whilst the use of debit cards at the point of sale increased 284%.[88] Card payments accounted for 62.4% of the total number of payment transactions in 2021,[89] with contactless payments rising to their highest level since data began to be collected in 2017.[90] The transition to electronic payments was accelerated by the COVID-19 pandemic, and the question that now arises is how to ensure the decline in cash is not outpacing the needs of society and the economy.

The ECB notes that cash is the only form of public money to which everyone can have direct access. Given its importance within the wider payments system, cash is the subject of a specific ECB strategy,[91] which aims to ensure that cash remains widely available and accepted as both a means of payment and a store of value. In addition to outlining the importance of cash, the ECB strategy identifies the role of national central banks and the banking sector in

[83] https://www.ecb.europa.eu/euro/cash_strategy/cash_role/html/index.en.html
[84] https://www.centralbank.ie/docs/default-source/news-and-media/press-releases/2014/april/10-april/national-payments-plan---final-version.pdf?sfvrsn=83bcd71d_4
[85] Financial exclusion in this context related to the high number of individuals without current accounts (e.g. 34% of unemployed people do not have a current account), which is the enabler of electronic payments. The NPP called for the introduction of a Standard Bank Account (this predates the EU requirement for a Basic Bank Account).
[86] Delivered to the public via the Central Bank, commercial banks (ATMs and branches), An Post and retailers.
[87] 2015: 152m ATM transactions; 2021: 82.5m ATM transactions: https://www.centralbank.ie/statistics/data-and-analysis/credit-and-debit-card-statistics
[88] https://www.centralbank.ie/statistics/data-and-analysis/credit-and-debit-card-statistics
[89] https://www.centralbank.ie/statistics/data-and-analysis/payments-services-statistics
[90] https://bpfi.ie/publications/bpfi-payments-monitor-q2-2022/
[91] https://www.ecb.europa.eu/euro/cash_strategy/html/index.en.html

supporting continued widespread access to cash. It also notes that, at the time of publication, cash remains the dominant means of payment within the euro area, as the clear majority of daily payments are made using banknotes and coins. Very importantly, cash also has a key role as a safety net in the event of the electronic banking or the payments infrastructure being impacted by electronic outages or cyber-attacks.

Notwithstanding its decline in use, cash continues to be preferred by many consumers and SMEs. It is the main money management tool for many of those who are less well-off[92] and it allows individuals, including those who are older, to control their own finances thereby reducing the risk of financial dependency or financial abuse.

Cash allows individuals, including those who are older, to control their own finances thereby reducing the risk of financial dependency or financial abuse

However, there are costs associated with the cash infrastructure that must be considered. As cash usage declines, if costs do not contract commensurately, the per-unit cost of cash increases. This development, along with a more general drive to reduce costs, has incentivised the traditional banks to move away from cash services, resulting in closures of branches, reduction or removal of cash services in branches, closures of ATMs and divestment of entire off-site ATM networks to independent operators. This phenomenon is a feature across developed economies[93] and in many cases happened without due consideration of the societal implications of these developments.

In response, governments and regulators have been leading discussions and developing national strategies to preserve access to cash. Arising from AIB's announcement in July 2022 that it planned to remove cash facilities from 70 of its branches, this conversation has accelerated in Ireland.

7.2. Access to cash in Ireland

DEVELOPMENTS SINCE 2013

There have been significant changes to the cash system since 2013 and efficiencies and savings have been achieved, mainly through a reallocation of roles within the system. The role of the cash-in-transit (CITs) firms has increased[94] as banks have reduced their cash infrastructures by closing their cash centres and outsourcing the activities they historically

[92] https://www.accesstocash.org.uk/media/1087/final-report-final-web.pdf
[93] For example, Sweden, The Netherlands and New Zealand have all seen material reductions in the provision of cash services.
[94] Providing cash centre processing and distribution (delivery and collection) to banks, post offices and retailers.

undertook to CIT firms.[95] Other changes to the cash infrastructure include closing branches, reducing cash services or removing cash counters in certain branches and the sale of off-site ATM networks to Independent ATM Deployers (IADs).[96] In a welcome development, the role of the post office increased when AIB, BOI and Ulster Bank entered into agency agreements with An Post which allowed their customers lodge and withdraw cash (subject to certain limits) across the 900+ post office outlets.

The provision of cashback facilities by retailers also represents a significant change - close to two thirds of adults have availed of cashback through a retailer, with one in eight using it once a week, suggesting that retailers are important in providing access to cash to consumers.[97] Cashback is considered to provide a more flexible way to withdraw cash compared to ATMs, as it allows for small denominations to be withdrawn, including coin. However, under existing EU Regulations,[98] cashback is not available to consumers unless the consumer purchases a good or service.

Each of these developments underpin significant changes in the retail banking cash network:

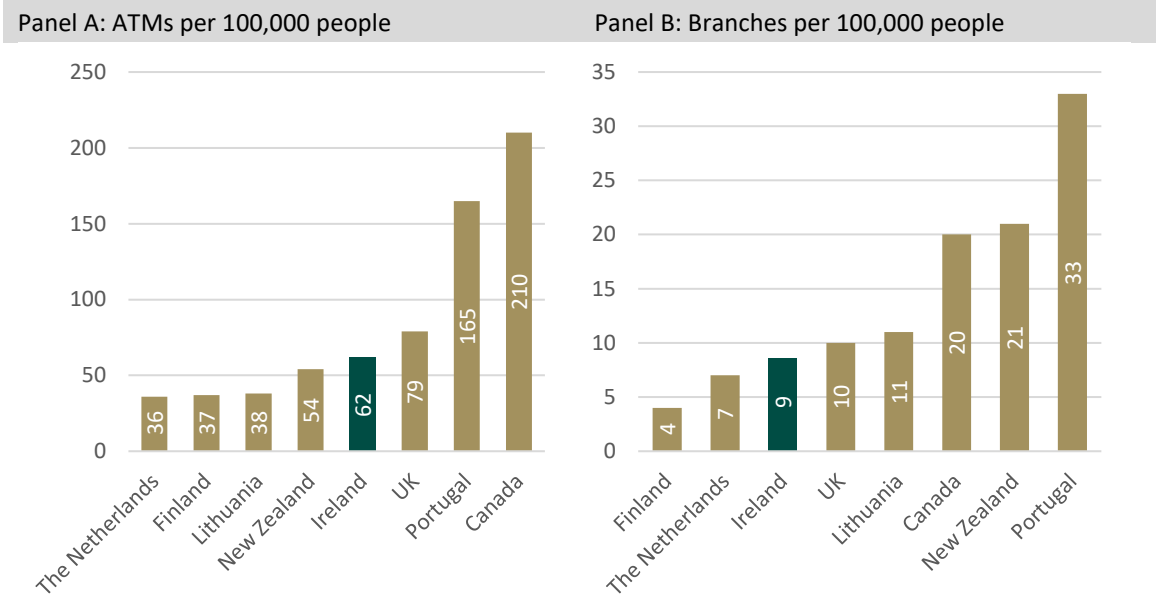
- Following the departure of Ulster Bank, the bank branch network will have reduced from 617 branches in June 2020 to 438 branches in September 2022. [99]
- Of the remaining bank branches, 21% (92) will have no staffed cash counter[100] though nearly all have an ATM inside or outside the branch, or both.
- The number of bank branches per 100,000 of population is 8.63,[101] whereas in June 2020 it was 12.93.[102] This compares to UK 10.4; New Zealand 21.4; Netherlands 7.0; Portugal 32.8; Lithuania 10.5; Finland 4.0; Canada 20.2,[103] though many of the branches quoted for some of these countries will also include firms that are akin to credit unions, and some/many may be cashless (see Figure 8).
- The number of ATMs per 100,000 is 62, which compares to the Netherlands 36; Finland 37; Lithuania; New Zealand 54; the UK 79; Portugal 165; Canada 210.
- As branches close or go cashless, the ATMs in those branches are removed and this is reflected in the reduction of the ATM network by 30% in the period 2017-20, which is the third highest decrease in the EU after The Netherlands (-62%) and Belgium (-34%).[104] The Dutch and Belgian reductions reflect the impact of the implementation of utility type models of ATM provision, and therefore the reductions occurred under a

[95] AIB, BOI and Ulster Bank closed their cash centres, and cash processing is now outsourced to the CIT sector. The CIT sector has consolidated due to acquisitions, and two CIT companies now account for 95% of the market. Source: The Central Bank
[96] IADs are commercial entities that own, manage and place cash machines in retail premises and other locations.
[97] https://www.gov.ie/en/organisation-information/3c122-retail-banking-review/#consumer-survey-results
[98] Payment Services Directive https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex%3A32015L2366
[99] 438 branches based on data supplied by AIB, BOI, PTSB and excludes college and hospital locations with no cash counters
[100] This is based on data supplied by AIB, BOI and PTSB to the Review Team (September 2022)
[101] Calculated based on 438 branches for population of 5,028,000
[102] Source: The Central Bank
[103] International Comparison (Deloitte) 2022
[104] Source: Deloitte

structured framework – this is not the case in Ireland where changes to the network reflect independent decisions of individual providers.

- In 2015, the entire ATM network in Ireland was operated by the traditional banks, whereas at the end-2021 IADs control c.75% of ATM locations throughout the country.[105] Nine IAD firms operate in Ireland, with the largest two being Euronet and Brinks.[106]
- Since the closure of their own cash centres, the banks are now entirely reliant on the CIT sector, where the two biggest CIT companies account for c.95% of the market.
- The number of credit unions has reduced due to mergers and closures. The sector now comprises 204 credit unions in over c. 400 locations (some credit unions operate sub-offices), that provide cash services to their respective members, but not on a universal basis as each credit union is a standalone entity. Some credit unions provide ATMs. The number of credit union physical locations is down 18% since 2013.[107]

Figure 8 - ATMs and branches per 100,000 people



Source: Department of Finance, International Comparison and Central Bank

In terms of access to branches, ATMs and the post office, the Review Team notes the following:

[105] Where each bank branch is considered as a single ATM point. Within ECB methodology of the measurement of access to cash, due to the significant clustering of ATMs within retail bank branches, each bank branch is considered as a single ATM point. By contrast, IAD ATMs tend not to cluster. If all retail bank ATMs were counted alongside all IAD-owned ATMs, recent data suggests overall IAD ownership of the ATM network may be in the region of 60%.
[106] Source: The Central Bank
[107] Source: The Central Bank

- Branches: While the Review Team is aware from the (Central Statistics office) CSO[108] that the average distance to a bank branch was 5.5km in 2019, this metric has not yet been updated to reflect changes since then, which are ongoing due to the further closure of Ulster Bank and KBC branches. However, the Consumer Survey identified that almost 50% of respondents lived within 5km of a branch of their main bank, with a further 28% living within 5-10km, and 24% living in excess of 10km away.
- ATMs: Research[109] undertaken by the Central Bank found that 87.3% of the population lived within 5km of an ATM, with 98.8% and 99.9% living within 10km and 15km respectively (June 2020). Regional disparities exist, with 5km proximity being highest in Dublin and lowest in the west and border regions. When compared to peers, the same research found that Ireland ranks in the bottom five out of the 19 Eurosystem countries when it comes to percentage of population within 5km of an ATM.
- An Post: When closing branches and ATMs, AIB, BOI and Ulster Bank sought to mitigate the impact on their customers by entering into arrangements with An Post whereby the local post office provide deposit and withdrawal cash (notes and coin) services to their customers. There are 912 post offices across the State - 93% of the population are within 5km of their local post office, and 99% within 10km.[110] However, the cash services provided by An Post are restricted (with limits on the value of notes and coin that can be lodged and withdrawn), unless specific alternative arrangements are agreed. This means that the cash services provided in the post office may not be equivalent to the service previously provided by the customer's bank branch, resulting in customers needing to travel to the next nearest branch where such services continue to be provided.

THE NEED FOR ACCESS TO CASH

In common with other EU countries, the majority of people in Ireland want to have the option to pay in cash, even if some of them have a preference for digital as a means of payment.[111] Information obtained by the Department as part of this Review suggests that only 11% of consumers do not use cash,[112] and that notwithstanding the increased use of debit cards, cash spending in-store relative to total spending still stands at 31%.[113]

When we talk about access to cash, the Review Team means access to both cash withdrawal and deposit facilities, including coin. As people tend to get their wages, salaries and other payments paid directly to their bank accounts they tend to have a greater need for withdrawal

[108] https://www.cso.ie/en/releasesandpublications/ep/p-mdsi/measuringdistancetoeverydayservicesinireland/generalresults/
[109] Source: The Central Bank
[110] Information provide by An Post – coverage levels are based on the 2016 Census results
[111] https://www.ecb.europa.eu/pub/economic-bulletin/articles/2022/html/ecb.ebart202205_02~74b1fc0841.en.html#:~:text=Published%20as%20part%20of%20the,geographical%20location%20or%20technological%20savviness.
[112] https://www.gov.ie/en/organisation-information/3c122-retail-banking-review/#consumer-survey-results
[113] Ibid

rather than deposit facilities. People use ATMs more than branches to withdraw cash,[114] though people in the age group 65+ have a higher dependency on their local bank branch.[115]

SMEs tend to have a higher dependency than consumers on bank branches for their cash services. In Ireland, of the one third of SMEs that visit their bank branch weekly, 88% do so for the purposes of depositing or withdrawing cash.[116] Research suggests that small retailers in particular need deposit facilities more than withdrawal facilities,[117] though the Review Team understands that small retailers need to withdraw coin more than deposit it as cash customers tend to pay with notes most of the time.

While cash use has been declining, it is apparent that cash is still preferred by certain users or in certain situations. The current challenge to be addressed is the extent to which further reductions will reflect actions by certain providers of cash services, rather than a desire by consumers and SMEs to operate in a society that still uses and needs cash, albeit at reduced levels. It is generally accepted that over time cash usage will decline further, however it is important that future reductions in the cash infrastructure do not outpace the expectations or needs of society.

Meanwhile, as ATM's are, and are likely to remain, the most common method for consumers to withdraw cash, it is important that they remain accessible not just in terms of their physical location and the cost of accessing them, but also in terms of the service they offer. Having an ATM close by, but which is not adequately accessible, is often out-of-order or regularly only dispenses high value note denominations (e.g. €50) can act as a barrier to access. These issues can particularly impact the socially vulnerable who may not have the means to travel to the nearest alternative ATM, or may have less than the lowest available note denomination in their bank account. Similarly, long queues at the cash counters in branches can act as a barrier to consumers and SMEs accessing cash services.

It is important that future reductions in the cash infrastructure do not outpace the expectations or needs of society

THE COST OF ACCESSING CASH

It is important to ensure that changes to the costs of accessing cash services, both deposits and withdrawals, are not covertly used to incentivise consumers and SMEs to move away from cash.

[114] https://www.ecb.europa.eu/stats/ecb_surveys/space/html/index.en.html
[115] According to the B&A Consumer Survey, ATMs were used by 73% of Irish adult respondents to obtain cash withdrawals
[116] https://www.gov.ie/en/publication/51315-sme-credit-demand-survey-october-2021-to-march-2022/
[117] https://www.communityaccesstocashpilots.org/

Under section 149 of the Consumer Credit Act 1995, as amended, banks and RCFs are required to notify the Central Bank if they wish to introduce any new customer charges or increase the level of any previously notified charges. While IADs, as unregulated firms, are not subject to section 149, they are subject to the current provisions of the Visa and Mastercard scheme rules, which prohibit access charges[118] for domestic cash withdrawals. However, these rules can be changed at the discretion of Visa or Mastercard.

Going forward, and as a matter of policy, the Review Team considers that Irish consumers should not be charged access fees for withdrawing their own cash via a domestic ATM. This approach is consistent with the Eurosystem cash strategy, where it is stated that cash withdrawals should be free, or incur only a reasonable fee.

It is recognised that prohibiting domestic access charges may impact the future viability of certain ATMs, particularly those in areas of low or modest usage. However there are mechanisms available to address these challenges, such as setting up a scheme like LINK in the UK[119] or the creation of ATM utilities as implemented in The Netherlands and Belgium. These initiatives could support the ongoing sustainability of the cash system, as well as access to it.

ACCEPTANCE OF CASH

Without retailers and other merchants, the cash system would grind to a standstill. For consumers and SMEs to be able to use their cash, it needs to be accepted as a means of payment for the goods and services they want to purchase. Put simply, if consumers and SMEs can access cash, but cannot use it as retailers or others refuse to accept it, cash may become redundant as a means of payment. A study in the UK considered that 'the issue of cash acceptance by merchants and retailers was more likely to drive the death of cash than issues around access.'[120] Although sufficient data is not available, anecdotal evidence suggests the costs to retailers of accepting cash are high,[121] which may incentivise retailers to prefer card payments over cash payments.

Euro notes and coins have the status of legal tender in Ireland. Retail transactions are governed by contract law and in the context of this, where a business places no restrictions on the means of payment it is prepared to accept, it must accept legal tender when offered by a customer to settle a debt that has arisen. However, if a business specifies in advance of a transaction that payment must be in a form other than cash, the customer cannot subsequently claim a legal right to pay in cash, even if that cash is legal tender. This can be achieved, for

[118] Access fees are charges to use a specific ATM and are separate to any bank charges incurred by a customer under the fee arrangements applying to their bank account. Visa and Mastercard scheme rules prohibit domestic access fees unless there is legislation or regulatory provisions permitting them in the relevant jurisdiction. Both Visa and Mastercard permit access fees for foreign transactions.
[119] LINK / Home
[120] https://www.accesstocash.org.uk/media/1087/final-report-final-web.pdf
[121] https://www.gov.ie/en/organisation-information/3c122-retail-banking-review/#dialogue

example, by displaying signs at the cash till and at the store entrance. Therefore, under certain circumstances, retail businesses or service providers can refuse to accept payment in cash.

In Ireland, consumers are already being impacted by some enterprises refusing to accept cash. Challenges range from minor issues such as the inability to purchase a coffee in a café, to being unable to seek insurance from some companies that do not accept cash. People who only use cash therefore have less choice and may not be able to access more competitive products or services where the provider only accepts electronic payments.

The case for policy or pre-emptive legislative actions to protect acceptance of cash in specified circumstances include the potential public policy issues and risks that could arise should retailers (e.g. large supermarket chains) and other public and private service providers (e.g. doctors, hospitals) choose not to accept cash. The case against any such action includes it being regarded as 'a blunt and potential harmful policy as it imposes costs on those merchants who would otherwise reject cash.'[122] These higher costs could be passed through to customers via higher prices. It is also suggested that mandating cash acceptance could also give a commercial advantage to merchants that operate solely online, and thus lead to a further shift away from bricks and mortar to e-commerce.[123] Further consideration of this matter is recommended. The Review Team notes that other jurisdictions, for example the United States, are currently debating whether to legislate for acceptance of cash.[124]

If consumers and SMEs can access cash, but cannot use it as retailers or others refuse to accept it, cash may become redundant as a means of payment

REGULATION OF THE CASH SYSTEM

The Central Bank does not regulate IADs or CITs, with the result that the Central Bank is limited in its powers to assess the resilience of the cash system or ensure it operates effectively in the interests of society and the economy. This situation also limits the Central Bank's ability to proactively engage with all stakeholders in the system to ensure a common strategic objective for the cash system and to address areas of risk and concern such as resilience and ensuring that appropriate contingency measures are in place, if required. The absence of regulation also means a framework has not been developed for the effective management of change in the Irish cash system. In a submission made directly to the Minister for Finance, the Private Security Authority (PSA) highlighted risks that could arise in the CIT sector, and called for it to be regulated.

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[122] The future of cash use: https://www.rbnz.govt.nz/have-your-say/closed-consultations/future-of-money---cash-system-redesign-te-moni-anamata---punaha
[123] 16th ERPB meeting: https://www.ecb.europa.eu/paym/groups/erpb/html/index.en.html
[124] https://cashessentials.org/us-considers-legislation-on-mandatory-acceptance-of-cash/

The Reserve Bank of New Zealand noted that the lack of a framework to manage the evolution of cash can mean that:[125]

- It is not clear where responsibility for outcomes and tasks sit amongst cash system participants.
- There is no vehicle for cash system participants to identify, assess and co-ordinate responses to change.
- There is no way to collectively identify change in the cash system.
- There is no system wide approach to business continuity planning.
- There may be no effective legislative or regulatory powers available to address issues that arise.

As outlined earlier, cash is an important element of the payments system in Ireland. This is also the case within Europe.

In September 2020 the ECB and the European Commission each highlighted the importance of cash. The 19 governors of the ECB approved the Eurosystem Cash Strategy,[126] which addresses safeguarding the future of cash. The strategy identifies responsibilities regarding:

- Availability of cash, whereby the Eurosystem ensures euro notes and coins are available to the public, through the provision of cash services to the retail banking sector.
- Access to cash, whereby the Eurosystem supports public access to services to withdraw and deposit cash, as facilitated by the retail banking sector and other stakeholders.
- Acceptance of cash whereby the Eurosystem promotes acceptance of cash as a means of payment by retailers, traders and other private businesses. When launching its vision for EU retail payments, the European Commission noted its own responsibility in maintaining cash as a legal tender, while promoting the 'emergence of digital payments to offer more options to consumers'.

The Commission also highlighted that it expects EU Member States to "*ensure the acceptance and accessibility of cash as a public good … while acknowledging the possible legitimacy of duly justified and proportionate limitations to the use of disproportionate amounts of cash for individual payments that may be necessary, inter alia, in order to prevent the risk of money laundering, terrorist financing and related predicate offences, including tax evasion*".[127]

Notwithstanding its key role in the payments system, the cash system in Ireland is not subject to full, direct regulatory oversight. In its engagement with the Review Team, the Central Bank outlined that its statutory objectives include the efficient and effective operation of payment

[125] https://www.rbnz.govt.nz/have-your-say/closed-consultations/the-future-of-cash-use---te-whakamahinga-moni-anamata
[126] The Eurosystem comprises the ECB and the national central banks of the Eurozone Member States
[127] https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52020DC0592&from=EN

and settlement systems but noted that it does not have an explicit legal mandate with regard to ensuring access to cash.

Regarding the traditional banks,[128] despite their pivotal role in the cash system and their regulatory status as credit institutions, they are not subject to an express legal responsibility with regard to ensuring access to cash. In this regard, the Eurosystem Cash Strategy makes clear that:

> *'On the basis Banks have privilege to create private deposit money [….] the Eurosystem has to prevent the banking sector withdrawing excessively from cash supply.'*

Due to the reduced role of the regulated banks in the direct provision of cash services, and the increased roles of largely unregulated CIT firms, and unregulated IADs,[129] CITs and IADs have become systemically significant players within the cash cycle. The c. 95% market share of the two main CIT providers is also noteworthy, although the Central Bank advise this level of concentration is not out of line with other countries in the Eurosystem.

Under current regulatory provisions, the traditional banks who outsourced services to CITs remain responsible for those services. The specific requirements are set out in the updated guidelines[130] on outsourcing from the EBA that were published in February 2019 and came into force in September 2019. Under these guidelines regulated firms are expected to have effective governance, risk management and business continuity processes in place in relation to outsourcing, to mitigate potential risks of financial instability and consumer detriment. Outsourcers are also required to bring activities back in-house, if necessary. Effective oversight and monitoring of these critical outsourcing contracts is pivotal to ensuring a seamless response should issues arise with an outsourcing partner.

While, in the context of access to cash, the role of the post office has also increased in importance, it has no specific statutory obligations regarding cash services. An Post is committed under a proximity protocol[131] agreed with Government to guarantee to provide all rural communities with a population of 500 or more to be within 15km of a post office, or for urban communities of 500 or more, to be within 3km. Under the arrangements agreed with the traditional banks, there are limitations on the cash services provided by An Post, meaning

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[128] Defined as Credit Institutions in the context of regulation

[129] CIT firms are subject to regulation by the Private Security Services Act (PSA) 2004 and must meet standards set by the PSA. The Central Bank also monitors CITs in their capacity as Professional Cash Handlers, regarding authenticity and fitness checking and recirculation of euro bank notes. IADs are not subject to any regulatory oversight and are not designated persons for the purposes of the Criminal Justice (Money Laundering and Terrorist Financing) Act 2010, as amended and as such do not fall within the supervisory remit of the Central Bank.

[130] https://www.eba.europa.eu/sites/default/documents/files/documents/10180/2551996/38c80601-f5d7-4855-8ba3-702423665479/EBA%20revised%20Guidelines%20on%20outsourcing%20arrangements.pdf?retry=1

[131] https://www.anpost.com/AnPost/media/PDFs/An_Post_A_new_vision_for_the_Post_Office_Services_in_Ireland.pdf

those services are not equivalent to the service provided by bank branches to their customers. Accordingly, bank customers may still require access to a bank branch for certain cash services.

7.3. Policy considerations for Ireland

The major shift in the traditional banks' role in wholesale and retail cash services has had significant knock on effects to the cash cycle infrastructure and how Irish society withdraws, uses and lodges cash. The substantive changes that have already occurred are based on individual commercial decisions by private enterprises, and while each decision on a standalone basis may have a strong commercial rationale, what has been absent is any overarching assessment of the strategic impact, including the risks and issues, of such decisions on a cumulative basis for the totality of Irish society, the economy, the resilience of the cash system and its potential impact on the stability of the overall payments system.

In terms of key changes, CITs and IADs now play a central role in processing, lodging and withdrawal facilities. The challenges associated with running a business where usage is declining, are factors impacting both CITs and IADs. The sustainability of the IAD business model depends on having their ATMs located in areas of high footfall, where they can boost the revenues generated from interchange fees[132] and currency conversion fees. ATMs in low footfall areas, most likely rural areas, mean revenues can be low and not cover the costs of the ATM. This may cause IADs to close the loss-making ATM, or, in the future if VISA/Mastercard rules change or legislation permits it, seek to introduce charges so that a specific ATM remains viable.[133]

Reduced cash services in branches, along with branch closures and where the post office or credit union alternative is not appropriate, can give rise to additional costs for SMEs, as they either incur the cost of engaging a CIT to manage their cash requirements, or travel longer distances to access cash services in their bank's next nearest branch that offers such a service – taking up valuable time, travel costs, incurring addition risk by storing/transporting cash, whilst also having negative consequences for the environment. Such developments can contribute to retailers and other merchants deciding to operate on a cashless basis, with consequences for consumers, particularly those who for budgeting or other reasons have a continuing preference to use cash.

LEARNINGS FROM OTHER JURISDICTIONS

Throughout Europe, and globally, many developed countries are grappling with the challenges that are emerging from a declining use of cash. In these countries, the development of policy,

[132] When a customer of a particular bank uses an ATM that is owned by another bank or an IAD, the former bank pays a fee to the bank or IAD that owns the ATM. This fee is known as the Interchange Fee.
[133] Under card-scheme rules as governed by Visa and MasterCard, an ATM operator cannot currently charge a transaction fee to domestic debit cardholders who use their debit card to withdraw cash from any ATM in the Republic of Ireland.

strategy and approaches to legislation and regulation of the cash system have been informed by significant consultation with stakeholders, over many years, including industry participants and consumer/business groups. These same countries continue to update and evolve their approaches, guided by their own experience, the experience of others and continuing trends.

Many developed countries are grappling with the challenges that are emerging from a declining use of cash

The Review Team engaged directly with UK, Dutch and New Zealand treasury / central bank colleagues to gain direct insights from developments and experiences in those countries. The UK Government is currently legislating for reasonable access to cash withdrawal and deposit facilities across the UK, as well as the regulation of the wholesale cash infrastructure.[134]

The Review Team also benefitted from its engagement with the Central Bank, which provided additional insights to the Review Team based on the Central Bank's direct engagement with colleagues in Sweden, Latvia and Lithuania.

A key finding is that all jurisdictions have their own unique features and are at different stages in the evolution of their cash infrastructures. In a recent assessment of approaches being taken in other jurisdictions, the New Zealand Reserve Bank (NZRB) concluded that 'there is no emerging global consensus on what constitutes the best suite of cash-system policies.'[135]

On an overall basis, it is therefore clear to the Review Team that legislators and regulators are still learning, and are considering the experiences of others as they develop and trial different approaches within their own countries.

Notwithstanding, there were key themes, principles and lessons that the Review Team identified from its review of the approaches and experiences of others, these being:

- There is broad cross-country consensus that there is a continued societal and economic need for consumers and SMEs to be able to use cash as a means of payment for so long as they need to. There is an acceptance that we are moving to a society where there is less cash, but that does not mean that society is yet ready for a cashless society. Indeed a cashless society may never emerge.
- Consumers and SMEs need to have good access to cash services, with most countries defining this as meaning the ability to withdraw and deposit notes and coin at locations within a reasonable distance and at a reasonable cost.

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[134] Financial Services and Markets Bill 2022
[135] https://www.rbnz.govt.nz/have-your-say/closed-consultations/future-of-money---cash-system-redesign-te-moni-anamata---punaha

- Commercial pressures are beginning to have a significant effect on access to cash, which will become more pronounced as cash demand and usage fall. Commercial organisations may act in their own interest, even when it is to the detriment of society as a whole. Without intervention, market forces will lead to a removal of services and a lack of coordinated action which may be difficult to stop once it has started.[136]
- Where the cash infrastructure has evolved purely from market forces, as a starting point, and before further uncontrolled changes occur, there is a need to preserve consumers' and SMEs' access to cash at current levels. This means that the current points where consumers and SMEs can access cash should, in principle, not become less accessible or more distant. This does not, per se, mean that it is an appropriate objective to preserve the status quo – instead, stakeholders need to focus on ensuring that consumers and SMEs needs are satisfied. Innovative ways to provide acceptable alternative cash services have already been developed, and are encouraged.[137]
- It is important to prepare people for increased digitalisation of services.
- There is a need for the cash infrastructure to be sustainable, thereby contributing to the resilience of the financial system. Where the current cash system was designed for a time of higher cash usage, it must be redesigned so that it is efficient and flexible and can adjust to changes in cash use over time. However, it is not desirable for cash infrastructure downsizing to outpace the decline in cash use, thereby encouraging it.[138]
- There is a need to ensure that there is clear ownership of responsibility for maintaining appropriate levels of cash access, as well as cash system resilience. In most countries, this is a shared responsibility of the Ministry of Finance and the Central Bank, who work in partnership to achieve the policy objectives set by government. However, banks also have a clear responsibility to provide appropriate access to cash services, notwithstanding the cost to them in doing so.
- Up to now, most governments and central banks have sought to achieve their desired societal and system objectives in collaboration with industry stakeholders, using non-binding tools[139] to underpin the agreements reached. However, there appears to be a growing acceptance that legislation may be needed to protect the cash system, and the users of the system, with some countries[140] having already taken the step to legislate and regulate. New legislation and regulation needs to be flexible to allow for changing cash usage levels.
- For the cash system to work effectively, businesses, including retailers, need to continue to accept cash as a means of payment. Businesses will continue to accept

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[136] https://www.accesstocash.org.uk/media/1087/final-report-final-web.pdf
[137] In the UK and NZ, Banking Hubs are being trialled and are proving successful. In The Netherlands, deposit devices such as seal bag machines and cash recycling machines were deployed
[138] nfps-towards-a-new-vision-on-cash-in-the-netherlands-may-2020-pdf.pdf (dnb.nl)
[139] In many countries, tools such as Memoranda of Understanding, or non-binding covenants have been used to date in order to underpin Access to Cash agreements that have been reached between stakeholders, including central banks, government departments, wholesale and retail cash system participants, as well as consumer associations
[140] Sweden implemented its legislation in 2021 and the UK is introducing requirements for banks to provide reasonable access to cash in the Financial Services and Markets Bill 2022.

cash so long as it is in their economic interest to do so, and so long as it is not difficult or expensive to deposit the cash they receive from their customers. A key policy question is whether public bodies should be required to accept or facilitate the acceptance of cash. This is the case in Sweden but there are some examples in Ireland of cash not being accepted for statutorily required documents.[141]

- As policy is developed, it is important that stakeholders are consulted and are listened to, in particular to ensure the cash system that is developed is fair and meets societal needs. National payment councils, often lead by central banks, can be useful to facilitate a dialogue on cash. Enhanced data, providing critical and up-to-date insights, is also important to inform and guide decision makers as they continue to develop policy as cash usage evolves.

7.4. The way forward

Taking into account the specific circumstances in Ireland, the Review Team believes there is a need to develop a new approach to managing Ireland's cash system, in particular to ensure resilience and access to cash. However, Ireland does not need to start from scratch, as we can build on elements of the 2013 NPP and the ECB cash strategy. It is clear that there are common themes and principles that other countries have reflected on, with lessons already learned, and which we can use to propel the development of policy in Ireland so that we do not lose valuable time by considering issues that have already been settled by others. Based on the learnings from other jurisdictions, the Review Team considers that pre-emptive action is needed in Ireland to avoid the situation that emerged in Sweden, where a review found that 'the rapid decline in cash caused issues that regulators were simply not ready to handle, and to which they responded too late.'[142]

Government policy should support the development and maintenance of a sustainable and resilient cash system for as long as cash is needed

Transformation in the way consumers pay for goods and services will likely lead to a further reduction in cash use, but we cannot allow the future development of the payment system to ignore the preferences, or in many cases, the needs of consumers and SMEs who continue to prefer to use cash as a means of payment. Government policy should support the development and maintenance of a sustainable and resilient cash system for as long as cash is needed. Government should also continue to support digital transformation which will likely continue at pace, as new technologies are likely to enable the further and better development of electronic payments. Digitalisation can improve efficiency within the banking sector, and enable some consumers and SMEs to conduct their banking and payments in a convenient

[141] https://www.ndls.ie/learner-driver/fees.html
[142] https://www.accesstocash.org.uk/media/1087/final-report-final-web.pdf

and cost effective way. As identified in the 2013 NPP, digitalisation can also serve as a basis for financial inclusion, as it can provide people with more frictionless and often cheaper access to banking and payments. The basic bank account and digitally enabled payments initiatives should continue to benefit from Government support.

While certain actions must be taken now to avoid further uncontrolled erosion of the cash system, a key Government objective regarding future developments in the payments system (cash and electronic) should be that it must evolve in a fair, orderly and transparent a manner, and the evolution must reflect input from all the main stakeholders. It is critically important that strategic decisions by key players in the system are considered in the wider context, particularly where the consequences of such decisions could lead to a growth in financial exclusion, a disregard for societal and business preferences, or a less resilient payment system, with financial stability consequences.

The Review Team recommends, as outlined below, that the Government legislates to provide for reasonable access to cash services for consumers and SMEs. In the immediate and short term, it is expected that the principle responsibility to ensure reasonable access to cash will fall on banks that meet objective criteria, which could include a bank's share of the current account market, and the amount of deposits in those current or other accounts.

Given the significant developments in the payment system since the NPP was published in 2013, it is appropriate that a new National Payments Strategy is now developed that sets out a roadmap for the future evolution of the entire payments system taking account of developments in digital payments. This new strategy can also guide future changes to the legislative Access to Cash criteria and to address additional issues such as the use of cheques as well as acceptance of cash by both the private and public sectors. The development of the strategy should be led by the Department with the support of the Central Bank, and in consultation with key stakeholders.

The Review Team recommends that:

Recommendation 7-1

The Department of Finance should develop Access to Cash legislation, and prepare heads of a bill in 2023 to:

- Require banks that meet objective criteria to provide reasonable access to cash. "Reasonable access to cash" criteria will be defined in consultation with the Central Bank and other stakeholders and the initial objective of the legislation will be to preserve access at December 2022 levels; and
- Provide that the criteria can be changed by the Minister for Finance by regulation, based on research and advice from the Central Bank. This will allow for the further evolution of the cash infrastructure to be managed in a fair, orderly, transparent and equitable manner for all stakeholders.

Recommendation 7-2

Pending development of this Access to Cash legislation, the banks should seek to preserve consumers' and business' access to cash services at December 2022 levels.

Recommendation 7-3

The Department of Finance should prepare heads of a bill in 2023 to require ATM operators to be authorised and supervised by the Central Bank.

Recommendation 7-4

The Department of Finance should prepare heads of a bill in 2023 to provide the Central Bank with responsibility and powers to protect the resilience of the cash system including the authorisation and supervision of cash-in-transit firms in respect of their cash handling activities and related financial services.

Recommendation 7-5

The Department of Finance should lead on the preparation of a new National Payments Strategy to be ready in 2024. The strategy should set out a roadmap for the future evolution of the entire payments system, taking account of developments in digital payments, the use of cheques and other issues, and guide how future changes should be made to the legislative Access to Cash criteria. The Strategy should be informed by, and aligned with, the retail payment strategies of both the EU Commission and the Eurosystem. The Strategy should also consider and consult on whether:

- To legislate pre-emptively to give the Minister for Finance the power to require certain classes of firms, sectors or sub-sectors to accept or facilitate (to an appropriate level) the acceptance of cash; and
- If it should be Government policy that public bodies should accept or facilitate the acceptance of cash for the payment of goods, services, taxes, levies, fees or charges.

8. Access to banking services

The branch banking model has been evolving from as far back as the 1980s. Initially, computerisation facilitated the centralisation of back office functions, while the introduction of telephone banking provided a further channel, with extended opening hours for customers to engage regarding their day-to-day banking needs.

Over time, other core activities, such as credit underwriting[143] were relocated to regional settings, to support the development of greater specialisms within credit, with more consistent credit assessment processes providing more consistent outcomes for customers. To better meet customer needs, many of the banks opened local business centres to provide specialised relationship management to SMEs, with larger corporate customers served by centralised corporate banking teams.

All of these developments reduced the extent to which branches were fully involved in all aspects of the customer relationship. Increasingly, branches became cash offices and locations where personal customers could open accounts, obtain financial advice, engage with bank customer service staff regarding queries and issues, pay bills and purchase foreign exchange. Branches were also pivotal in the mortgage application process, as typically customers dealt directly with a bank mortgage adviser in their local bank branch.

Since the GFC, banks sought to simplify and streamline their business models even further by investing further in technology, and enhancing their digital capabilities. Online and digital banking became more prevalent. This change sought to capitalise on some customer's growing acceptance of, and in some cases a preference for, digitally enabled interactions with their banks. Digital transformation is also attributable to banks' responding to competition from digitally-enabled, non-bank competitors, who mainly operate in the payments segment of the market. The banks benefitted from this transition to digital, as they gained significant operational efficiencies and cost savings.

8.1. The impact of branch changes

By and large, the banks have been successful in transitioning large numbers of their personal customers to the new banking channels on offer, which has resulted in a significant reduction in branch footfall. Digital channels (mobile app, or online banking) now dominate in terms of being the main form of contact customers have with their main bank,[144] offering extended banking hours to customers and the opportunity to conduct business without the need to travel to a branch. These changes offer significant advantages for customers, many of whom (due

[143] Where lending would exceed the lending limit of the branch manager.
[144] B&A Consumer Survey - the mobile app was the main form of contact for 41% of respondents; online banking (non-app) was the main form of contact for 29%: https://www.gov.ie/en/organisation-information/3c122-retail-banking-review/#consumer-survey-results

to work and other commitments) would otherwise be unable to conduct their banking business. This is evidenced by the fact that less than a quarter of consumers consider bank branches as their main form of contact.[145] Of those who do interact with their bank using the digital channels that are on offer, customer experience is generally positive.

Of those who do interact with their bank using the digital channels that are on offer, customer experience is generally positive

However, concerns have been raised about the effect of the reduction in services available in certain branches, as well as the closure of branches on those who need in-person services. In the same way as it is the older population and those that are less well-off that have a greater dependency on cash, so too is it the case that this same demographic has greater reliance on bank branches to conduct their banking business.[146] That said, it is also true that for certain queries, even the most digitally enabled customers will visit their branch for assistance.

With regard to reduction in services available in branch and branch closures, issues arising include:

- Consumers and SMEs need to travel further, with inevitable increased cost, to access their nearest branch. These longer distances create significant challenges for those who are less able to move to online banking, or for those who do not have the ability or means to travel to the next nearest branch. These longer travel distances also have negative climate impacts.
- Consumers who are unable to use online or digital channels, or cannot or are unable to engage with the new channels on offer, risk being excluded from the financial system. This may cause them to rely on the help of others, creating a financial dependency that could be abused.
- People's experience of the remote channels on offer, such as telephone banking, is not always positive. Long waiting times cause frustration, and dissatisfaction levels can be made worse if the issue is not resolved in the customer's first call with the call centre. It can often be the case that the customer is transferred to other call centre operations, often with additional waiting times, and often having to explain the same issue multiple times to different call centre staff. It is possible that dissatisfaction levels with the remote services on offer are driving some people to continue using branches.
- Those who use the branch the most, namely those who are older, were least satisfied with the service they could get at their branch. Dissatisfaction levels were mainly attributed to poor customer service, not enough staff resulting in long queues and slow service.[147]

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[145] B&A Consumer Survey
[146] B&A Consumer Survey - monthly branch visitors are likely to be 55+ and from the less well off. 55% of the 65+ age group consider the in-person visit to the bank branch to be their main form of contact with their bank.
[147] B&A Consumer Survey

- For SMEs, feedback from the Dialogue suggested the decline of the branch has resulted in the loss of good banking relationships, meaning SMEs no longer have a contact point in the bank who 'knew their business.' It was also suggested, amongst other things, that it was difficult to talk to someone who had expertise in banking for SMEs, and that online banking was not suitable for all banking transactions, particularly larger transactions. Other feedback suggested that online banking is too complex for the needs of smaller SMEs. These issues as they relate to SMEs are considered are further in the chapter on SME Credit.

Whilst the Consumer Survey found that branches are most used by older or less well-off consumers, it would be wrong to assume that branches do not play an important role for other customers. The Consumer Survey found that only 7% of respondents never visit a branch, whilst 41% of those aged 25-35 visited a branch to speak to someone regarding a specific product, such as a mortgage, loan or overdraft. Other reasons for consumers visiting a branch included paying bills, financial advice, transferring money, as well as lodging/withdrawing cash.[148]

Also of interest is research from the CCPC suggesting that of the consumers who had already switched banking providers from Ulster Bank or KBC, just over a quarter said the availability of a local bank branch was the main reason for choosing their new provider.[149]

8.2. Regulation of branch closures and alteration of services

Under the CP-Code general principles, regulated firms are obliged to act honestly, fairly and professionally and with due skill, care and diligence in the best interests of their customers. The minimum standards of behaviour set by the CP-Code apply regardless of the delivery method of the relevant banking services.

When a bank intends to amend or alter its range of branch services, or close a branch, it is required under the CP-Code to provide notice to customers – one month in the case of an alteration in service, and two months in the case of a branch closure. A bank is required to give notice to the Central Bank when it is closing a branch, but is not required to give any notice to the Central Bank when altering a service.

When making a commercial decision to alter branch services, or close branches, there is no explicit regulatory requirement on banks to assess the impact on customers. There is also no regulatory requirement for banks to conduct an ex- post assessment and review of the impacts on customers where their specific branch has been closed or where services have been changed, to determine customer's satisfaction with or experience of the alternative channels

[148] B&A Consumer Survey
[149] https://www.ccpc.ie/consumers/2022/11/02/ccpc-publishes-second-phase-of-current-account-switching-research/

that replaced the in-branch offering. As such, there is no requirement on banks to have supporting data or detailed knowledge regarding the impact of branch closures on their customers, or the suitability of the alternative offering. With the result that it is not a requirement that experiences from changes in one branch location inform decisions in others.

In addition, the CP-Code does not have any specific requirements in relation to customer service standards. By contrast, firms in other regulated industries such as telecommunications have to abide by minimum service levels, which are clearly defined, and can be fined for failures.

8.3. International good practice and lessons from abroad

The Review Team is concerned that fewer branches, or less services at branches, could cause the financial exclusion of customers, including customers in need of additional support, particularly where the alternative channels being put in place are not adequately accessible or effective. As identified by the Central Bank earlier this year call waiting times on the customer support phone lines in the traditional banks need improvement.[150]

The Central Bank is currently reviewing and updating the CP-Code, to 'address emerging trends and risks across the rapidly changing financial services landscape, to ensure that it continues to deliver strong protections for consumers into the future.'[151] This review is welcomed, though as the review is not expected to be concluded until 2024, the Review Team considers that, in the interim, the retail banking sector should take steps to ensure customers are not placed at risk of financial exclusion, in particular due to poor customer service standards across key access channels.

The retail banking sector should take steps to ensure customers are not placed at risk of financial exclusion, in particular due to poor customer service standards

In considering the measures that could be taken, and the basis for requiring banks to take such measures, the Review Team considered the High-Level Principles on Financial Consumer Protection ('OECD Principles'), which are expected to be adopted shortly.[152] Discussed further in the chapter on Consumer Protection, the OECD Principles are considered to be the global international standard for consumer protection, and firms in the sector are expected to do their utmost to fully implement them.

Relevant themes and issues being addressed by the OECD Principles are access and inclusion, the impact of digitalisation, as well as financial literacy and the specific need for equitable and fair treatment of consumers who may be vulnerable. The OECD Principles

[150] https://www.centralbank.ie/news/article/press-release-central-bank-requires-improvements-to-banks-support-phone-lines-18-February-2022
[151] https://www.centralbank.ie/news/article/speech-derville-rowland-bpfi-membership-forum-16-mar-2021
[152] https://www.oecd.org/finance/high-level-principles-on-financial-consumer-protection.htm

recognise that the digitalisation of banking services can negatively impact vulnerable customers, and that the retail banking sector has a responsibility to ensure that consumers remain included in the financial system.

Specifically with respect to the principle on *Access and Inclusion*, the OECD Principles state:

> *'Governments, oversight bodies and financial service providers and representatives should seek to support consumers' access to and use of financial products and services where possible and promote an inclusive financial system. Achieving these objectives requires both addressing barriers that prevent consumers from accessing and using financial products and services in the formal, regulated financial system, as well as ensuring consumers remain included in the financial system for example, in the event of financial hardship. Digitalisation should be leveraged where relevant to enhance financial access and usage.'*

When addressing the specific issue of vulnerable consumers, the new (relevant) principle states that 'the enhanced use of digital technology to support decision making by financial service providers should not lead to inappropriate or discriminatory outcomes for consumers.'

This same principle goes on to say:

> *'Special attention should be paid to the treatment of consumers who may be experiencing financial vulnerability.'*

REGULATION IN OTHER COUNTRIES

To inform the Review Team's view on how to address the impact on consumers of branch closures and reduction in branch services, the Review Team considered how regulators in other countries[153] approach these issues.

Some key observations were:

- The decision to close a branch, or alter the service provided in a branch, is considered to be a commercial matter for the bank/financial institution.
- Guidelines on branch closures vary in how prescriptive they are. One regulator required the bank that is closing a branch (or altering a service) to engage with

[153] The Review Team considered the approaches take by the UK's Financial Conduct Authority and also the Financial Consumer Agency of Canada

customers and communities, and to incorporate the feedback from those engagements into the bank's decision making processes. The bank that is closing the branch was also required to demonstrate to their regulator that they had taken measures to address concerns raised by stakeholders.[154]

- Regulators required banks to take specific measures to assist the vulnerable, who are typically identified as older, and/or lower income customers.

In the context of consumer protection, the Review Team considers that the UK regulator's new Guidelines[155] appear to have a more explicit and broader remit than other regulators in that they are more prescriptive in the type of measures they expect banks to adhere to when considering branch closures. The UK regulator's guidelines also empower them to request a bank to delay a planned branch closure if it is not satisfied with the measures taken by the bank.

OTHER LESSONS

The retail banking sector in other countries, such as New Zealand and the UK, have piloted Banking Hubs to see if they can address the needs of customers following the closure of bank branches in certain locations. Banking Hubs offer cash services but also other bank services, as their aim is to maintain a range of banking services in the communities they serve. A review in the UK[156] outlined a number of useful findings in relation to the non-cash bank services offered by Banking Hubs, including:

- Banking Hubs, where one staff member from each of the main banks offered drop-in support for one day a week, enabled important face-to-face support, particularly where there were more vulnerable populations such as elderly customers.
- Customers typically used the hubs to obtain the support of staff for ongoing account management, such as not knowing how to make a transaction online. Asking for help to transfer money was also a common theme, 'with many customers concerned about making a mistake and losing their money' if they used digital services.
- It is important that the support staff who deal with customers are selected carefully, and appropriately trained to enable them support the more financially vulnerable.
- Not every community needs or wants an expensive face-to-face service. The UK Review[157] cautioned against the assumption that Banking Hubs were the 'silver bullet,' as they are not. Interventions that cater for the specific needs of the community, having been designed in partnership with the community, were the most successful.

[154] https://www.fca.org.uk/news/press-releases/fca-updates-guidance-branch-closures
[155] https://www.fca.org.uk/news/press-releases/fca-updates-guidance-branch-closures
[156] https://www.communityaccesstocashpilots.org/
[157] Ibid

In New Zealand, a recent pilot of Banking Hubs has proven successful and is being extended.[158]

8.4. Ensuring customers are not financially excluded

The onus is on key stakeholders to collectively bridge the digital divide and ensure consumers are not left behind during the banks' digital transformation process

Until customers are ready for a complete transition to digital or remote services, digital transformation needs to be balanced with appropriate preservation of in-person banking services. At present, the transition to digital is at risk of outpacing consumers' and SMEs' ability to use the alternative channels being offered by banks.

Also, as outlined in the chapter on SME Credit, the quality of digital and telephone delivery is not sufficiently customer centric, so even where customers are willing to engage through those channels, issues arising during the process lead certain customers to visit a branch to resolve those issues or seek assistance to complete transactions.

Accordingly, where customers either cannot access remote channels, or where they do but the service standards are poor, there is a significant and increasing risk that consumers become excluded from the financial system, or that the service standards are insufficient and fail to meet customers' reasonable expectations.

This does not mean that banks and others should not continue to develop their digital channels. Many customers benefit from the banks' enhanced digital and online offering. They can help with financial inclusion, as additional contact channels can enable more consumers access the financial system. Digital or online banking can also reduce the cost of doing business, as SMEs save time and cost by transacting their banking business from their own premises. Also, an effective and efficient telephone banking channel has many advantages, as person-to-person engagement is often the most appropriate way to deliver strong customer service, whether in the provision of new products or resolving customer queries. The increased use of online video appointments (via Zoom, etc.) with customers also brings many of the advantages of face-to-face engagements, and it will be important for the retail banking sector to expand the use and efficiency of these options, including with regard to account openings.

At present, the transition to digital is at risk of outpacing consumers' and SMEs' ability to use the alternative channels being offered by banks

[158] https://www.nzba.org.nz/2022/08/05/banks-expand-regional-banking-hubs-trial/

Action is therefore needed to ensure there is continued access to retail banking products and services for those who need them. The onus is on key stakeholders, principally the banks, the regulator and the State to collectively bridge the emerging digital divide and ensure consumers are not left behind during the banks' digital transformation process.

RESPONSIBILITY OF REGULATED FINANCIAL SERVICE PROVIDERS

In line with the draft OECD Principles, financial service providers must fulfil their duty to ensure consumers remain included in the financial system.[159] In practice, the Review Team believes that this must mean that before a bank takes the decision to close a branch or significantly change the services offered, they must assess, analyse and understand the needs of customers currently using the branch, the potential impact on customers including those that are at most risk of financial exclusion, as well as the appropriateness and viability of the alternative channels that are being put in place. And assuming the risks to customers are appropriately identified and mitigated, having implemented the change, the banks, or indeed any other provider of retail banking products and services, must ensure their channels are effectively managed, and their operation retrospectively reviewed, to ensure customers' reasonable expectations are met and that customers do not become excluded.

Effective solutions can be developed when banks are collectively minded to do all they can to help their customers

Whilst the decision on the location of, and services offered by, bank branches remains a commercial decision for each bank, the taking of additional measures, as outlined above, will help mitigate the impact on consumers and SMEs. The Review Team has also outlined above how the development of Banking Hubs offered valuable and effective solutions for customers who need to engage with their bank face-to-face. Whilst not the panacea, the Banking Hubs demonstrate that innovative and effective solutions can be developed when banks are collectively minded to do all they can to help their customers, and where good engagement takes place with customers and communities to identify solutions that meet their needs.

The Review Team recommends that:

Recommendation 8-1

While complying with competition law requirements, the retail banking sector should increase its levels of collaboration, wherever possible, to reduce costs and improve/retain customer service levels. Potential areas include:

- Shared banking hubs in locations where all branches have closed; and
- Developing utility entities in areas such as ATM provision and operation

[159] Governments, oversight bodies and financial service providers and representatives should seek to support consumers' access to and use of financial products and services where possible and promote an inclusive financial system.

A NEW CUSTOMER CHARTER

In industry generally, as well as in utility companies and the public service, it is common for customer charters to be developed that outline a statement of the standards of service that customers can expect to receive when engaging with them. These standards are measurable, and typically address the full range of customer services, including for example, turnaround times for decisions, standards customers can expect when engaging, whether by telephone, email or at their premises, as well as how customers can expect complaints to be managed. In some cases, customers are given financial compensation where the firm does not meet the standards it sets for itself and the firms themselves may be fined by their regulators.

The Review Team considers that all regulated providers of retail banking products and services, including retail credit firms and credit servicing firms, should be required under the revised CP-Code to develop and publish comprehensive customer charters that outline clear and measurable customer service standards, and include a clear objective that customers do not become excluded as a consequence of changes in their engagement channels, or due to the manner in which those channels are managed.

As part of its normal supervisory activities, the Review Team considers that the Central Bank should review a firm's compliance with the high standards that firms must set out in their customer charters, which should also be Board approved. This will enable the Central Bank supervise the firm against these high standards, and take action where material issues arise.

The primary responsibility for ensuring good customer service standards rests with the banks and providers of retail banking products and services

While this Recommendation is a matter for the Central Bank to consider in its reform of the CP-Code, the Review Team notes that it will be 2024 before the revised CP-Code will be adopted. The Review Team considers that some reforms, as outlined in the Recommendation, should be implemented ahead of the review of the CP-Code being completed, but recognizes that the primary responsibility for ensuring good customer service standards lie with the banks and all providers of retail banking products and services. As such, and pending changes that may ultimately be made to the CP-Code, the Review Team recommends that the retail banking sector implement the recommendations below on a voluntary basis as soon as possible.

If in the course of its review of the CP-Code, the Central Bank reaches the conclusion that existing legislation does not permit the mandatory introduction of requirements for customer charters, then draft legislation should be prepared to address this as a matter of urgency.

The Review Team recommends that:

Recommendation 8-2

The Central Bank should, in its review of the Consumer Protection Code and, unless otherwise stated, in advance of the completion of its Consumer Protection Code review:

- Require banks to submit robust, board approved, assessments to the Central Bank when they are planning to significantly alter the services provided through branches or when planning to close a branch. These assessments should examine the impact on customers, the suitability of alternative service provision arrangements, and the plans for migrating customers to them, especially at-risk customers. Such assessments, excluding commercially sensitive information, should be published by the relevant bank.
- Require ex-post assessments by banks, to include a survey of impacted customers, nine to 15 months after the change or closure and a requirement to rectify material issues.
- Increase the minimum notice period required to four months (currently one) for significant banking service changes (e.g. going cashless) and to six months (currently two) for branch closures and credit institutions leaving the market.
- Require, in the revised Consumer Protection Code, all providers of retail banking products and services to set out and publish customer charters, incorporating service standards. In advance of changes that may ultimately be made to the Consumer Protection Code, the Review Team recommends that all providers of retail banking products and services implement this recommendation on a voluntary basis.

9. Mortgages in Ireland

For a large number of people in Ireland, obtaining a mortgage is the only pathway available to them to own their own home. In recent years, there has been much discussion of the challenges that people face, such as the price of housing in Ireland, interest rates and regulation. Since the GFC, new regulation has placed limits on the amount people can borrow as we know from experience that borrowers with high levels of debt relative to their income or to the value of their house are more likely to face financial difficulties in challenging economic times.[160]

The decision of Ulster Bank and KBC to leave the Irish market has given rise to concerns that people will now have less choice. There are concerns that the reduction in the number of mortgage providers could reduce the pressure on the remaining lenders to offer competitively priced quality products, enhance innovation and maintain high service quality.

9.1. Scale of the mortgage market

The Government's *Housing for All* plan estimates that Ireland will need an average of 33,000 new homes to be provided each year from 2021 to 2030.[161] Demand for housing is underpinned by Ireland's strong demographics. Our population was estimated to be 5.1 million in April 2022, which is its highest level since 1851. Of this population, 1.4m (27 %) were in the age group 25-44,[162] which is a key group in the market in relation to house purchase. Demand for housing is also strengthened by reductions in household size.

The increasing supply of housing, underpinned by strong demand, will result in a continuing strong requirement for mortgage credit for a number of years. Of the 57,995 houses purchased in 2021, BPFI figures show 34,476[163] relied on a mortgage to fund the purchase.[164] According to the BPFI, the average mortgage drawn down in 2021 was circa €240,000.[165]

It is clear that this demand is primarily coming from people looking to buy a home, and not investors. Of the total €10.8 billion mortgage drawdowns in 2021, first-time-buyers (FTBs) accounted for 53% of the total, whilst second and subsequent buyers (SSBs) accounted for 35%. People re-mortgaging with another lender accounted for 9%, whilst people getting mortgage top-ups or purchasing an investment property accounted for just 3%.[166]

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[160] https://www.centralbank.ie/financial-system/financial-stability/macro-prudential-policy/mortgage-measures
[161] gov.ie - Housing for All - a New Housing Plan for Ireland (www.gov.ie)
[162] https://data.cso.ie/
[163] https://bpfi.ie/publications/bpfi-mortgage-drawdowns-q4-2021/
[164] https://www.centralbank.ie/financial-system/financial-stability/macro-prudential-policy/mortgage-measures/new-mortgage-lending-data-and-commentary
[165] The latest data from the BPFI shows the average mortgage drawn down for the first nine months on 2022 has risen to c. €263,000: https://bpfi.ie/publications/bpfi-mortgage-drawdowns-q3-2022/
[166] https://www.centralbank.ie/financial-system/financial-stability/macro-prudential-policy/mortgage-measures/new-mortgage-lending-data

The Review Team considers that increased demand for mortgage credit will come from consumers who want to use the equity in their home to fund the retrofitting of their properties, meaning mortgage top-ups could increase over the next decade.

With supply increasing, and notwithstanding the current economic headwinds, demand is likely to remain strong. The Review Team considers that there will be significant opportunities for lenders to expand their mortgage portfolios in the near term. This opportunity will be stronger for the remaining mortgage providers in the market given that Ulster Bank and KBC will not be competing for this stream of new business. Improved balance sheet health, in terms of capital, liquidity, and non-performing loans, means that the traditional banks are in a strong position to support mortgage growth.

9.2. Evolution of the mortgage market

Following the GFC, several traditional banks in foreign ownership scaled back or left the Irish market. Actions taken by the State following the GFC included amalgamations and closures of banks that resulted in a smaller, but more stable banking system. The consolidation of the retail banking sector resulted in the number of traditional banks who offered mortgage products reducing from twelve to five. This will now reduce to three, namely AIB, BOI and PTSB, following the announcements by Ulster Bank and KBC.

The traditional banks in Ireland are the main providers of mortgage finance to Irish consumers. At end-2021, they accounted for €90bn (80%) out of a total stock of €112bn.[167] In 2021 they accounted for just over 86% of all new mortgage lending which amounted to €10.8bn.[168] Of this 86% of new lending, AIB (including its subsidiaries EBS and Haven), BOI and PTSB accounted for 28%, 23% and 18% respectively with KBC and Ulster Bank making up the balance. The combined market share of new business for the three traditional banks remaining in the market will increase with the withdrawal of KBC and Ulster Bank.

In recent years, non-banks have increased their share of new mortgage lending. Over the period 2018-2021, they increased their share of new mortgage lending from 3% to 13%.[169] The three most significant non-banks are Avant Money, Dilosk and Finance Ireland and an overview of each of these is provided in Box 1 below.[170]

[167] https://www.centralbank.ie/statistics/data-and-analysis/credit-and-banking-statistics/mortgage-arrears
[168] https://www.centralbank.ie/financial-system/financial-stability/macro-prudential-policy/mortgage-measures/new-mortgage-lending-data-and-commentary
[169] https://www.centralbank.ie/docs/default-source/publications/financial-stability-notes/non-bank-mortgage-lending-in-ireland-recent-developments-and-macroprudential-considerations.pdf?sfvrsn=f0ab911d_8
[170] Other non-bank mortgage providers include Investec and Spry Finance.

The credit union sector also offers mortgages to its members. However, with total stock of c. €260 million across the sector as at end-2021, they remain a small player in Ireland at present. Local authorities also provide mortgage finance.[171]

Box 1 - Overview of the main non-bank mortgage providers October 2022

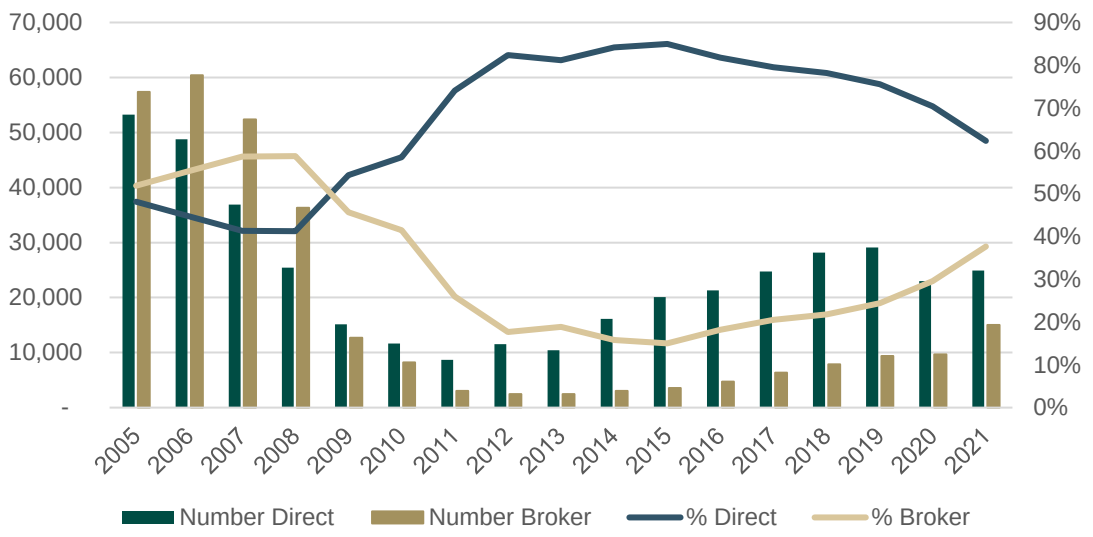
Avant Money	• Owned by Spanish banking group – Bankinter • Started offering mortgages in Ireland in 2020 • Product suite includes long term fixed rates up to 30 years
Dilosk	• Dilosk is a privately owned company which trades under the ICS brand • Dilosk entered the mortgage market in 2014 with the acquisition of the ICS brand and distribution platform and a portfolio of mortgages from BOI • Dilosk offers owner-occupied and Buy to Let (BTL) mortgages with fixed rates of up to 15 years
Finance Ireland	• Founded in 2002, Finance Ireland is a privately owned financial services group • In addition to offering residential mortgages, business lines include motor finance, asset finance and leasing, commercial mortgages and agri-finance • Residential mortgage product suite up to recently included fixed rate mortgages up to 20 years. Their current fixed rate are for three and five years.

The traditional banks offer their mortgage products to consumers through direct channels (namely through branches, online or via telephone) as well as through broker channels. The non-banks operate almost exclusively through broker channels. Brokers must be regulated by the Central Bank either as a mortgage intermediary or a mortgage credit intermediary.

The number and share of mortgages originated through brokers dropped significantly following the GFC but, as ***Figure 9*** illustrates, recent trends suggest that consumers are increasingly using brokers to obtain a mortgage. Statistics suggest that 62% of homebuyers (FTB and mover purchaser) applied for a mortgage through the banks' direct channels in Q1 2022, which compares to 85% in 2015.

[171] https://localauthorityhomeloan.ie/

Figure 9 - Mortgage drawdowns – direct versus broker channels since 2005



Source: BPFI

9.3. Competition in the mortgage market

Concerns have been raised, including through responses to the Public Consultation, that the reduction in traditional bank mortgage lenders provides less choice for consumers.

However, there is a need to be mindful of our recent and difficult experience. The final report of the Banking Inquiry commented that 'the introduction of new and aggressive lending arising from increased competition in the period leading up to the crisis ultimately adversely affected the customer.'[172] In the period leading up to the GFC, there were 12 traditional banks offering mortgages to Irish consumers who were all trying to achieve scale in a small market. The outcome of this was a lowering of underwriting standards and the provision of excess credit to people who could not afford it.

As highlighted in the International Comparison at Table 6 below, it is not unusual for a small number of providers to dominate the mortgage market. The departure of Ulster Bank and KBC represented a significant opportunity for a new provider to enter the market and purchase their combined c. €24bn mortgage portfolios, enabling it to build immediate scale, however this did not happen.

Similarly, before the Ulster Bank and KBC announcements, and despite EU single market and passporting rules that enable banks across the EU and EEA sell their products and services

[172] https://inquiries.oireachtas.ie/banking/

without barriers into Ireland, apart from Bankinter (trading through its non-bank subsidiary Avant), no other mortgage lender has availed of this market opportunity.

Table 6 International comparison – market share of dominant mortgage providers

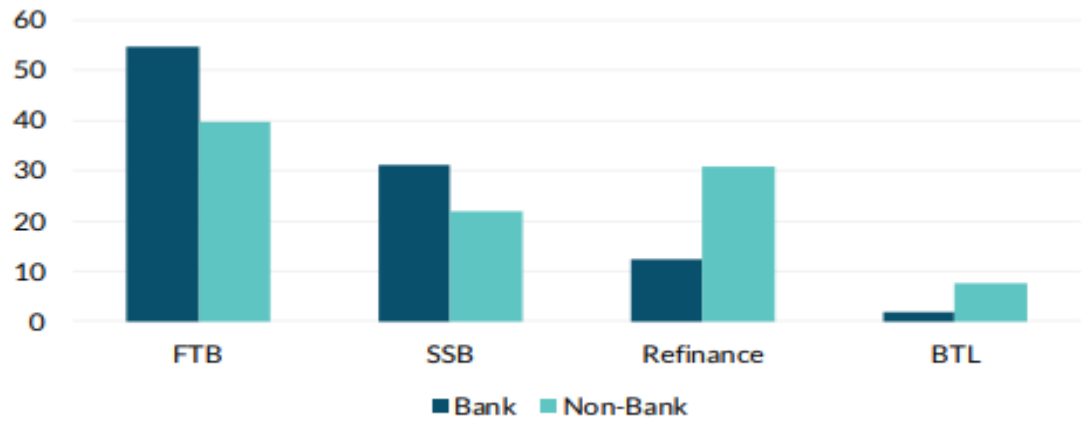
Country	Number of dominant providers	Market share
Ireland	5	86%
Portugal	5	92%
Finland	3	77%
New Zealand	4	85%
Netherlands	3	49%

Source: Department of Finance, International Comparison

Whilst changes can be made, such as more efficient switching processes, to make the Irish market more attractive to new entrants, it seems unlikely, due to countervailing factors such as the scale of the Irish market and differing legal systems, that a new mortgage lender of scale will enter the Irish market in the near future. As such, while noting the competition from non-banks, the Review Team expects that the Irish mortgage market will remain concentrated and, notwithstanding the role played by non-banks in recent years, largely dominated by the three remaining traditional banks.

The Review Team expects the non-bank sector to continue to play an important role in ensuring the Irish mortgage market remains competitive. Based on research from the Central Bank, the non-banks play a particularly important role in the refinance and BTL segments of the market (see Figure 10), although their market shares in the FTB and SSB segments have also grown significantly since 2018.

Figure 10 - New Lending by purpose as a percentage of total new lending 2020-21



Source: Central Bank

In the short to medium term, there is a possibility that the non-banks may retrench and lose market share. This is due to their funding models, which leaves them vulnerable to developments in the global financial markets. With the exception of Avant, which obtains its funding from its parent company Bankinter, the other non-banks in the Irish market rely on wholesale funding which is leaving them more sensitive to rising interest rates and market sentiment globally. This was a point highlighted in a recent research note issued by the Central Bank in relation to mortgage lending by non-banks.[173]

However, as the market develops through the economic cycle, the Review Team expects that opportunities exist for new non-banks to enter the market and for the existing players to continue to play an important role in developing new products, as they have done to date, providing consumers with more choice. The €1bn in total funding available to two non-bank mortgage lenders by BOI, which is a condition of the CCPC's approval of the bank's acquisition of certain assets and liabilities of KBC Ireland, is a positive development, particularly in light of the current conditions in the financial markets.

The chapter on Competition outlines potential barriers to entry to the Irish banking market. In the context of mortgages, this includes the relatively small size of the market, the low level of switching, relatively higher capital requirements, and the persistence of Long Term Mortgage Arrears (LTMA)[174] including slow recovery of collateral when mortgages are in default.

[173] https://www.centralbank.ie/news-media/press-releases/non-bank-lending-to-mortgage-borrowers-has-grown-in-importance-in-recent-years-26-may-2022
[174] LTMA are defines as accounts in arrears for more than 1 year.

Since the GFC, Ireland has seen more mortgage providers leave rather than enter the market. Whilst the reducing number of mortgage providers means less consumer choice, there is little evidence to suggest that this reduced choice means that Ireland's mortgage market is uncompetitive.

As high interest rates in a market can indicate poor competition, high levels of NPLs, capital requirements, and weak collateral realisation are likely to have played a more important role, the Review Team examined this issue, which is discussed further below, and concluded that there are largely Ireland specific issues that are driving the current level of interest rates. High levels of NPLs, capital requirements, and weak collateral realisation are likely to have played a more important role than the level of competition.

NEXT STEPS

To ensure that the mortgage market remains competitive, the Review Team has made a number of recommendations, which are included in the chapter on Competition. These recommendations have focused on ensuring that prudent and efficient access to the market is provided to providers who identify a market opportunity, who can meet the regulatory requirements. However, having gained access, it is important that they can build scale through gaining market share from new opportunities as well as efficient switching processes and this is discussed below. Furthermore, forthcoming legislative amendments and a separate Recommendation on supporting the credit union sector will help the credit union sector to compete in the mortgage market.

9.4. Mortgage switching

Recent Central Bank research has highlighted that mortgage switching is low in Ireland.[175] This applies equally to borrowers switching provider, or switching to a lower rate with their existing provider. More recent data does show a significant increase in re-mortgaging, apparently driven by the increasing interest rate environment and Ulster Bank and KBC leaving the Irish market. While it would be positive if this behaviour becomes embedded among Irish consumers, it is too early to make any such finding. Indeed it is likely that there will be a return to lower levels of switching when the interest rate environment stabilises and this is the assumption underpinning the following text.

With respect to consumers switching their mortgage provider, the recent research, which focused on eligible accounts,[176] found that three in five mortgage borrowers could save €1,000

[175] https://www.centralbank.ie/docs/default-source/publications/economic-letters/economic-letter-12-mortgage-switching.pdf
[176] For the purposes of the research, mortgage accounts eligible for switching were defined as those on a variable rate (excluding tracker mortgages); or, a on a fixed rate with a remaining fixed term of less than 12 months. Eligible accounts were further restricted to accounts that had a current outstanding balance of at least €30,000, a loan-to-value ratio below 90% with no outstanding mortgage arrears and classified as 'performing'.

per annum in the first 12 months and €10,000 over the remaining mortgage term by switching.[177] At the time the research was completed, there were a total of c. 874k mortgage accounts of which c. 182k (20%) were defined as eligible. Despite the potential savings, the research found that just 2.9% of borrowers switched their mortgage to another provider in H2 2019. One of the reasons given for the level of switching was that borrowers perceive the process as too long and complicated.

A separate piece of Central Bank research[178] focused on borrower behaviour in relation to refinancing with their existing provider. The research examined cases where borrowers received a cost free offer from their existing mortgage provider to avail of a lower interest rate due to a reduction in the loan-to-value ratio. For the sample of 46k mortgage borrowers that were analysed, only 33% accepted the offer. It was estimated that the average first year saving could have been €490, with an average saving of €5,400 over the remaining life of the mortgage. Taking into consideration the fact that this type of product switching does not require conveyancing, the low level of take-up is significant.

Over a number of years, the Central Bank and the Department have endeavoured to better understand the reasons for these low levels of switching. Collectively, the research suggests that 'the perceived 'barriers' to switching cover issues such as a lack of knowledge on the costs or potential savings of mortgage switching and the level of complexity of the process (involving, as it does, solicitors and conveyancing), in addition to a fear or uncertainty about the outcome of the process.'[179]

These messages were reinforced by the Consumer Survey, which found that consumers perceived switching mortgage provider to be difficult compared to other financial products. The perception that it would be too expensive to switch was not prominent.[180] Of interest is that these perceptions run contrary to the experience of people who did actually switch, though as sample numbers in the Consumer Survey were small, this finding may not be representative.[181]

MEASURES TAKEN TO DATE TO IMPROVE SWITCHING

In 2018, the Central Bank introduced a number of amendments to the CP-Code that were designed to provide additional transparency to mortgage holders and facilitate mortgage switching.[182] These measures included requirements for lenders to notify borrowers if cheaper

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[177] https://www.centralbank.ie/docs/default-source/publications/economic-letters/economic-letter-12-mortgage-switching.pdf?sfvrsn=4
[178] https://www.centralbank.ie/docs/default-source/publications/research-technical-papers/refinancing-inertia-irish-mortgage-market.pdf?sfvrsn=80a1971d_9
[179] https://www.centralbank.ie/docs/default-source/publications/economic-letters/economic-letter-12-mortgage-switching.pdf?sfvrsn=4
[180] The Consumer Survey found that prominent reasons for not switching in the past five years included: difficult to switch provider; didn't have time to switch; difficulty in gathering the required information to switch
[181] The Consumer Survey found that 67% of switchers said they were satisfied or relatively satisfied, and 21% saying they were neither satisfied nor dissatisfied. Only 9% were dissatisfied.
[182] https://www.centralbank.ie/news-media/press-releases/mortgage-switching-20-June-2018

interest rates were available, for example, due to a move in the borrowers LTV interest rate band, as well as the imposition of a time-bound mortgage application process on lenders.

However, there is no standalone mortgage switching code. It is understood that the Central Bank did consider this issue in recent years but concluded at the time that there would be major overlap with the mortgage related measures in the CP-Code. This arises because once a decision to switch lender has been made by a customer, the mortgage underwriting and drawdown process to be followed with the new lender is identical for all borrowers, whether switching or not.

The Review Team notes that many of the measures in the CP-Code related to switching involve information obligations for lenders. However, there is little information in the CP-Code about what rights a borrower has or what a borrower considering switching can expect in the process. Accordingly, and in its current review of the CP-Code, the Review Team suggests the Central Bank consider including a specific standalone section on mortgage switching within the CP-Code.

In 2017 and 2018, the Department ran two advertising campaigns seeking to promote awareness of the benefits of switching. These campaigns were run in two phases and as part of a range of competition measures agreed with the European Commission to raise awareness and promote customer switching in retail financial products, including mortgages.

The recent research by the Central Bank[183] on borrower behavior in relation to refinancing with their existing provider, discussed above, will be used to inform further work.

Furthermore, forthcoming research from the Central Bank which, at the time of completing this Report, was expected to be published in December 2022, will demonstrate the benefit of taking account of behavioral insights at policy design stage. The Central Bank used behavioral insights in a large-scale field experiment to enhance the design of existing mandatory consumer disclosures in the mortgage market and improve consumer engagement with advantageous refinancing opportunities. This initiative was the first of its kind in the Irish mortgage market.

CONVEYANCING AND SWITCHING

The process of buying a property or switching a mortgage can be lengthy, driven in some cases by a challenging and lengthy conveyancing process. An issue that has arisen recently is that an elongated mortgage drawdown process can cause prospective borrowers or

[183]The Central Bank's research found only 33% of eligible people took up the option to avail of a cost free option lower interest rate https://www.centralbank.ie/docs/default-source/publications/research-technical-papers/refinancing-inertia-irish-mortgage-market.pdf?sfvrsn=80a1971d_9

switchers to lose out on favourable interest rates, particularly in a rising interest rate environment.

While the conveyancing system is not within the ToR of this Review, any initiatives that make the process more efficient would be welcome.

In this respect, the Review Team notes that the Legal Services Regulatory Authority is expected to submit a report on the creation of a new profession of conveyancer to the Minister for Justice in the coming months. Separately, the Law Society's initiative in relation to e-conveyancing is ongoing. It is understood that the Law Society has made a significant investment in this project and that it made a detailed submission to the Department of Justice in January 2022[184] identifying legislative amendments that would improve the process.

NEXT STEPS ON SWITCHING

The OECD Principles contain a principle on competition, which places responsibility on policy makers to ensure competition between providers delivers good consumer outcomes. To achieve these good outcomes, the OECD Principles state:

> *'Consumers should be able to search, compare and, where appropriate, switch between products and providers easily and at reasonable and disclosed costs.'*

Consistent with this objective, the Department commissioned the ESRI to undertake research with respect to switching, which is due to complete in H1 2023. Focusing on the behavioural aspects of switching, this work is being delivered in three stages:

- Stage 1 - A survey of consumers to diagnose the key problems associated with choosing and switching among the main financial service products, including mortgages.
- Stage 2 - The design and development of a series of decision aids to boost consumers' ability to switch to better value financial products.
- Stage 3 – Following lab testing, the trial of some of the decision aids identified in large-scale field studies with consumers.

The Department will work closely with the Central Bank to address any issues that emerge from the ESRI Report or consumer experiences via the trials in the coming months. The Review Team would expect that insights gained from this collaboration will inform whether or how the CP-Code should be updated.

[184]Statutory Declarations and Statements of Truth in Conveyancing: https://www.lawsociety.ie/Solicitors/Representation/Submissions

The Review Team recommends that:

Recommendation 9-1

The Department of Finance should work with the Central Bank in 2023 to identify measures and initiatives to build consumer and SME knowledge and confidence in the switching process for mortgages and other retail banking products, including taking actions that make switching easier, and that address impediments and gaps identified in the process. This work will be informed by the wider switching research being undertaken for the Department of Finance by the ESRI.

Recommendation 9-2

The Central Bank should, as part of its review of the Consumer Protection Code, consider enhancing requirements on how regulated firms provide information on alternative mortgage products to their customers to improve the take-up by mortgage holders of cheaper options which may be available to them. This should be addressed in a standalone section of the Consumer Protection Code.

9.5. Product choice

A mortgage is a relatively standard credit product, typically involving a large sum that is secured against a property, and which is repaid over an agreed period or on the occurrence of a defined event in the future (e.g. sale of the property or the death of the borrower), and on which interest is paid. As such, compared to non-banking products such as cars or technology, there are a limited number of features of mortgages that can actually be varied. Accordingly, when innovation does happen, it tends to be limited to changes in a small number of mortgage variables, such as loan term, repayment arrangements and interest rates.

The Review Team examined the range of mortgage product choice available to Irish consumers, and how this has developed in recent years. The Review Team found:

- All mortgage lenders offer borrowers a range of mortgage terms, with lenders typically requiring the mortgage to be repaid by the time the borrower reaches retirement age. Loan terms typically range from 15-35 years, but can be shorter.
- All originating lenders offer borrowers the ability to manage their interest rate risk appetite, with all lenders offering fixed rate as well as variable rate mortgages. In recent years, the non-banks differentiated themselves by offering borrowers the ability to fix their mortgage rate for very long terms, up to 30 years. Until recently, these products were competitively priced. The traditional banks also offer long-term fixed rates, but up to a maximum of 10 years.
- Typically, lenders offer lower interest rates to customers who have a lower loan-to-value (LTV), with the lowest interest rate typically available to borrowers with an LTV of sub 50%. The interest rate differential between low LTV mortgages and high LTV mortgages can be significant.

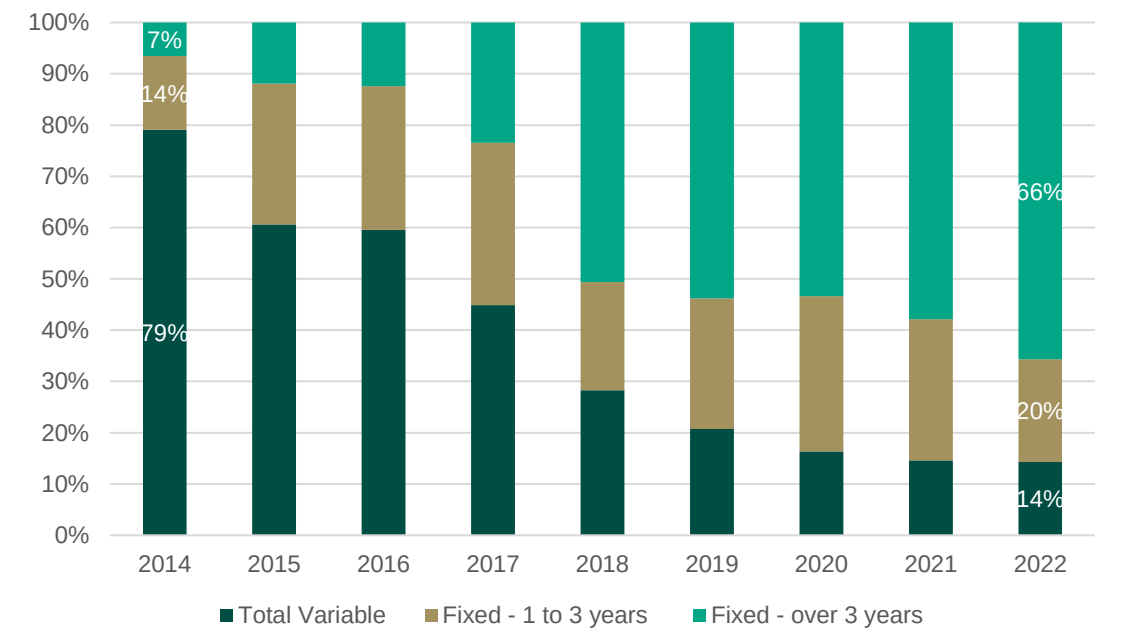
- The traditional banks, but not non-banks, offer lower interest rates to customers where their property has a good energy efficiency rating. These mortgage products are relatively new to the market, and have been called 'green mortgages'.
- At the time of mortgage origination, the traditional banks offer cash-back to their new borrowers, whether those new borrowers are buying a new home or switching their mortgage from their existing provider. Cash-back mortgages can include different types of cash incentives to new borrowers, such as getting a percentage of the mortgage value back in cash when you take out the mortgage, or a set amount of money. Some banks also offer an additional cash back after a number of years if the mortgage remains with the bank – a type of loyalty bonus.
- Where mortgage customers have their current accounts with a traditional bank, the bank may offer free banking on their current accounts, or perhaps even a discounted mortgage rate for having another banking product with them, such as a current account.[185]

It is clear that mortgage customers have responded strongly to lenders' fixed rate products as demonstrated by the shift in new business flow since 2014 (see Figure 11). This shift in choice is not surprising given the low interest rate environment of the past number of years and borrowers' desire to lock in repayment amounts for some time into the future. The traditional banks have 37% of their current mortgage portfolio fixed for three years or longer, with a further 14% fixed for between one and three years.

In more recent times, the non-banks have provided borrowers with more product choice, in particular by offering fixed rate terms of up to 30 years. However, demonstrating the impact that volatility in financial markets can have on non-bank lenders, one non-bank mortgage provider has recently temporarily withdrawn fixed rate mortgages of 10 years and longer to new customers.[186]

[185] Are special offers worth it? - CCPC Consumers
[186] https://www.irishtimes.com/business/2022/10/26/finance-ireland-temporarily-pulls-its-most-popular-longer-term-fixed-rate-loans/

Figure 11 - Variable/fixed rate choice since 2014 – PDH



Source: Central Bank

CASHBACK MORTGAGES

Cashback offers have been a feature of the Irish mortgage market since 2015 and have been a popular choice for borrowers. Cashbacks have been the subject of some debate with some commentators suggesting they can ultimately lead to a borrower paying a higher cost of credit over the lifetime of the loan, assuming it runs its full term. Indeed, some commentators have called for cashbacks to be banned entirely.

The Review Team is of the view that cashback offers provide valuable choice for some consumers. They provide a lump sum to cover additional costs that come with purchasing a house including furnishing and decorating. Cashbacks also provide funds to cover costs for borrowers who are switching mortgage provider (for example, legal fees).

In relation to transparency, the Review Team notes that section 6.12 of the CP-Code requires a lender, when offering an incentive such as cashbacks, to inform the borrower of the total cost of the mortgage both with and without the cashback.

Table 7 - Cashback offers

Lender	First time buyer	Switcher	Comment
AIB	-	€2,000	
Bank of Ireland	2%	2%	Additional 1% in 5 years
EBS*	2%	2%	Additional 1% in 5 years
Haven*	€5,000	€5,000	For mortgages over €250,000
PTSB	2%	2%	

Source: Banks' website

'GREEN' MORTGAGES

Each of the three traditional banks have introduced 'green mortgage' products which are aimed at addressing climate change and supporting the transition to a low carbon economy by providing finance for energy efficient homes. These products are broadly similar with each of the banks offering discounts of around 0.3% if the property has a BER rating of B3 or higher. 'Green mortgages' are accounted for up to 35% of the individual banks' total mortgage new business in 2021.

Mortgage lenders should do more to help consumers make their homes more energy efficient

However, feedback from the Public Consultation was that the retail banking sector is not providing appropriate support and funding to consumers to transition to carbon neutral, with respondents suggesting that placing 'green' in front of a product is not enough to promote the transition to a green economy. As outlined in the chapter on Climate, the Review Team considers that a material increase in momentum is required to support Ireland to meet its 2030 and 2050 targets. Mortgage lenders should do more to help consumers make their homes more energy efficient, particularly where it has been found that consumers are increasingly willing to make sustainable choices.

The Review Team has already outlined how mortgage lenders could be more innovative, for example, by exploring how they could bridge SEAI grants to enable consumers commence the retrofit of their homes, as well as potentially developing products that aim to align the monthly repayment, insofar as this is possible, with the energy cost saving that will accrue to the consumer.

Were lenders to undertake a review of their mortgage portfolios, there is potential for them to identify borrowers that have LTV headroom which, subject to normal and prudent underwriting standards, could provide opportunities to fund retrofitting.

A specific Recommendation to the retail banking sector as to how it can support consumers in their transition to a lower carbon future is outlined in the chapter on Climate.

CONCLUSIONS ON PRODUCT CHOICE

Product innovation in recent years in the mortgage market has been limited to three, albeit very important, areas – the introduction of longer fixed rate terms (particularly by the non-banks), cashbacks, and 'green mortgages.' In the course of its work, the Review Team identified different mortgage products available in other countries which, if offered to Irish consumers, would increase product choice and perhaps better serve the specific needs, preferences, or life circumstances of certain borrowers. In Box 2 below, the Review Team outlines two specific mortgage products that are offered in Finland, with features that may appeal to some borrowers.

Whilst it would not be appropriate for the Review Team to call on mortgage lenders to introduce specific types of products, the Review Team considers that they could review mortgage offerings in other jurisdictions and give consideration to developing products and innovations that aid consumers by providing greater product choice.

The Review Team notes that the CCPC has required BOI to make a €1 million fund available for distribution to companies involved in developing innovations in the mortgage market. The Review Team calls on eligible firms to utilise these funds, and also calls on other providers in the sector to contribute to this initiative.

Box 2 - Alternative variable mortgage rate products available in Finland

An equal principal component in each scheduled repayment amount

- This suits a borrower who can afford to make higher monthly repayments in the earlier years of the mortgage. The monthly instalment will reduce, however, as the principal gets paid down and the monthly interest charge falls. The accelerated principal pay down results in a lower total cost of credit for the borrower over the life of the loan.

Fixed repayment amount for the life of the loan

The repayment amount stays constant for the full term of the loan. This mortgage type is marketed as suitable for customers who have a preference for a fixed repayment amount and who can absorb a longer repayment period.

- If the mortgage interest rate increases, the term of the loan and total cost of credit over the life of the loan increases.
- If the mortgage rate reduces, the term of the loan and the total cost of credit over the life of the loan reduce.
- The repayment must always be at least equal to the amount of interest.

This product combines the key feature of long term fixed rate mortgages, i.e. a fixed monthly payment, with a variable rate mortgage.

One caution worth highlighting is if interest rates rise significantly, this may extend the term of the mortgage beyond a borrower's desired target date. Accordingly, in Finland, borrowers are urged to adjust repayments to manage rising interest rates.

Related to product choice, the Review Team notes that circa one third of the responses to the Public Consultation were in relation to the absence of Sharia law compliant mortgages, which prohibits the charging of interest, in the Irish market. The Review Team understands that a key issue in relation to these type of mortgage products is that the mortgage structure needed would result in stamp duty being paid twice under Irish tax law, once when the property is originally purchased, as is the case in all other house purchase transactions, and again when the mortgage term is completed because the property is then 'sold' by the lender to the borrower.

The Department is aware of the potential impact of double stamp duty in respect of mortgages, which are compliant with Sharia law. The Department has engaged with Revenue, who administer the tax code, in order to try to identify a way in which this issue could be addressed and resolved. Although this work is ongoing, no indication could be provided at the time of completing the Review as to the outcome of this engagement.

The Review Team recommends that:

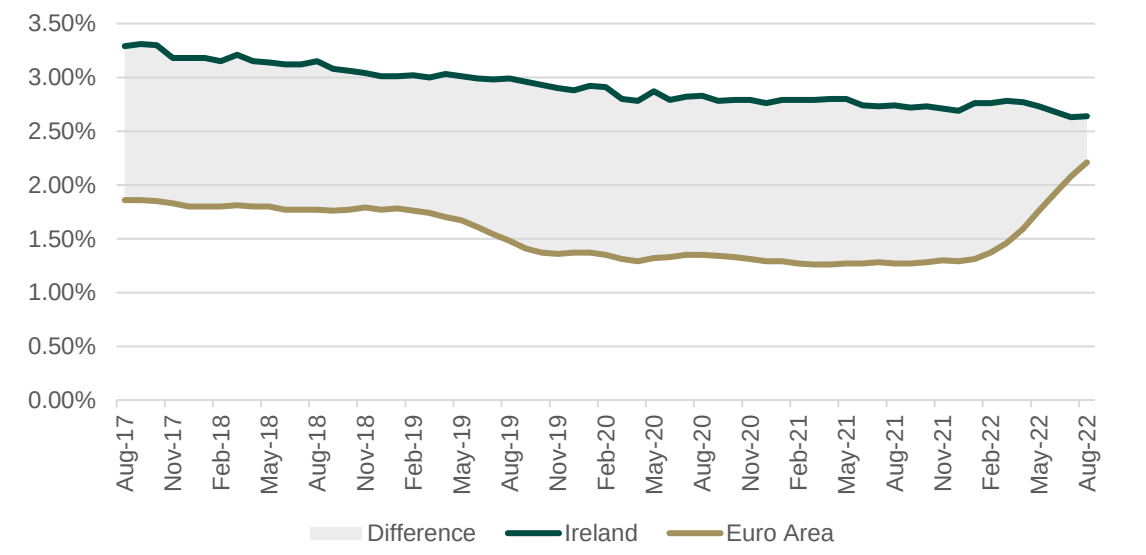
Recommendation 9-3

The retail banking sector should review their existing mortgage product suite to identify opportunities to enhance and expand it for the benefit of their customers, in particular where this could help reduce the borrower's overall cost of credit.

9.6. Mortgage interest rates

In recent years there has been much media, political and other commentary on the relative level of Irish mortgage rates compared to other countries in the euro area, with commentators often attributing interest rates in Ireland to a lack of competition or the higher levels of capital that Irish banks are required to hold. Based on data published monthly by the Central Bank, the interest rate for new mortgages in Ireland has averaged 2.92% over the past 5 years, compared to the euro area average of 1.55%, with an average differential of circa 1.37% for the period. As illustrated in Figure 12, the differential has narrowed significantly during 2022. However it may be that the gap will widen again with the Irish banks just beginning to pass through recent ECB rate increases, lagging behind Eurozone banks.

Figure 12 - Weighted average interest rate for new mortgage lending – Ireland compared to euro area average



Source: ECB

BASIS OF COMPARISON

Whilst at a high level a comparison of rates across EU countries is of interest, the interest rates quoted for each country are not comparable on a like-for-like basis. The rates quoted in

the Central Bank data are headline rates, and do not include all of the variables that can impact the overall cost of credit to the borrower over the lifetime of the mortgage. For example:

- Unlike in Ireland, banks in many euro area countries charge their customers upfront fees, such as arrangement fees, when they get a mortgage. These additional costs to customers are not reflected in the headline interest rate, but if included, would push up the average euro area rate closer to the Irish headline rate.
- Many banks in Ireland offer their mortgage customers a cashback incentive when they drawdown a mortgage. The cashback benefit is not reflected in the Irish headline interest rate but, if included, would bring down the Irish headline interest rate closer to the average euro area rate.

Analysis previously undertaken[187] suggests that if adjustments are made to facilitate a like-for-like comparison between Irish and euro area rates, the difference between Irish and euro area interest rates reduces from 1.32% to 0.92%.

EXPLAINING HIGHER MORTGAGE RATES IN IRELAND

The Review Team reviewed recent research[188] that examined the drivers of the differential for the purpose of (a) explaining how it arises and (b) forming a view on whether there is potential for the differential to narrow, bringing Ireland's average headline rate closer to the euro area average.

In addition to the 0.40% differential that is accounted for when a like-for-like comparison is carried out, the research identified three other factors that account for a further 0.78% as outlined below, leaving a residual of c. 0.14%.

- Higher capital requirements – 0.30%
- Higher operational costs – 0.40%
- Higher bad debt charge – 0.08%

Higher capital requirements. Under European requirements, in addition to considering expected losses on their loan portfolios and providing for these in their determination of profits, banks are also required to hold capital to cover unexpected losses. The more risky the portfolio is perceived to be, the more capital a bank is required to hold. For mortgage lending, banks apply a risk percentage (commonly called the risk weight) to their mortgage portfolios.[189] [190]

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[187] Download Irish Banks; Changing the Conversation II - Looking at the building blocks of a
At the time the Goodbody analysis was completed, the difference was 1.32%.
[188] Download Irish Banks; Changing the Conversation II - Looking at the building blocks of a
[189] c. 90% of Irish bank mortgages are modelled using in-house developed models.
[190] Key inputs to determining the risk weight are (i) the probability of a loan defaulting, (ii) if the loan defaults the expected loss on the loan and (iii) the time it takes to realise the security that underpins the loan. The longer it takes to realise security the higher the loss as the models take account of the time value of money.

This is determined by either using standardised risk weights or, more typically, using models developed in-house, which generally result in lower risk weights.

The amount of capital the bank should maintain for those mortgages is calculated by applying the relevant risk weight to the total value of mortgages and then applying the required percentage of capital. The internal risk based models must comply with European regulatory requirements.[191] However, the data and assumptions underpinning the calculations are determined by each bank, and are heavily influenced by the historical performance of the relevant loan portfolio.

The capital requirements for Irish banks for mortgage lending are currently twice the level of the European average.[192] This has been a contentious issue and the subject of much commentary. However, it is important to recognise that these capital levels are reflective of the significant performance issues with Irish mortgages in the aftermath of the GFC. Irish mortgages were more likely to default, and when they did the loss on each loan was generally much higher than in other jurisdictions. This higher loss experience reflects the relatively poor underwriting standards, as well as the extended length of time it typically takes to recover security for Irish mortgage debt, relative to other jurisdictions. This latter issue was raised by the IMF during the recent FSAP in the context of LTMA.

Due to global concerns regarding the capital calculations determined by banks' in-house models, new regulations are in the process of being introduced that will set a floor on the risk weights banks can apply to their mortgage lending.[193] Implementation of the floor, which is set at 72.5% of the standardised risk weight, is due to commence in 2025 and will be phased in over a 5-year time frame. As average risk weights on Irish mortgages are currently only marginally higher than the proposed floor, any material reductions in mortgage risk weights due to improved credit quality will be limited. Given the fact that the average risk weights in European banks are well below the floor, the new regulations mean that European banks will have to allocate significantly more capital to their mortgage portfolios.

Finally, it has been suggested that speeding up the repossession process would significantly reduce capital requirements. Attempts have been made by the Review Team to quantify this, but it has proved difficult. The general impression is that such an initiative would feed slowly through to the metrics used to calculate risk weights and, therefore, the impact on interest rates would be muted. In any event, the introduction of the output floor, discussed above, limits the scope.

Over the course of this Review and at the Dialogue, some stakeholders commented that impediments to recovering collateral could act as a possible barrier to entry for potential

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[191] Bank supervisors review such models and their approval is required where material amendments to a model are proposed.
[192] https://www.centralbank.ie/docs/default-source/publications/financial-stability-notes/risk-weights-on-irish-mortgages.pdf?sfvrsn=4afb931d_7
[193] Commonly referred to as Basel III.

entrants to the market. Later in this chapter there is a Recommendation supporting the implementation of the IMF recommendation that the resolution of LTMA needs to be addressed by relevant state agencies. As part of this, further analysis of collateral recovery should be undertaken.

Higher operating costs. The research considered by the Review Team estimates that the operational costs for mortgages in Ireland was 1.05% versus the European average of 0.65% – a difference of 0.40%. Many of the costs applicable to universal banks such as AIB, BOI and PTSB have a fixed component such as infrastructure, levies, regulatory and digital investment. Accordingly, they impact the Irish banks in a disproportionate manner due to their relatively small size. In addition, the specific costs associated with significant portfolios of NPLs contribute to total operating costs. While the traditional Irish banks must continue to place a strong focus on cost management, their relative scale disadvantage will persist, albeit at a reduced level due to the recent loan acquisitions.

Bad debt charge. A difference of 0.08% is attributed to the relative bad debt charge with a normalised charge of 0.20% in Ireland compared to 0.12% for the euro area average. Reasons given for this include the lower recovery rate and longer time to recovery in Ireland. Over the medium to long-term, with improved outcomes[194] and addressing the issues regarding timely recovery, this differential should reduce.

Based on this review of the drivers of higher interest rates in Ireland, the Review Team considers that while there is some scope for the differential to reduce, the most material impact is more likely to arise from the application of interest rate increases by European banks, as they pass on the costs associated with higher capital requirements.

VARIABLE MORTGAGE INTEREST RATES

In Ireland, interest rates charged by lenders for variable rate mortgages ('variable mortgage') are determined on the basis of a wide range of factors such as cost of funds, capital requirements, loan default risk, operational costs, expected return and competition. Changes in any of these may, depending on the contractual terms of the particular loan, result in changes to the interest rate.

However, as set out in Table 8 below, it is common practice for banks in other countries to use predefined indices when determining the cost of funds element of the interest on a variable mortgage and to add a fixed margin to it. Euribor (Euro Interbank Offered Rate)[195] is commonly

[194] Reflecting the impact of better underwriting standards, the positive impact of the Central Bank's mortgage measures, better bad debt management by banks and improvements in the insolvency regime.
[195] Euro Inter-Bank Offer Rate (EURIBOR) is based on the average interest rates at which a large panel of European banks borrow funds from one another. There are different maturities, ranging from one week to one year. The European Money Markets Institute, through the Calculation Agent, is the sole official source of publication of the Euribor rates. As an Authorised Administrator, The European Money Markets Institute is duly supervised by the European Securities and Markets Authority.

used in Eurozone countries. However, there are other benchmark indices, each with their own calculation method and particular characteristics.

Table 8 - Weighted average interest rate for new mortgage lending – Ireland compared to euro area average

Market	Index
Portugal	EURIBOR
Lithuania	EURIBOR & Country Economic Indicator
Finland	EURIBOR
The Netherlands	ECB rate
Canada	Bank of Canada Overnight Rate
United Kingdom	Bank of England Base Rate*
New Zealand	Official Cash Rate
Portugal	EURIBOR

Source: Department of Finance, International Comparison
* While index or tracker mortgages are offered in the UK, they tend to be as introductory rates for a fixed period at the start of the mortgage.

From a consumer perspective, the benefit of having a mortgage priced off an index is that it provides added transparency for the borrower. Increases in the index being used translate into interest rate increases and vice versa. However, as seen in the current environment of higher interest rates, variable mortgages can have the advantage that the lender may choose not to pass on increases immediately, or at all. This is particularly the case where lenders are competing for new business.

Mortgage lenders are required under the CP-Code to publish variable interest rate mortgage policy statements on their websites. A review of these policies shows they typically include a qualitative description of the inputs that are considered when determining the variable interest rate. However, there is no disclosure of how changes in the inputs quantitatively impact the variable interest rate. The broad message from these policy statements is that the lender can choose to pass on all pricing risk to the borrower.

While there would appear to be no appetite among lenders to offer index based mortgages here in Ireland, consideration should be given to how lenders can provide greater transparency on their variable rate mortgage pricing so as to give borrowers better information.

However, it must be recognised that this is a complex issue and significant work has been undertaken by the Department and the Central Bank in recent years to improve transparency. Furthermore, unintended consequences must be avoided, especially due to the past

experience during the GFC and the impact on Irish banks from mispricing index based mortgages, for example, tracker mortgages.

The Review Team recommends that:

Recommendation 9-4

The Department of Finance should consult with mortgage lenders and the Central Bank to determine if lenders can provide increased transparency in relation to the composition of variable mortgage pricing.

9.7. Regulation of mortgage lending

Regulation of mortgage lending in Ireland derives from a range of domestic and EU legislation, as well as the various codes that the Central Bank has developed, in particular in response to the lessons learned from the GFC.[196]

The CP-Code is a cornerstone of the Irish consumer protection framework with respect to mortgages, and comprises a set of general principles and specific requirements that lenders must adhere to. In their broadest terms, the General Principles of the CP-Code require financial services firms to meet minimum standards of care towards their customers, and to ensure that firms operate to protect their customers' best interests.

The CP-Code confers specific transparency obligations on lenders when offering mortgages to consumers, and places an obligation on lenders to fully assess the applicant's affordability of credit. The mortgage credit directive,[197] which was transposed into Irish law in 2016, also places responsibility on the lender to satisfy themselves that the mortgage applicant has the ability to fully repay the mortgage, having due regard to their individual circumstances. If, following this assessment, the applicant is refused the mortgage, the lender must explain the reasons for the refusal.

The Central Bank's Code of Conduct on Mortgage Arrears (CCMA), which is a statutory code, requires a lender to have fair and transparent processes in place for dealing with borrowers in or facing mortgage arrears, and places an obligation on the lender to takes specific steps that aim to get the borrower back on track with their mortgage should they experience financial difficulty.

[196] Direct domestic legislation includes the Consumer Credit Act 1995 which was last amended in June 2022.
[197] The European Union (Consumer Mortgage Credit Agreements) Regulations 2016 (CMCAR), which transposed the Mortgage Credit Directive (MCD) https://www.irishstatutebook.ie/eli/2016/si/142/made/en/print

Other Central Bank requirements include obligations on firms to clearly explain the pros and cons of any mortgage incentives, such as cashback offers, as well as obligations on lenders to increase transparency and facilitate mortgage switching.

In addition, in 2015 the Government legislated to ensure that the State's consumer protection framework, including the Central Bank's codes, apply to all mortgage borrowers irrespective of whether they have their mortgage with a bank or non-bank. Furthermore, in 2019 the Consumer Protection (Regulation of Credit Servicing Firms) Act 2018 came into effect, meaning firms who purchase loan books from the original lender must be regulated by the Central Bank.

The Central Bank's codes are subject to ongoing review to ensure they remain fit-for-purpose and forward-looking. In 2018, at the request of the Minister for Finance, the Central Bank completed a review on the effectiveness of the CCMA in the context of the sale of mortgages by banks and other regulated lenders. It was found that for borrowers who engage with the process, the CCMA is working effectively and as intended.

THE MORTGAGE MEASURES

The Central Bank, as part of its independent mandate to preserve and protect financial stability in Ireland, has statutory responsibility for the regulation of mortgage lending by banks and other commercial lending institutions operating in Ireland. In line with this mandate, the Central Bank introduced macro-prudential measures for residential mortgage lending in February 2015. The mortgage measures apply certain loan-to-value (LTV) and loan-to-income (LTI) restrictions on residential mortgage lending. The analysis undertaken by the Central Bank shows that mortgages originated under the mortgage measures have been much less risky than loans originated before the GFC. The number of defaulted accounts and the probability of the mortgage holder defaulting is significant less than prior to the GFC. Also, it was seen during the pandemic that mortgages originated under the mortgage measures were less likely than mortgages that predated the mortgages measures to require a payment break.[198] This demonstrates that the mortgage measures have helped guard against weaker lending standards by mortgage providers.

Review of the mortgage measures framework

The Central Bank carried out a comprehensive review of the structure of the mortgage measures framework that also incorporated the annual calibration exercise. Arising from the review, which was published on 19 October 2022,[199] the Central Bank preserved the structure of the measures but made some changes to its calibration including an increase in the LTI limit for first-time-buyers from 3.5 to 4 times income, and an increase in the LTV limit for non-

[198] https://www.centralbank.ie/docs/default-source/publications/financial-stability-notes/no-5-covid-19-payment-breaks-on-residential-mortgages-(gaffney-and-greaney).pdf
[199] https://www.centralbank.ie/financial-system/financial-stability/macro-prudential-policy/mortgage-measures/mortgage-measures-framework-review-public-engagement

first-time-buyers from 80% to 90%. In addition, the proportion of aggregated lending allowed above limits was recalibrated. The Review Team considers that the changes to the measures are proportionate.

As part of the Review process, the Department, which supported the measures that have proved successful in ensuring prudent lending, suggested consideration should be given to changing to a debt-service-to-income (DSTI) ratio. DSTI[200], which has also been suggested by the IMF and is the most common mortgage income measure in use in Europe, incorporates an automatic balancing mechanism in that the permitted level of borrowing goes down as interest rates increase and vice versa. The Review Team also notes that DSTI could be calibrated to support other policy priorities such as tackling climate change or to promote longer fixed term rate mortgages. The Central Bank considered this in its review bur deemed, overall, that the simplicity and public awareness of the LTI measure were valuable attributes. Furthermore, the Central Bank highlighted that the LTI measure complements, but does not replace, banks' own lending practices, and acts as a guardrail to lending standards consistent with its macro-prudential objective.

MORTGAGE ARREARS

Following the GFC, Ireland saw a significant increase in the level of mortgage arrears on the balance sheets of its banks. As illustrated by Figure 13 below, mortgage arrears peaked in September 2013, and have been declining year-on-year since. In June 2022 they were at their lowest level since March 2010. This decline is as a consequence of many borrowers resolving their financial difficulty, as well as the focus and effort of the banks, non-banks and the regulator. In addition, economic conditions in Ireland were improving strongly, which helped people emerge from their financial difficulty.

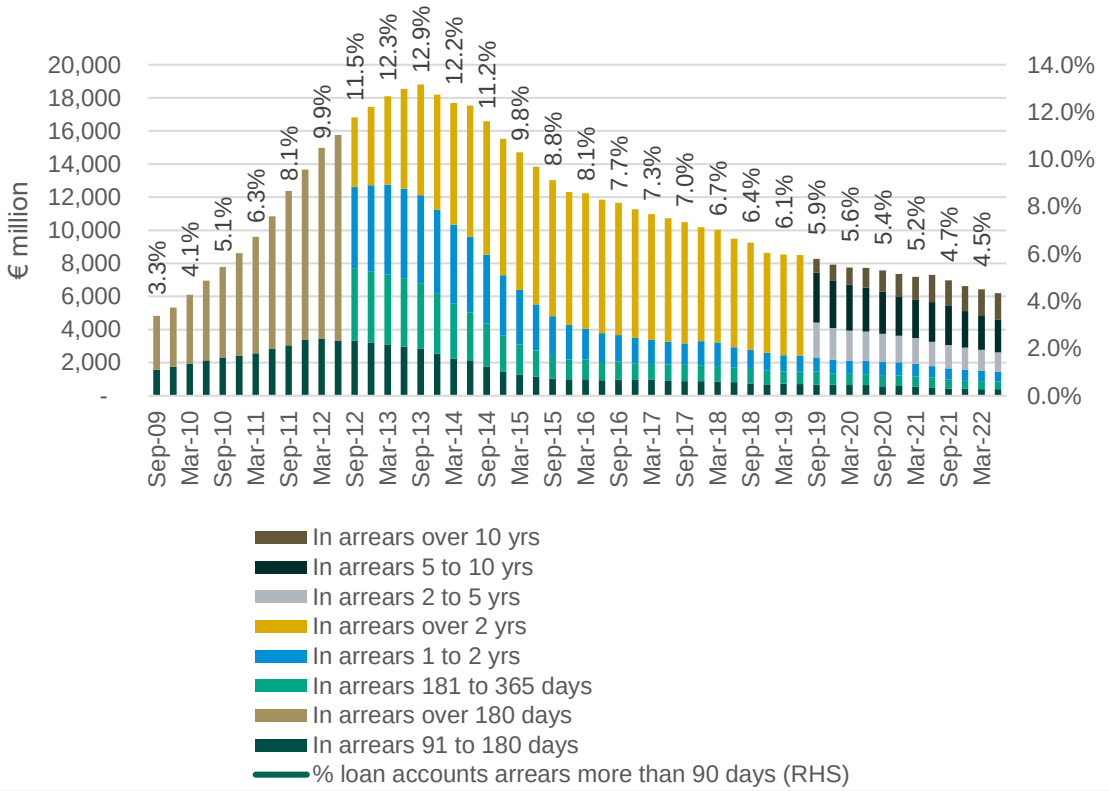
Notwithstanding this progress, given the new economic challenges Ireland is facing, including higher interest rates, complacency about mortgage arrears being only a legacy issue must be avoided. The sector and all stakeholders need to maintain their focus and efforts on helping borrowers to engage and tackle arrears as soon as they arise in order to reduce the numbers entering the LTMA category.

A key feature of Ireland's mortgage arrears landscape, which differentiates it from other euro area countries, is the level of LTMA, particularly very long term mortgage arrears. LTMA are defined as accounts in arrears for more than one year. There were still c.25,000 PDH accounts classified as LTMA as at June 2022 (54% of total accounts in arrears). Of the total mortgages

[200] The IMF also referenced the use of a debt-to-income (DTI) ratio commenting as follows "Monitor possible leakages from unsecured credit and be ready to expand borrower based measures to include DTI/DSTI limits."https://www.imf.org/en/Publications/CR/Issues/2022/09/07/Ireland-Financial-Sector-Assessment-Program-Technical-Note-on-Macroprudential-Policy-523204

in LTMA, 16% are between one and two years 28% are between two and five years in arrears, 33% are between five and 10 years and 23% greater than 10 years.[201]

Figure 13 - PDH Mortgages Accounts in Arrears 2009 - 2022



Source: Central Bank

The resolution of LTMA remains an important issue and resolving it has been a priority for Government and the Central Bank. There have been significant policy and legislative responses in areas of Central Bank codes and initiatives, and comprehensive reforms to the insolvency framework (see**:** Appendix 5**)**. This remains a key focus and based on the Central Bank's most recent mortgage arrears statistics, it is clear that year-on-year progress continues to be made.

However, in its recent FSAP of Ireland[202], the IMF noted the persistence of very long-term mortgage arrears 'despite the authorities in Ireland having pursued a multi-faceted strategy to resolve them.'

Stating that further efforts are needed, the IMF highlighted that:

[201] https://www.centralbank.ie/statistics/data-and-analysis/credit-and-banking-statistics/mortgage-arrears
[202] https://www.imf.org/en/Publications/CR/Issues/2022/07/07/Ireland-Financial-System-Stability-Assessment-520469

> *'LTMA pose a challenge to the effectiveness of the overall system for debt resolution and creditors' rights, and failure to fully resolve these arrears has the potential to undermine credit growth and affordability, given the impact on credit risk of uncertainty of realizing collateral.'*

The IMF recommended the adoption of a coordinated, multi-agency strategy for resolving mortgage arrears to be informed by data on borrowers' financial situation and debt servicing capacity. The IMF suggested that consideration should be given to publishing more granular guidelines on solutions that creditors offer to borrowers and it suggested broader social housing would also reinforce such an approach. Personal insolvency can also play a role, by ensuring that court-approved mortgage repayment plans provide sustainable solutions.

The Review Team recommends that:

Recommendation 9-5

Implementation of the IMF recommendation that the resolution of long term mortgage arrears needs to be considered and addressed in a coordinated way by various agencies, including the Department of Finance, the Central Bank, the Department of Justice, and the Insolvency Service of Ireland in consultation with other relevant agencies. The Department of Finance should, together with all the other relevant bodies, take this recommendation forward.

9.8. Mortgage supports in Ireland and some international models

There are a number of schemes in Ireland which have been developed, with Government support, with a view to facilitating increased home ownership. These schemes include:

- The Help-to-Buy scheme, which gives cash of up to €30,000 to eligible borrowers by way of a refund of income tax and Deposit Interest Retention Tax paid over the previous 4 years. The scheme is available to first time buyers for new properties, including self-builds. In order to qualify, the property value cannot be more than €500,000, and the loan to value ratio must be at least 70%.
- The First Home Scheme (FHS) where the State and participating banks pay up to 30% of the cost of the property (20% if the Help-to-Buy scheme is also availed of) for a stake in the property. Eligible properties are subject to area-based price ceilings within a range of €225,000 to €450,000. For the first 5 years, the FHS loan is interest free. From year 6 to 15, interest is charged at 1.75%, and from year 16 to 29 at 2.15%. If the (FHS) loan extends beyond this, interest is charged at 2.85%.

- The Local Authority Affordable Purchase Scheme which is similar to the FHS and is designed to help people on low to moderate incomes buy homes at a reduced price. This is achieved by the local authority making the property available with a price discount which is determined by the individual authority. Local authorities have indicated that they expect to make properties available at an average price of €250,000. To qualify for the scheme, applicants must show that, under the loan-to-income rule included in the Central Bank Mortgage Measures, they would not be able to afford more than 85.5% of the price of the property.

As part of its review, the Review Team also considered whether the mortgage models, or model features, in place in other countries could be replicated, at least in part, to deliver better outcomes for mortgage borrowers in Ireland. The Review Team considered three of the better known models in this regard.

In Denmark, there are specific mortgage banks which do not take deposits or raise funding from other banks for lending purposes. Instead, they issue and sell bonds to investors to fund loans, with repayments from borrowers used to service bond interest payments and pay down the principal. The benefits of this model to consumers are held to include transparent loan costs with market based pricing being applied. The mortgage bank, for its part, is protected from market risk associated with changes in interest rates.

In the United States, two government sponsored entities (Fannie Mae and Freddie Mac) purchase mortgages from the originating banks thereby providing the banks with funds to generate new mortgage lending. These two entities package the mortgages purchased into mortgage backed securities (MBS) which are sold to investors which guarantee payment in the case of borrower default. The security provide by these guarantees make the MBS popular with investors. The main benefit for the consumer is that the mortgage market is very liquid which, in turn, makes loans more affordable.

In The Netherlands a scheme guaranteed by the State allows borrowers to take out an affordable mortgage (at lower than market interest rates) and provides protection to borrowers in the event that they run into financial difficulty. As the state provides the guarantee, there are zero regulatory capital requirements on these mortgages, meaning the lender can offer the mortgage at more competitive interest rates. The cost of the guarantee is a once off fee of 0.6% of the mortgage drawdown amount, and the scheme is available to all borrowers up to a maximum purchase amount of €355,000. There are no income thresholds in place.

Based on the Review Team’s consideration of these three models, it was concluded they are not appropriate for the Irish market, at least for now. In arriving at this conclusion, the Review Team considered a number of matters including the structural uniqueness of the Danish and US models which would require a fundamental change to the functioning of the mortgage market, including replication of property transfer and repossession systems. Cherry-picking

elements of the models that are attractive is not feasible without dealing with the end-to-end mortgage, banking and property law systems.

In the case of the US mortgage model and the insurance scheme in place in The Netherlands, there is a transfer of risk to the State which ultimately provides a backstop. The Review Team did not consider it appropriate for the State to assume these liabilities.

While a full global analysis of mortgage models is outside the scope of the Review, there may be merit in conducting a subsequent exercise in this regard. Should such an exercise be conducted, the schemes already in place in Ireland and described in this section should be taken into consideration.

10. SME Credit

10.1.Market overview

The c.272,000 SMEs in Ireland play a key role in its economy, comprising 99.7% of the total enterprise population, 66.4% of employment, 43.6% of total turnover and 36.9% of gross value added ('GVA') in the Business Economy.[203] The contribution of many small businesses associated with primary production activities across agriculture, forestry and fishing are not included in these figures. Primary producers are also essential contributors to the economy, with 137,000 farms producing over €8bn in output in 2019. Given the critical role SMEs play in the Irish economy, it is important that they have appropriate access to retail banking products and services that meet their needs. In addition to availability of good day-to-day banking and payment facilities, SMEs also require access to credit to function effectively and to support their growth and development. Per the EU definition, SMEs fall into three broad categories:

Table 9 - Categories of SMEs

Description*	Employee Numbers	Turnover - EUR	Balance Sheet - EUR
Micro	1-9	<= 2 million	<= 2 million
Small	10-49	<= 10 million	<= 10 million
Medium	50-250	<= 50 million	<= 43 million

Source: European Commission

* A company that satisfies two of the three criteria, one of which is employees, is deemed to be an SME.

The CSO Statistical Year Book 2021 data provides a breakdown and contribution of each category:

Table 10 - Breakdown and contribution of each SME category

Enterprise category	Proportion of Enterprises by % and (number)	Proportion of Persons Engaged by % and (number)	Proportion of Gross Value Added by % and (number)
Micro	91.4 (249k)	24.4 (425k)	17.8 (€45.1bn)
Small	7.0 (19k)	21.7 (379k)	8.5 (€21.6bn)
Medium	1.3 (3.6k)	20.3 (354k)	10.5 (€26.6bn)
SME Total	**99.7 (271.6)**	**66.4 (1,158)**	**36.8 (€93.3bn)**
Large*	0.3 (0.7k)	33.6 (585k)	63.1 (€159.6bn)

Source: CSO
* Enterprises whose scale exceeds the SME criteria.

Importantly, the SME sector has been a growing source of employment. In the period 2014-2019 employment in the SME sector increased by 236,000 to 1.16m, versus an increase of 170,000 to 585,000 in the large enterprise sector. The sector is characterised as

[203] https://www.cso.ie/en/releasesandpublications/ep/p-bii/businessinireland2019/smallandmediumenterprises/

heterogeneous, active across all aspects of economic activity - 49% of persons employed by SMEs work in the services sector, followed by 24% in distribution, 12% in construction, 12% in industry and 3% in finance and insurance.

10.2.External developments impacting SMEs

The business environment is dynamic and SMEs are constantly anticipating and responding to external developments. Specific developments of particular relevance to Irish SMEs are discussed briefly below are Brexit and the COVID-19 pandemic, the acceleration of digitalisation and enterprises' climate change obligations. The global impact of the invasion of Ukraine is also a key factor with far-reaching consequences for consumer and SME sentiment and the global economic outlook. This will undoubtedly lead to more cautious decision-making by all players in the economy, including SMEs.

BREXIT AND COVID

Given the strong and well-established trading links between Ireland and the UK, the UK's decision to leave the EU has implications for Ireland that go beyond the impact on other EU Member States. At a time when Irish industry was adapting to the departure of a key trading partner from the single market, the additional challenges presented by the COVID-19 pandemic added significant complexity to the operating environment for Irish SMEs.

Research by the ESRI[204] highlights that both events have had negative consequences for SMEs. One positive finding by the ESRI in September 2020 is that there is little overlap between sectors most impacted by a hard-Brexit and those most affected by the pandemic.[205] Nonetheless, the impact of each shock has been material for the most exposed sectors.

While Government was extremely proactive, providing a wide-range of supports to impacted SMEs such as the COVID-19Restrictions Support Scheme, the Tax Debt Warehousing Scheme, Employee Wage Subsidy Scheme, the Brexit Impact Loan Scheme and COVID Credit Guarantee Scheme, it cannot fully mitigate long-term adverse consequences, and therefore affected firms also need to develop strategies to respond to the consequences of Brexit and the pandemic. Some firms will have benefitted from support via additional debt and deferred liabilities which must be repaid and consequently they have will implications for SMEs in the medium term.

[204] https://www.esri.ie/publications/examination-of-the-sectoral-overlap-of-covid-19-and-brexit-shocks
[205] Paper does not distinguish between SME and large enterprises.

DIGITALISATION

COVID-19 accelerated the transition to digitalisation across large sections of the economy, including the SME sector. Implementing digitalisation strategies allowed firms to continue to trade. The EIB Investment Survey 2021[206] identified that 48% of SMEs expected that COVID-19 would lead to an increased use of digital technologies in the long term. Irish respondents reported that c. 50% of firms became more digital arising from COVID-19 (vs. 50%-60% in the 8 highest European respondents, and the US). While the report does not specifically seek information from companies on investment in digitalisation, the survey did ask firms what proportion of investment was made on 'software, data, IT and website (which is a reasonably good proxy), with the intention of maintaining or increasing your company's future earnings.' Investment by Irish firms in these areas was c. 20% of the total spend. On investment more generally, c. 80% of Irish respondents believed they had invested 'about the right amount' over the previous three years, with the balance considering they had invested 'too little.' A total of 17% of Irish firms reported they had no investment planned for the forthcoming three years, compared to a survey average of less than 10%.

Digitalisation, executed well, can be transformative. Many SMEs have already successfully transitioned to a digital first strategy during the pandemic. Being aware of technological developments, proactively assessing how best to leverage changes in technology and planning how best to implement technology driven change is required to ensure SMEs are considering how best to position themselves for the future. Having the necessary business, digital and financial skills, as well as appropriate access to finance are key enablers to successfully navigate this evolution.

CLIMATE CHANGE AND ENERGY EFFICIENCY

In its discussion of climate change targets the Programme for Government states:

> *'Irish enterprise will be required to implement a detailed agenda of transition and change if it is to ensure that our sectors are climate resilient and can remain competitive in a decarbonised world.'*

To support SMEs develop their climate action plans the Government's *Climate Toolkit 4 Business*, is available to all enterprises and it will generate a tailored company specific climate action plan.

[206] https://www.eib.org/en/publications/econ-eibis-2021-eu

Notwithstanding the fact that the Climate Action Plan requires all sectors of society act decisively to address climate risk, Irish firms generally underperform their EU peers in relation to climate change action. The Climate Action Plan clearly notes the need for action stating:

> *'Companies and sectors that fail to decarbonise their activity across their entire business model will become increasingly uncompetitive, with potential far-reaching negative impacts for the economy – including undermining our long-term sustainable competitiveness and locking us into a redundant fossil-fuel based economic model.'*

The 2021 EIB Investment Survey[207] notes that Irish respondents identified the impact of climate change on their businesses as a risk, an opportunity or having no impact in equal proportions. On average 43% of EU firms have already invested in tackling the impacts of weather events and reducing their carbon emissions, while Irish firms reported that c. 15% had already invested, with c. 40% planning to invest. This response puts Ireland well behind EU peers.

Despite the state-sponsored grant aid available to industry to fund climate related investment, a range of credit offerings from commercial lenders and the recently launched €150 million SBCI Energy Efficiency Loan scheme, based on the survey findings Ireland remains well behind European peers. Given these findings, SMEs, Government and the retail banking sector must all act now and play their part in ensuring the required investment is undertaken. SMEs must assess how they can best meet their individual climate actions via government supports, commercial lending options and deploying their own resources as appropriate so that they take action in a timely manner.

SMEs must assess how they can best meet their individual climate actions via government supports, commercial lending options and deploying their own resources, as appropriate

The retail banking sector is called upon to prioritise how it can best support Ireland's SMEs to meet the 2030 climate targets. In this regard the sector should engage more proactively, and develop further its climate focused financial offering, so as to provide competitive and effective financial products and services to SMEs to assist in the transition to a lower carbon future (see also Chapter on Climate).

[207] https://www.eib.org/en/publications/econ-eibis-2021-eu

FINANCIAL SKILLS, DIGITAL LITERACY AND OTHER CORE SKILLS FOR BUSINESS SUCCESS

To succeed, a business needs access to a wide range of financial and non-financial skills. Financial literacy is consistently identified as a core competency in business, and its importance is articulated in Principle 7 of the OECD's High Level Principles on SME Financing (OECD SME Principles).[208] Participants at the Dialogue noted that financial literacy is an issue for SMEs, with micro and other SMEs having different needs. Participants noted, and the Review Team concurs, that the traditional banks could provide better support to SMEs in this important area as a means of making themselves more attractive to the sector, while also assisting with developing financial understanding within the SME sector and therefore resulting in firms submitting better proposals to support credit requests.

In terms of areas of focus, in June 2022, MentorsWork, a joint initiative between Skillnet Ireland and the Small Firms Association, reported the findings from a self-assessment survey of 615 business owners/managers across key areas linked to finance, strategic planning and motivation for growth.[209] Scores revealed that improvements are needed in the key areas of financial literacy, financial analysis and understanding risk, as well as understanding access to finance and financial support. This survey found that in general the larger the firm, and the longer it is established, the more likely it is to have higher scores in these three areas. The MentorsWork initiative is a welcome addition to the range of supports available to SMEs to build their skills in these important areas.

The Department of Enterprise, Trade & Employment (DETE) recognises the need to support the sector with enhanced financial advisory services, to help raise the level of financial acumen for all SME owners and managers, while also providing information on managing financial risks and providing visibility on financing options tailored to the specific needs of the enterprise at various stages of development. In this regard, DETE has developed a proposal to establish a 'one stop shop' Business Financial Advisory Hub that would provide broad-ranging practical knowledge and information on areas including accounting, budgeting, tax, forecasting, as well as reading and understanding financial statements and using such statements to inform decision-making. The Hub would operate alongside existing offerings such as Skillnet. Further steps to progress this proposal are planned for early 2023. The Review Team welcomes this proposal.

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[208] Principle 7 states ' To enable SMEs to develop a long-term strategic approach to finance and improve business prospects, public policies should champion SMEs' enhanced financial literacy; their awareness and understanding of the broad range of available financial instruments; and changes in legislation and programmes for SMEs. SME managers should be encouraged to devote due attention to finance issues, acquire skills (including digital skills) for accounting and financial and risk planning, improve communication with investors and respond to disclosure requirements. Efforts should also aim to improve the quality of start-ups' business plans and SME investment projects, especially for the riskier segment of the market. Programmes should be tailored to the needs and financial literacy levels of different constituencies and target groups, including groups that are underserved by financial markets, such as women, young entrepreneurs, minorities, and entrepreneurs in the informal sector, and to different stages in the SME business cycle.'

[209] Finance and Growth Skills of Small and Medium Enterprises in Ireland: https://www.ibec.ie/sfa/campaigns/mentorswork .

10.3.SME credit in Ireland

Traditionally access to credit has been a challenge for SMEs, with the exception of the years leading up to the GFC, when credit was relatively easy to obtain. However, as noted below, much of the lending undertaken by SMEs in this period was non-core, mainly relating to real estate investment, and resulted in a significant number of SMEs being over-leveraged once the impact of the crisis emerged.

STOCK OF SME CREDIT

As of 31 December 2021, SME credit outstanding on the balance sheets of the Irish traditional banks was €18.3bn, of which €12.7bn related to core borrowings and €5.6bn was property related,[210] as illustrated in Figure 14 below. A further c. €4bn was due to non-bank lenders.[211] The value of outstanding SME credit in traditional banks has reduced consistently year-on-year since the GFC. Much of the reduction is attributable to deleveraging related to pre-crisis over-investment, primarily in non-core real estate activities, and portfolio sales by banks to non-bank lenders.

Figure 14 - Stock of SME debt 2011-2021

Source: Central Bank

[210] https://www.centralbank.ie/statistics/data-and-analysis/credit-and-banking-statistics/sme-large-enterprise-credit-and-deposits/previous-statistical-releases
[211] https://www.centralbank.ie/publication/financial-stability-review/financial-stability-review-2022-i

Since the launch of the Central Credit Register[212] data on credit provided by non-bank lenders is also available to the Central Bank. Between January 2019 and December 2021, Irish SMEs borrowed over €6bn from 60+ non-bank lenders – these firms provided lending of c. €2.2bn in 2021, €1.9bn during 2020 and €2.1bn in 2019. The share of non-bank lending expanded from an average of 28% per quarter in the 2019-2020 period to an average of 36% per quarter in 2021. 43% of non-bank lending related to firms in the real estate sector. Data from the Central Bank[213] show that 24 of the 58 non-bank lenders to SMEs in 2021 had over €50 million in loans. This compares to 12 out of 55 lenders with over €50 million in loans in 2019. It is possible that further debt is being provided to the SME sector by unregulated lenders who have determined that the reporting requirements under the Credit Reporting Act 2013 do not apply to them.

ACCESS TO AND AVAILABILITY OF CREDIT

In response to the Public Consultation question regarding the adequacy of access to and availability of credit from the retail banking sector, a sizeable majority of the over 50 who responded to the question said 'No'. While some of those respondents acknowledged positive aspects of the market, they also raised concerns across a broad range of issues including, limited access to overdraft facilities, lenders credit policies being overly conservative, lack of funding for (i) certain activities (e.g. agriculture, innovation, multi-unit dwellings) and (ii) longer tenors (e.g. 7-10 years, notwithstanding the strong demand for the SBCI Future Growth Loan Scheme), too much focus on collateral, lenders' overly focused on / preferring State-sponsored lending schemes and lack of access to appropriately skilled and experienced lending staff who understand the SME's business. Respondents noted that lenders have less direct knowledge of their customers and their business operations, which in turn become potential impediments to credit decision making, particularly given the heterogeneity across the SME business universe.

Respondents acknowledged positive aspects of the market, they also raised concerns across a broad range of issues

The transition away from relationship manager led banking, at least for SMEs seeking smaller loans has left certain SMEs without the traditional input and support they require, and given the time constraints they operate under, while competition and choice are welcome, many SMEs would prefer a 'one stop shop' for their retail banking requirements. Sharia compliant business lending was also raised by a number of respondents. Key factors inhibiting acceptance of digitally enabled provision of credit include:

- Gaps in SMEs financial and digital literacy

[212] Fully operational from September 2018.
[213] https://www.centralbank.ie/docs/default-source/publications/financial-stability-review/financial-stability/financial-stability-review-2022-i.pdf?sfvrsn=3e74961d_5

- Cumbersome digital delivery models, including complicated online application forms and the associated processes
- Insufficient opportunities for borrowing SMEs to access a lender in the bank (remotely or in-person)
- Insufficient flexibility in traditional banks' processes to respond to the bespoke nature of many SMEs business models and associated credit requirements.

The issues raised by the respondents are broad-ranging, extending across all aspects of credit provision. While it is critically important that lenders have appropriate credit risk appetites and supporting policies and processes, it is equally important that lenders must be accessible, with efficient and effective delivery models for SME customers. Assessing credit requests from SMEs can be challenging for lenders, as it is difficult to develop models to accommodate the heterogeneity across a sector, where the scale and the nature of business activities are very broad. The greater use of call centres, algorithmic decision making and digital delivery, appear to have not matured sufficiently to completely replace branch based in-person services. As a result gaps in service are evident from the responses to the Public Consultation and other feedback received during the Review.

The greater use of call centres, algorithmic decision making and digital delivery, appear to have not matured sufficiently to completely replace branch based in-person services

Given these and other issues raised within the report, the retail banking sector should review their strategies and delivery models for SME credit. This work must consider the trade-offs between how banks' models can efficiently deliver sustainable credit and other banking services to this heterogeneous sector of the economy at competitive pricing. Given the fact that the traditional banks remain the main source of external finance for most SMEs, it is critically important that banks engage effectively, so that sustainable financing and the wider banking needs of the SME sector are met. Building, developing and maintaining a strong cohort of SME lending staff is critical as all lenders and their customers face into a more challenging economic environment. Material improvements are required as SME credit delivery models evolve. Meanwhile, lenders must consider what immediate changes can be made to provide much needed improved service and support to SME borrowers.

The Review Team recommends that:

Recommendation 10-1

The retail banking sector reviews its strategies and delivery models for SME credit, making amendments where required to ensure good customer service standards and to facilitate effective engagement by SMEs with skilled staff, either remotely or in-person, as appropriate.

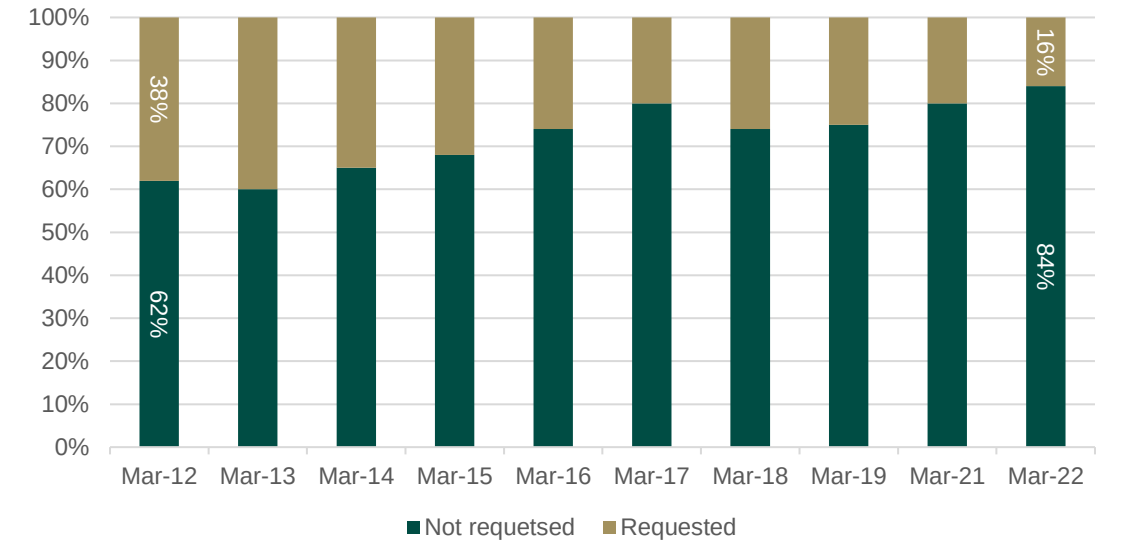
COMPETITION IN SME CREDIT

There is no objective evidence of a lack of competition in SME lending generally, and while overdraft facilities are the preserve of the traditional banks, term debt and other funding options are available from a broad range of providers. Given the withdrawal of Ulster Bank, the successful execution by PTSB of its SME strategy, discussed in more detail later in this chapter, along with continued strong offerings and focus from AIB and BOI will be important in the context of availability and choice, particularly in the provision of overdraft facilities for SMEs. The Department will closely monitor developments in the provision of overdraft facilities.

CREDIT DEMAND AND APPROVAL LEVELS

Regarding credit demand, since its inception in 2012, the Credit Demand Survey (CDS) has reported a year on year decline in demand for credit from SMEs, with demand falling from 40% in 2013 to 16% in 2022[214], as outlined in Figure 15 below:

Figure 15 - SMEs requesting credit



Source: Department of Finance Credit Demand Survey

The issue of declining credit demand has been considered by the Department over many years and it is of the view that this is attributable to three main factors:

[214] It should be noted that some of the demand in the earlier years of the survey related to requests for debt restructures: https://www.gov.ie/en/publication/51315-sme-credit-demand-survey-october-2021-to-march-2022/

- Many SME owners have had direct or indirect experience of GFC-related over-indebtedness, and they have reduced their risk appetite for debt significantly as a result,
- Many SME owners are satisfied with the current scale of their business and see no need to borrow; and
- Many SME owners prefer to utilise internal resources to fund investment / expansion and they scale their businesses on the basis of those resources and are not prepared to borrow to expand.

During the Dialogue, a number of contributors highlighted that fear of borrowing is a factor for SMEs, and of particular note is the fact that approximately half of Irish SMEs report having no bank debt outstanding.[215]

Notwithstanding the number of providers and low levels of demand for credit, in terms of access to finance, based on analysis of responses in the CDS, the ESRI's July 2022 report stated that 'close to one-third of firms agreed or strongly agreed that access to finance was a barrier to investment, while 47% disagreed.' More indepth insights from the firms who identified issues with access to finance would be extremely beneficial in terms of informing the development of policy responses to address the underlying causes, where appropriate.

Central Bank Research[216] that considered SME credit conditions in the pandemic recovery examined credit demand and noted that in addition to a pre-existing tendency to having low levels of demand, the strong pandemic-related liquidity support provided by Government through tax deferrals and grants, as well as extensive levels of forbearance on other liabilities, may have displaced demand for conventional credit and be a contributing factor for the particularly low level reported in the year to March 2022. This demand could re-emerge as supports taper off and deferred liabilities begin to fall due.

Based on the International Comparison, lending per SME in Ireland at €80,900[217] exceeds that for New Zealand (€72,300), Portugal (€67,400), Canada (€64,200), the UK (€43,200) and Lithuania (€39,500), while Finland and the Netherlands have higher levels at €99,400 and €97,500 per SME respectively in 2020. The International Comparison found relatively stable volume increases in outstanding SME lending year on year for most markets in the study. However, Portugal and the Netherlands saw 16.2% and 10.4% decreases respectively across the decade. Of note also is the fact that New Zealand recorded an 88.6% increase in SME lending between 2014 and 2020, while Finland's SME lending increased by 140% between 2014 and 2019 – but has since dropped by 26.5% in 2020. In the absence of qualitative insights into the specific dynamics that underpin these markets, and acknowledging that the metrics are relatively crude, it is not possible to draw any specific conclusions from these

[215] https://www.centralbank.ie/publication/financial-stability-review/financial-stability-review-2020-i
[216] https://www.centralbank.ie/docs/default-source/publications/financial-stability-notes/no.2-sme-credit-conditions.pdf?sfvrsn=16
[217] Department of Finance estimates based on data from December 2021.

findings. However the absolute levels of debt per SME per country suggest that Ireland is not materially out of line with the countries in the sample.

While it is critically important that viable SMEs have access to sustainable levels of credit to support their business needs, it is equally important that SME owners' determine their appetite for debt finance, which should align with their business strategies and related appetite for financial and non-financial risk. The Review Team cautions against any initiatives that focus purely on increasing credit demand.

Regarding credit approval rates, the CDS also reports that approval levels have tracked upwards since the survey commenced, rising from 76% in 2013 to 89% in 2016 and then remaining between 86% and 89% in the intervening period.

Based on the information available, the Review Team concludes that while there are mixed views on access to finance, there is not sufficient evidence to demonstrate there are material issues in the provision of credit to SMEs, or that there is unmet demand for sustainable lending. However, a more significant finding relates to issues in the delivery of credit, particularly regarding how the traditional banks engage with and support applicants during the credit application process. As outlined earlier, immediate actions by the traditional banks and the inclusion of material improvements as they continue to evolve their digital delivery models are necessary to ensure SME lending by the banks is fit for purpose.

10.4.SME credit and the State

In recognition of the important role SMEs play in economic performance and employment the SME sector benefits from significant State support. In this regard, a key focus is ensuring that viable SMEs who wish to access credit from traditional bank and non-bank sources can do so. In the aftermath of the GFC, three agencies focused on SME lending were established – the Credit Review Office (CRO) in 2010, Microfinance Ireland (MFI) in 2012 and the Strategic Banking Corporation of Ireland (SBCI) in 2014.

THE CREDIT REVIEW OFFICE

The Credit Review Office (CRO) was established in 2010 by the Minister for Finance to ensure the flow of credit to viable Irish businesses. The CRO provides a simple and effective credit review and appeals process for business owners who have been refused credit from participating banks, or where facilities have been reduced or withdrawn. Participating banks are AIB, BOI, PTSB and Ulster Bank. At the request of a borrower from one of the participating banks, a declined case will be reviewed by the CRO, who will engage directly with the relevant bank on the borrower's behalf.

Over 80% of the business owners supported by the CRO have had unfavourable credit decisions by their bank overturned.[218] In July 2021 Government approved placing the CRO on a firmer legislative footing and extending its scope, and drafting of the legislation is well advanced. While the numbers of cases appealed to the CRO are small, the support the CRO provides to applicants is significant, with dedicated reviewers engaging directly with applicants to ensure the credit proposal meets the lenders' requirements and thereby enhancing the prospects of a positive response. Success is evidenced by the subsequent high approval rates for loan applications that are supported by the CRO. Expanding the CROs remit is a welcome development for SME borrowers.

MICROFINANCE IRELAND

Microfinance Ireland (MFI), established by the Minister for Jobs, Enterprise and Innovation, provides loans of up to €25,000 to newly established and growing viable microenterprises (turnover less than €2m and staff of less than 10, with at least one full-time position) that may have experienced difficulties obtaining credit from commercial providers. MFI works closely with the 31 Local Enterprise Offices (LEOs) located across Ireland, and, to a lesser extent, with the Irish Local Development Network. The traditional banks also make referrals to MFI when they cannot lend, thereby providing micro-enterprises with a further opportunity to obtain credit. Thanks to legislative changes in 2020[219], SBCI has become the provider of liquidity to MFI, committing €30m which significantly increased MFI's lending capacity. MFI's 1% interest rate discount where an applicant applies via a LEO, ensures that borrowers benefit from expert input as part of the application process. It also gives LEOs the opportunity to direct micro-enterprises to other available business supports.

From 2012 to 30 June 2022, MFI has provided €73.3m in lending to 4,402 micro-businesses, supporting up to 10,000 jobs.

THE STRATEGIC BANKING CORPORATION OF IRELAND

The Strategic Banking Corporation of Ireland's (SBCI) statutory function is to provide, and promote the provision of credit to businesses, in particular to SMEs. Its function also includes promoting competition and encouraging an increase in the number credit providers. The SBCI achieves these aims through the provision of low cost liquidity and risk-sharing or guarantee schemes; thus supporting the provision of appropriately priced, flexible funding to SMEs. The SBCI works through bank and non-bank on-lenders, including a number of credit unions. This serves to expand on-lenders beyond the traditional banks, thereby giving SMEs access to credit from increasingly diverse sources.

[218] https://www.creditreview.ie/review-process/
[219] https://www.irishstatutebook.ie/eli/2020/act/3/enacted/en/html

Recent and ongoing SBCI guarantee schemes, which are usually delivered on behalf of relevant departments, especially Department of Enterprise, Trade and Employment (DETE) and the Department for Agriculture, Food and the Marine (DAFM), have addressed Brexit, COVID-19 impacts and the lack of availability of longer term (7 to 10 years) lending through the popular Future Growth Loan Scheme.[220] The SBCI also launched, on its own initiative and with the support of the Minister for Finance, its €150m Energy Efficiency Loan Scheme to enable SMEs and farmers to cut their energy bills and reduce their carbon emissions in July 2022. Additional schemes to address impacts from the Ukrainian war and residential retrofit, in cooperation with Department of the Environment, Climate and Communications (DECC), are in development and should be launched later this year and next.

As the economy faces into significant headwinds, State oversight and input into the provision of credit to SMEs must remain agile

SBCI's provision of attractively priced liquidity to lending partners gives them certainty regarding ongoing access to credit lines for on-lending. This is particularly important for non-bank lenders who are facing headwinds in securing funding from the wholesale markets due to the current geopolitical and economic environment.

Since it commenced operations in March 2015 to the end June 2022, through its risk sharing and liquidity partners, the SBCI has provided over €3bn in low cost, flexible funding to more than 50,000 SMEs.

CREDIT DEMAND SURVEY

To ensure policy decisions are appropriately informed, the Department conducts a twice yearly Credit Demand Survey (CDS), which provides a comprehensive range of quantitative and qualitative outputs. Since its inception in 2012 results from the survey have been pivotal in determining the nature of State actions in the ongoing provision of credit, as well as acting as a barometer for the levels of demand for credit amongst SMEs. As the economy faces into significant headwinds, State oversight and input into the provision of credit to SMEs must remain agile, to ensure timely responses to the ever-changing environment. The ongoing evaluation of information from the CDS, and other sources, is pivotal to ensure funding and guarantee schemes are tailored appropriately, whilst also ensuring that the State is not displacing commercial lenders' risk taking activities. Furthermore, data from the CDS is used for research by the ESRI, often on a joint basis with the Department. The Department is also informed by the monitoring of SME credit market developments and the publication of regular data and relevant qualitative information by the Central Bank.

[220] Up to €500.000 on an unsecured basis

MODEL FOR STATE INTERVENTION

The new agencies established following the GFC, along with a consistent flow of data from the CDS, the Central Bank and the traditional banks, provide the State with an effective infrastructure to assess the provision of credit for SMEs, intervening where appropriate. As evidenced by the take-up of credit from the SBCI and MFI, and lenders' positive responses to CRO recommendations, these interventions have provided significant additional support to the SME sector.

The International Comparison conducted as part of this Review found that Ireland's model of State involvement is generally closely aligned with the approach taken in those jurisdictions reviewed as part of the study, in terms of the rationale for state involvement and the distribution model, whereby credit is provided to SMEs mainly via a partnership model with the commercial sector.

While no substantive changes are proposed to the current model, active oversight and engagement by the Department, together with relevant agencies, remains a key priority, to ensure that appropriate actions can be taken in a timely manner in response to issues being identified. In this regard:

- A continuation of the CDS is recommended, to be conducted annually, as it is a valuable means of obtaining regular data and qualitative feedback from SMEs on this important topic, which in turn can inform actions taken by policy makers, regulators and lenders. A deep dive into some SME's reluctance to borrow could provide new insights to inform all stakeholders.
- The ongoing assessment of the supply of SME credit should remain a key area of focus for the Department. In this regard, the Review Team requests the Central Bank to continue to monitor market developments and to publish regular data and relevant qualitative information that will support this assessment.
- In the past 10 years the increased role of the State in supporting SMEs access to credit has been significant. In this regard, the Department should continue to work with other Government departments and the SBCI to identify SME credit market gaps or failures, and to develop risk sharing schemes in conjunction with the European Investment Fund to address them.

The Review Team recommends that:

Recommendation 10-2

The Department of Finance should continue to commission the Credit Demand Survey on an annual basis.

Recommendation 10-3

The Department of Finance should continue to work with other Government departments and the SBCI to identify SME credit market failures or gaps and to develop risk sharing schemes to address them. Where possible, this should be done in conjunction with the European Investment Fund.

10.5.Commercial and other providers of credit to SMEs

While the State plays a strategic role in the provision of credit to the SME sector, the traditional banks and non-bank lenders continue to be the main providers. Since the GFC the market dynamics have changed and for certain types of credit, firms have greater choice as in addition to seeking funding from banks, they can also source credit from a mix of regulated and unregulated non-bank lenders.

TRADITIONAL BANKS

Within the traditional banks, AIB and BOI have a dominant market position, while historically Ulster Bank was also a strong competitor in SME credit. A key concern with the departure of Ulster Bank, and to a lesser extent KBC, is that current accounts with overdraft facilities will only be available from the remaining three banks. While PTSB is a relative newcomer to SME credit, however the bank has ambitious plans to grow its market share. In this regard, in January 2022 it announced a €1bn loan fund to be deployed over the next three years, while it is also acquiring Ulster Bank's micro business lending and Lombard & Ulster's asset finance business[221]. Through a combination of organically developing its SME lending resources, and the acquisition of assets and experienced staff from Ulster Bank, PTSB's ambitions in SME lending, if realised, should mitigate somewhat the departure of KBC and Ulster Bank. Nonetheless, given the small number of overdraft providers the importance of the traditional banks role cannot be under-estimated and requires close monitoring by the Department.

A key concern with the departure of Ulster Bank, and to a lesser extent KBC, is that current accounts with overdraft facilities will only be available from the remaining traditional banks.

As noted earlier in this Report, feedback received at the Dialogue and submissions received in response to the Public Consultation identified particular challenges for SME borrowers with the transition by the traditional banks away from in-person banking services. The responses to the Public Consultation are generally disappointing, as they point to gaps in the retail

[221] December 2021 announcement reported that the micro-business portfolio was c. €230m and the asset finance portfolio was c. €400m. The transaction also includes c. €7bn in non-tracker performing mortgages, 25 branches and c. 450 staff: https://www.permanenttsb.ie/about-us/notices/2021/december/permanent-tsb-signs-legal-agreement-to-acquire-7.6bn-of-assets-from-ulster-bank/

banking sector's capacity to understand and engage with the firms that make up the SME sector, and, if this is the case, it is difficult for banks to appropriately meet SMEs funding needs. The responses also point to gaps in the delivery model as banks transition to digital delivery. On the other hand, all the traditional banks say that they are devoting considerable resources, especially staff, to serving the SME market. This includes significant numbers of trained advisers who will meet clients at a location that suits the client. However, the responses outlined above suggest that this is not the picture that SMEs see.

The issues identified as part of the Review process give rise to some concerns, given the dominant position of the traditional banks in the provision of credit and wider banking services to Irish SMEs. While recognising that a return to the traditional model of relationship-led in-person engagement will not occur, it is imperative that appropriate engagement models are in place to deliver credit effectively.

DIGITAL BANKS

Currently digital banks operating in Ireland offer payment services to SMEs, but they do not have a credit offering for their business customers.

CREDIT UNIONS

Credit unions also play a small role in the provision of credit to SMEs, with a loan book of €144m at June 2022. In this regard, in addition to certain credit unions having built up small SME loan portfolios, a number of credit unions also participated in more recent SBCI schemes and their own Cultivate Loan Scheme[222] targeted at the agricultural sector. Given the community-based nature of credit unions, with appropriate investment and collaboration within the sector to enable business model transition, the sector should be well-placed to scale up its activities to develop into a more significant provider of credit to the SME sector.

The Review Team notes that the forthcoming Credit Union (Amendment) Bill 2022 introduces reforms which will allow credit unions to further collaborate and enable them to compete more effectively.

As outlined in the chapter on Competition, the Department and the Central Bank will engage constructively through the stakeholder roundtable and with CUAC to give further consideration to the sector's legislative and regulatory framework as the wider financial services policy framework develops.

LOCAL PUBLIC BANKING

As discussed in the chapter on Competition, several submissions in response to the Public Consultation proposed that Ireland needs to introduce local public banking to address

[222] https://cultivate-cu.ie/

perceived gaps in the market, mainly resulting from the traditional banks rationalising their networks and reducing / outsourcing their cash services. In the context of SME credit, aside from low numbers of providers of overdraft facilities (i.e. AIB, BOI and PTSB), and notwithstanding the issues SMEs have identified regarding delivery, it is difficult to determine that the establishment of a local public bank is justified at this juncture. Also, noting the credit union sector's ambition to grow its participation in SME credit, it seems appropriate to give the sector the opportunity to build expertise and scale in SME lending over the coming years. Given the current number of providers in the market, which includes 60+ non-banks, and the diversity and choice they offer, as well as the credit union sector's aspirations to develop scale in SME credit, it is not evident to the Review Team that a need currently exists to commence the process to establish a local public banking model.

NON-BANK LENDERS

Although non-bank lenders are not a new feature of the Irish market, their presence has grown and they now form an important element of the SME financing ecosystem, providing innovations in products and funding models.[223] Recognising their role in SME financing, certain Government and SBCI schemes include a number of participating non-bank lenders. The Central Bank paper referenced earlier notes that non-bank lenders can play an important role in improving access to finance to a wider range of SME borrowers, as they can have different risk appetites. However, this can result in excessive leverage in some SMEs, or lending to firms with poorer performance, creating the possibility of unexpected losses and greater sensitivity to changing economic conditions. As their market share increases, the linkages to the wider economy and non-bank lenders funding models' resilience through the economic cycle are important factors in the context of financial stability. This issue was also raised by one respondent to the Public Consultation, who recommended that such lenders be subject to prudential supervision.

The Central Bank work noted that non-bank lenders tend to specialise in certain sectors or product lines. Lending to real estate SMEs is a particular area of focus, in addition to leasing, asset finance and invoice discounting. Just under 90% of non-bank lenders have non-Irish owners, with US based asset managers being the largest group, followed by UK financial firms. Whereas European owners tend to be non-financial firms linked to ownership of leasing and asset finance specialists, who are often the

Non-bank lenders can play an important role in improving access to finance to a wider range of SME borrowers, as they can have different risk appetites

[223] https://www.centralbank.ie/statistics/statistical-publications/behind-the-data/the-role-of-non-bank-lenders-in-financing-irish-smes

manufacturer of the assets being financed, for example Volkswagen and BMW.

While non-bank lenders generally bring strong product / sector-specific knowledge to the segments of the market they serve, the strategic rationale for their presence, and/or the funding models they deploy, could impact on their level of participation in the Irish market at different points of the economic cycle. Some early evidence has already emerged in non-bank mortgage lending, with upward adjustments to pricing, withdrawal of longer tenor fixed rate products and a reduction in lending capacity being noted in the market. The extent to which non-bank lenders participate in the market at current levels through different economic cycles remains to be seen.

REGULATION OF SME NON-BANK LENDERS

A difference in regulatory treatment exists as SMEs who borrow from unregulated non-banks cannot avail of the conduct protections available under the Central Bank's SME Regulations, although unregulated non-banks availing of SBCI assistance are required to apply them. This issue was raised in the Public Consultation and an overwhelming number of respondents supported a proposal to bring all non-bank SME lenders within the regulatory perimeter. This aligns with the EU Commission's 2022 Post-Programme Surveillance Report that called for a level playing field, given the increasing level of overlap of the activities of non-bank lenders and traditional banks.[224] Also, since January 2022 crowdfunding, which is a source of finance for SMEs is subject to regulation.

As outlined earlier, around €2bn of the c. €6bn of annual SME credit is advanced by non-banks, some of whom are unregulated while others are within the regulatory perimeter. As protections for SMEs, particularly micro and small enterprises, should not depend on who you borrow from, and in the interests of ensuring a level playing field, the Review Team recommends the Department prepare legislation to require providers of credit to SMEs to be authorised and supervised by the Central Bank. In preparing this legislation, the Department should consult with the Central Bank and engage with relevant stakeholders to ensure unintended consequences are avoided.

The Review Team recommends that:

Recommendation 10-4

Following consultation with stakeholders, the Department of Finance should prepare legislation to require providers of credit to SMEs to be authorised and supervised by the Central Bank, so that all SME borrowers benefit from the protections of the Central Bank's SME Regulations.

[224] https://economy-finance.ec.europa.eu/publications/post-programme-surveillance-report-ireland-spring-2022_en

SME REGULATIONS AND PERSONAL GUARANTEES

Following its 2015 consultation regarding the SME Regulations, the Central Bank made amendments in relation to personal guarantees in response to feedback it received. As part of its ongoing work, the Department has noted that residual concerns remain regarding the definition of 'unreasonable personal guarantee requirements' and the absence of a requirement for annual advices to guarantors regarding the continued existence of a guarantee, the current exposure under the guarantee and a reminder to the guarantor of the nature of the guarantee – limited or all sums. In this regard, it is proposed that the Central Bank consider these concerns further in the context of a review of the SME regulations.

Given developments since the most recent version of the SME Regulations came into force the Review Team recommends that the Central Bank reviews and amends the regulations. Recommended amendments include the following:

- Amend the regulations so that one set applies to all SMEs
- Expand the regulations to cover all products provided to SMEs
- Strengthen adherence and monitoring systems to ensure compliance with the Regulations
- Reflect any changes required following the completion of the legislative process to expand the remit of the CRO
- Take account of developments in the reformed CP-Code, particularly digital/online matters, automated decision making and customer charters and service standards
- Consideration should also be given to the definition of "unreasonable guarantee requirements" and better information flows regarding ongoing guarantees.

The Review Team recommends that:

Recommendation 10-5

The Central Bank should review and amend the SME Regulations to take account of legislative changes and developments in the revised Consumer Protection Code, particularly digital/online matters, automated decision making and customer charters and service standards. The Central Bank should also review the regulations applicable to guarantees issued by, or on behalf of, SME borrowers.

10.6.Loan pricing

In the most recent CDS, interest rate and fees were identified as the most important factors for SMEs when seeking finance, with net important scores[225] of 79% and 64% respectively, followed by the relationship with provider (58%), type of finance provider[226] (44%) and location

[225] Net Important score denotes the percentage of respondents who, when rating importance using a scale of 1 (not at all important) and 5 (meaning extremely important), answered either 4 or 5.
[226] Example provided e.g. bank or non-bank.

of the provider (21%). This highlights the importance of pricing to borrowing SMEs, while also identifying a preference for relationship with the lender, over type of provider or location.

Lenders price products based on a targeted risk adjusted return on capital – inputs to the calculation include the cost of funding the loan and a margin, where the latter is to cover an allocation of costs (fixed and variable), including the cost of risk and a profit margin on the loan. The perceived riskiness of the lending is a critical component of the pricing calculation – higher risk lending should attract a higher cost of risk and therefore result in a higher price. Loans with a longer tenor are generally more expensive than short-term facilities, albeit, this may not apply to property investment loans (e.g. commercial mortgages).

Since the GFC, to ensure their future viability, the traditional banks have been implementing significant cost saving programmes - they have increased their use of automated decision-making and reduced the extent to which experienced lending staff engage directly with SME borrowers. While cost savings and greater deployment of technology have been necessary, and are a contributing factor to reductions in determining SME loan pricing, the focus by banks on digital delivery is challenging for many SMEs.

It is noteworthy that in some instances SME non-bank lenders, despite the fact that they generally have lower cost structures, apply higher pricing than the retail bank competitors. This could reflect a range of factors, including their smaller scale, the customers' willingness to pay more for a more tailored product or a better service, or it could arise from a risk premium applied by the lender due to higher risk lending.

In terms of risk, banks are required to hold capital to cover unexpected losses on balance sheet assets, which for the traditional banks, mostly comprise their lending portfolios. The riskier the bank's balance sheet, the more capital it is required to hold. In the context of SME credit, this issue was addressed in a Financial Stability Note.[227] The research concluded that within the risk models used by the Irish banks for Irish Non-Financial Corporate (NFC) lending, of which SME credit is a component[228], the major driver is the elevated default rates observed across Irish NFC portfolios relative to European averages. It is particularly noteworthy that the research found that even during the relatively strong Irish economic recovery after the financial crisis, default rates for Irish NFCs remained higher than European averages. Given the fact that Irish SME lending has a higher risk profile it is to be expected that banks will charge more to appropriately reflect the higher risk. It should be noted that where SME loans are covered

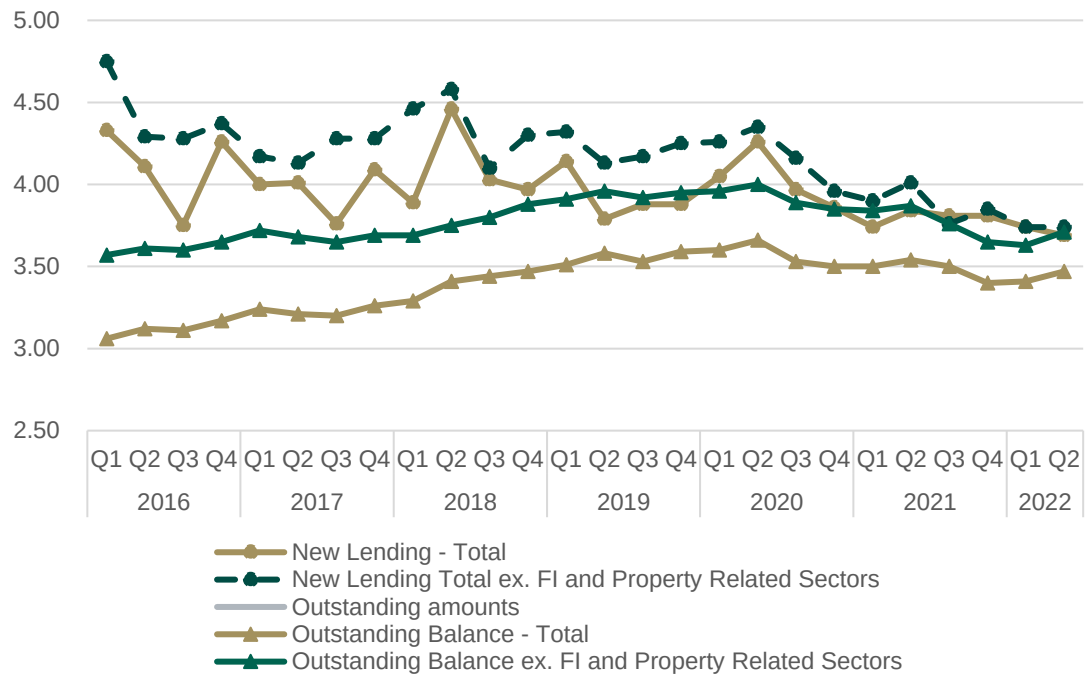
[227] https://www.centralbank.ie/docs/default-source/publications/financial-stability-notes/no-4-risk-weights-on-non-financial-corporate-lending-by-irish-retail-banks-(lyons-and-rice).pdf?sfvrsn=47e4961d_3

[228] The IE traditional banks use models where the inputs are set out mainly in regulation, whereas in many EU jurisdictions banks' develop the statistical inputs to their models based on the specifics of their portfolios, which typically result in lower capital requirements.

by a SBCI guarantee scheme, the lender's risk weight is lower[229], with a consequent lower capital requirement – this saving is passed on to borrowers by means of a lower interest rate.

Interest rates on new and outstanding Irish SME loans are outlined in Figure 16 below[230]. Rates on new lending drawdowns have generally been reducing since 2016, with some quarter on quarter increases evident over the period, culminating in a rate of 3.69% in Q2 2022. While in relative terms these rates do not appear excessive, when compared to Eurozone competitors, rates paid by Irish SMEs are typically higher than most jurisdictions, with only Greece and Malta having rates higher than the Irish average. However, the basis for reporting interest rates for cross-European comparison purposes does not factor in applicable fees, and so the comparisons do not show the overall cost of borrowing, which would be a more appropriate measure.

Figure 16 - Interest rates on new and outstanding SME loans 2016-2022



Source: Central Bank

The downward trend in the interest rates applicable on new SME lending is welcome and provides some evidence of a dynamic lending environment. It is also influenced somewhat by the drawdown of loans that benefit from an SBCI guarantee scheme, and therefore reduced pricing.

[229] Risk weights do not apply to credit unions.
[230] https://www.centralbank.ie/statistics/data-and-analysis/credit-and-banking-statistics/sme-large-enterprise-credit-and-deposits

Arising from the implementation of the Basel III reforms, changes to the loss input components of risk weight models are to be implemented across the EU. In general, this will increase the risk weights for SME loans across the EU, but less so in Ireland. ‘ All else equal’, if this impact on the cost of lending is passed on to SME borrowers in those jurisdictions where higher risk weights will apply, the pricing differential between average Irish and average EU pricing for SME credit should reduce.

Given the upward trajectory in interest rates globally, including in the Eurozone, it is to be expected that the positive trends in pricing evidenced in recent years will reverse as ECB rate increases are applied by Irish lenders.

10.7.Considerations for the future

In the context of a fit for purpose banking sector that will meet SME credit needs in the next 5-10 years, a number of key considerations are:

- The traditional banking sector will have three active providers, once KBC and Ulster Bank leave the market, with AIB and BOI having dominant positions. However in common with other jurisdictions, it is envisaged that the traditional banks will remain the main providers of banking services to SMEs. Accordingly, it is of pivotal importance that those banks provide competitively priced, accessible products and services to SME customers.
- As SMEs have increased the extent to which they access credit from non-banks, the capacity of the non-bank sector to remain active through the economic cycle with be a key factor in the smooth supply of credit. This important factor in ensuring sufficient access to credit to the SME sector through the economic cycle is unproven.
- The sector will need to give greater consideration to devising new credit products to better support Ireland's SMEs to meet the 2030 climate targets.
- The SBCI and MFI are key providers of support to SMEs, and they have delivered real value since they commenced operations. It is important that the provision of credit remains principally the domain of commercial lenders, and that State-sponsored schemes do not displace commercial lending, but rather expand access in line with the SBCI and MFIs mandates.
- Digital delivery of banking products including SME credit will continue to gather pace, requiring greater levels of financial and digital literacy amongst SMEs if they are to engage effectively.
- In the context of digital delivery, all retail banking providers must ensure that their digital offerings are developed in a manner that facilitates users to engage seamlessly, while also recognising that in certain circumstances personal engagement with a borrower, either in person or via remote channels, is appropriate. Delivery models should incorporate this feature.
- With annual demand of €6bn to €7bn for SME credit, and a somewhat mixed view on access to finance, continued focus on access, as well as monitoring the extent to which SMEs have sufficient choice should they choose to borrow remains appropriate.

11. Consumer credit

Consumer credit is generally defined as debt taken out by consumers to purchase goods and services. In many cases this debt is unsecured. In recent years, digitalisation has led to significant changes in the consumer credit landscape, including the emergence of new products and new providers offering credit through faster and more readily accessible channels. In addition, the growth in online purchases has resulted in greater opportunities for online lenders to offer credit at the point-of-sale, making credit more accessible to those who want it.

Whilst this greater access and availability can meet important financial inclusion objectives, it also carries risks, including the risk of consumers becoming over-indebted. In recent years, policy makers have introduced measures to address these new risks. In Ireland, as discussed below, there have been significant legislative developments to extend the application of regulatory requirements to additional credit providers. This also means that the Central Bank's consumer protections apply to consumers of newer and emerging credit products, as well as the traditional range available from existing providers.

11.1.Consumer choice

In the context of two banks leaving the market, the Review Team considered whether consumers have adequate choice of credit providers and credit products across each of the types of consumer credit available in the market.

Consumer credit comes in various forms, and includes loans, overdrafts, personal contract plans (PCP), hire purchase, credit cards and BNPL. Many of these products ultimately offer similar or comparable functionality and benefits as other consumer credit products, and are therefore sometimes interchangeable. For example, credit cards, and to a lesser extent BNPL, offer consumers the same benefits as an overdraft in that they allow consumers the ability to use credit to purchase goods online or at the point of sale.

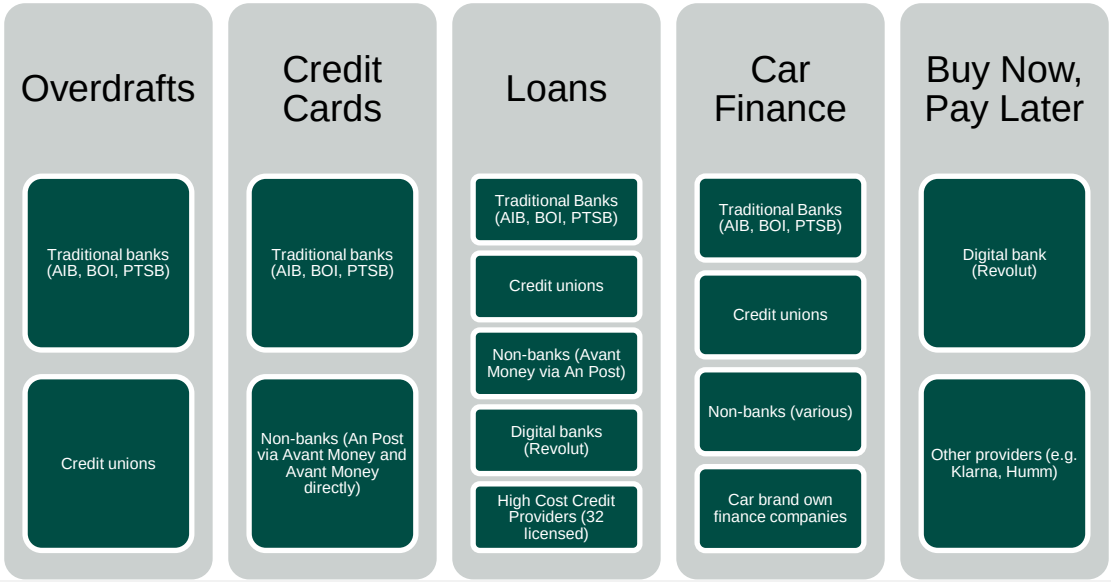
In some cases, the features of certain products may better suit consumer's different needs. For example, credit cards do not charge interest or fees on borrowings if consumers pay their full bill within a set number of days, and so using a credit card may be preferred over an overdraft if the debt can be repaid in full within the set timeframe.

An overview of the current range of providers that offer these products is outlined in Figure 17.

CHOICE OF PROVIDERS

The Review Team considered the range of providers offering each of the principal credit products:

Figure 17 - Overview of providers of consumer credit



Source: Department of Finance

Overdrafts – Overdrafts can only be provided by banks or credit unions. Whilst the withdrawal of Ulster Bank and KBC will reduce the number of firms providing overdrafts to consumers, the remaining three traditional banks, as well as a growing number of credit unions offer overdrafts.[231] The digital banks who currently operate in Ireland are licenced to provide overdrafts, but do not currently offer this product. In certain circumstances, other products such as BNPL and credit cards are products that are potentially interchangeable with overdrafts.

Credit cards – Irish consumers currently have a choice of credit cards from the three traditional banks as well as a credit card offered by An Post, operated by Avant Money. Avant Money also offers its own credit card.[232] Each provider's products have different costs and benefits.

Loans – There are various providers of loan finance in the market with the range dependent on the size of the loan being sought. Consumers can choose from the traditional banks, credit unions, non-banks, and as of 2022, one of the digital banks.[233]

The traditional banks typically offer loans from €2,000 to as high as €75,000, depending on the purpose of the loan. Credit unions also offer choice for various sizes of loans – the average

[231] Since 2016, some credit unions started providing overdrafts and 77 now offer these products to their members
[232] Avant Money, which is licenced by the Central Bank as a retail credit firm, and is owned by Spanish banking group, Bankinter
[233] Revolut now offers personal loans (from €2,000 up to a value of €30,000) to Irish consumers

value of a consumer loan in the credit union sector was circa €8,500 as at September 2021.[234] An Post offers personal loans from €5,000 to €75,000 with a loan term of up to 7 years as an agent for Avant Money. Avant Money also offers personal loans directly to consumers.[235]

For lower value loans, consumers can borrow from credit unions and HCCPs,[236] as well as BNPL providers who offer products that in some cases are similar to loans. In the year to September 2021 credit unions issued 49,371 loans below €500 and 145,442 loans between €500 and €2,000.

Car Finance - For consumers seeking credit to purchase a car, car loans can be obtained from the traditional banks as well as the credit unions, who all offer car finance. Consumers buying cars can also be offered credit at the point of sale, which is typically provided by a specialist lender, or other non-bank that is related to, or in partnership with, the manufacturer of the car. Credit made available through the car dealer channel, usually in the form of hire purchase agreements and Personal Contract Plans (PCPs) provides consumers with more choice beyond the traditional banks and credit unions. Under a hire purchase agreement ownership of the vehicle transfers to the consumer once the last payment is made. PCPs, which are a type of hire purchase and which were introduced in Ireland towards the end of the last decade, offer consumers the choice to repay less of the total amount borrowed during the term of the PCP compared to hire purchase, though this does mean there is an outstanding obligation at the end of the credit agreement.[237] There is some evidence, albeit limited and dated, that PCPs and hire purchase have proved popular choices for consumers.[238]

Buy now, pay later - BNPL is a type of credit agreement offered by a range of retailers and merchants when consumers are shopping online and in-store. The BNPL provider is usually different from the retailer, and therefore the credit contract is with the BNPL provider and not the retailer selling the product. Some BNPL providers have a relationship with the retailer and receive a percentage of the purchase price. However, some providers offer the service directly to consumers at the point of sale and charge a service fee. There are a number of BNPL providers servicing the Irish market.[239]

For lower cost goods (generally less than €500), the BNPL product offering includes interest-free credit, repaid by regular instalments, typically within a short period from the date of purchase (e.g. 30 days). For larger amounts, BNPL operates akin to a personal loan, usually

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[234] https://www.centralbank.ie/docs/default-source/regulation/industry-market-sectors/credit-unions/financial-conditions-of-credit-unions/financial-conditions-of-credit-unions-2021-i.pdf?sfvrsn=108f921d_4
[235] https://www.avantmoney.ie/personal-loans
[236] Central Bank of Ireland Moneylender Register as of 10 October 2022, https://registers.centralbank.ie/DownloadsPage.aspx
[237] https://www.ccpc.ie/business/research/market-studies/personal-contract-plans-irish-market/
[238] As at February 2020, the traditional banks provided €1.2 billion in PCP finance and €1.8 billion in hire purchase. Source: Table A.19: https://www.centralbank.ie/statistics/data-and-analysis/credit-and-banking-statistics/bank-balance-sheets/bank-balance-sheets-data
[239] Klarna, Humm (formerly FlexiFi), Revolut

with interest charged and repayments scheduled over longer periods, typically up to three years.

It should be noted that consumer credit over the value of €500 must be recorded on the CCR[240] together with details of repayments that are overdue, which may affect a consumer's credit record.

PRODUCT CHOICE

The Review Team considered the range of product choice available to Irish consumers, in particular to determine whether there was effective competition between the providers that remain in the market. While the decision of Ulster Bank and KBC to leave the Irish market will lead to the loss of two traditional banks, all of the product types offered by the two banks leaving the market are also offered by other providers operating in the market.

In its review of each of the core consumer credit products, the Review Team identifies that many providers offered different product options within each product type.[241] As outlined earlier, consumer credit products are sometimes interchangeable, and this ultimately broadens the range of choice available.

BNPL and PCP are the main product innovations in the market in the past decade and provide consumers with additional choice beyond the traditional banks and credit unions. A key aspect of these products is that they often provide consumers with near instant credit decisions. The availability of credit close to the point of sale is not new – hire purchase has been available for many years, primarily for the purchase of larger consumer goods. However, the widespread availability of credit, obtainable within minutes via a mobile phone app for products such as clothes and footwear, and from a more diverse range of businesses, is a new development.[242]

The widespread availability of credit, obtainable within minutes via a mobile phone app for products such as clothes and footwear is a new development

Digitalisation and automated credit decisioning are key enablers that have facilitated new providers to enter the consumer credit market. These technological developments also enable the traditional banks and other loan providers to compete at the point of sale. As well as Revolut, each of the traditional banks provide app enabled credit decisions within minutes, with loan funds then made available instantly to the customer's current account.

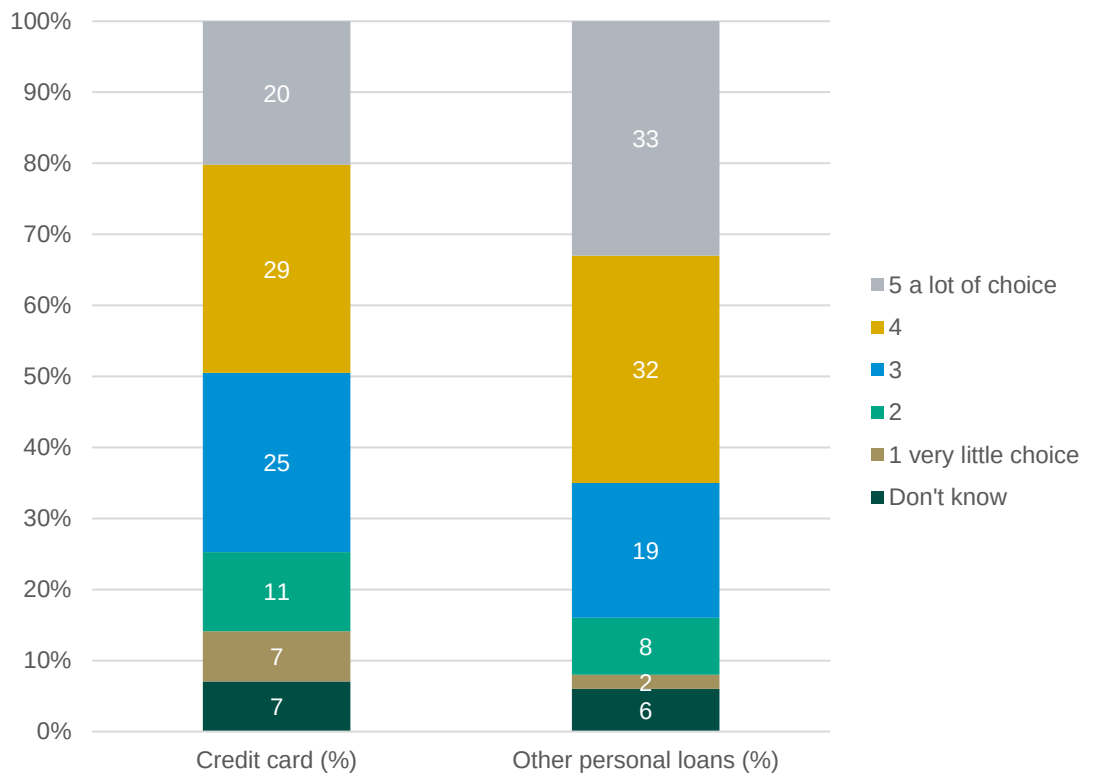
[240] The Register is a national database of personal and credit information that is maintained and operated by the Central Bank, in accordance with the provisions of the Credit Reporting Act 2013
[241] For example, the five credit card providers noted above offered 13 credit card products between them.
[242] https://www.ccpc.ie/consumers/money/loans/buy-now-pay-later/

ACCESS AND AVAILABILITY OF CREDIT – STAKEHOLDER FEEDBACK

In response to the question in the Public Consultation regarding the adequacy of, access to, and availability of consumer credit from the retail banking sector, c. seven in ten of those who responded stated they did not consider access and availability to be adequate. Of those who provided a reason for their answer, a significant proportion stated that their 'No' response was due to a lack of availability of Sharia compliant banking options. The other significant theme that emerged from the 'No' responses was that if local public banking existed in Ireland it may provide more choice. Both issues are addressed in the earlier chapters on Mortgages and Competition.

In the Consumer Survey, when asked about the level of choice and competitiveness in the areas of 'other personal loans' and credit cards, the survey responses suggest there is a reasonable level of choice. Holders of 'other personal loans' consider the level of choice to be better than credit card holders. Figure 18 illustrates this point.

Figure 18 - Perception of Level of choice in market for credit cards and other personal loans among product holders



Source: Department of Finance, Consumer Survey

A potential factor impacting the feedback of respondents, though this cannot be verified without further research, may be the fact that consumers are increasingly making decisions to

access credit 'in the moment,' either at the point of sale or via an app. There may be a lack of awareness as to the range of alternative credit options. From a consumer protection perspective, this lack of awareness may lead consumers to make less informed decisions.

Of interest from the Consumer Survey was that of the 1,507 total respondents, 92 (6.1%) said they currently have a personal loan, whilst 527 (35%) said they currently have a credit card. However, this data may not accurately reflect the full extent to which respondents hold personal loans, as the term 'personal loan' may mean different things to different consumers, and may not capture loans such as car loans, home improvement loans, BNPL, or PCP credit. The Review Team recommends that the Department should carry out the Consumer Survey on an annual basis and adjustments could be made to future questionnaires to reflect learnings and outcomes from the recent survey.

The Review Team recommends that:

Recommendation 11-1

The Department of Finance should commission an annual survey of consumers' experiences and perceptions of the retail banking market based on the consumer survey commissioned for the Retail Banking Review.

THE AVAILABILITY OF GREEN CREDIT FOR CONSUMERS

Consumer credit, and consumer credit providers, have a key role to play in supporting consumers achieve their sustainability ambitions. Good availability of credit can act as a complementary measure to public funding and grants to assist consumers make their homes or cars more energy efficient, and can help them manage the upfront installation costs associated with energy-efficient technologies or renovations.

Consumers are increasingly willing to make sustainable choices, they will only be incentivised to take out green loans if they are competitive and affordable

The State, via the SBCI, is providing assistance to consumers. As previously noted, the SBCI is working on a new €500m residential retrofit scheme for personal consumers to retrofit their homes to a more energy efficient standard.[243] However, a review undertaken in 2021 by an umbrella group for consumer organisations[244] in the EU has found that whilst consumers are increasingly willing to make sustainable choices, they will only be incentivised to take out

[243] https://sbci.gov.ie/news/invitation-for-pre-qualification-to-deliver-the-retrofit-loan-guarantee-scheme
[244] Bureau Européen des Unions de Consommateurs (BEUC)

green loans if they are competitive and affordable. The same review suggested that 'green loans' are not widely offered.[245]

In the course of its work, the Review Team noted some consumer credit providers, though almost solely two of the traditional banks, offer what are termed 'green loans,' with each of these banks offering their customers lower interest rates on these 'green loans.'[246] Consumers can generally avail of these loans to fund home improvements or to fund the purchase of battery electric or plug-in hybrid electric vehicles. However, almost eight in ten of respondents to the Public Consultation considered that the retail banking sector could do more.

In addition to the providers of mortgage and SME credit, and as outlined in the chapter on Climate, the Review Team considers that the retail banking sector should consider how best to expand its consumer credit products and services to help the transition to a lower carbon future.

CONCLUSIONS ON CONSUMER CHOICE

There is no objective evidence to suggest there are material issues with access to or availability of credit to consumers

Based on the work undertaken, as well as stakeholder feedback, there is no objective evidence to suggest there are material issues with access to or availability of credit to consumers. There is also no objective evidence of a lack of competition in consumer lending generally, and while overdraft choice is more limited, there are products available to consumers that can sometimes be interchangeable and offer similar benefits.

However, as outlined hereunder, there is a lack of published data to enable a more complete assessment of the consumer credit market, including current and changing consumer preferences and this represents an information gap which should be bridged. The Review Team's recommendation that the Department commission an annual consumer survey will assist policy makers consider this issue.

11.2.Trends in consumer credit

Given the changing landscape in consumer credit, the Review Team sought to develop its understanding of how consumers are being served by the market, and in particular to understand:

- The size of the overall consumer credit market in Ireland.

[245] https://www.beuc.eu/sites/default/files/publications/beuc-x-2021-076_affordable_green_loans.pdf
[246] APR is in the range of 6.4-6.5% for "green loans"

- Consumer preferences and ability to access the type of credit that they need.
- Consumer indebtedness levels, and whether there is any evidence of emerging stress.
- Trends in consumer credit over time, including on the issues highlighted above.

However, compared to the mortgage and SME credit sectors, there is significantly less up-to-date published data in the area of consumer credit. For example:

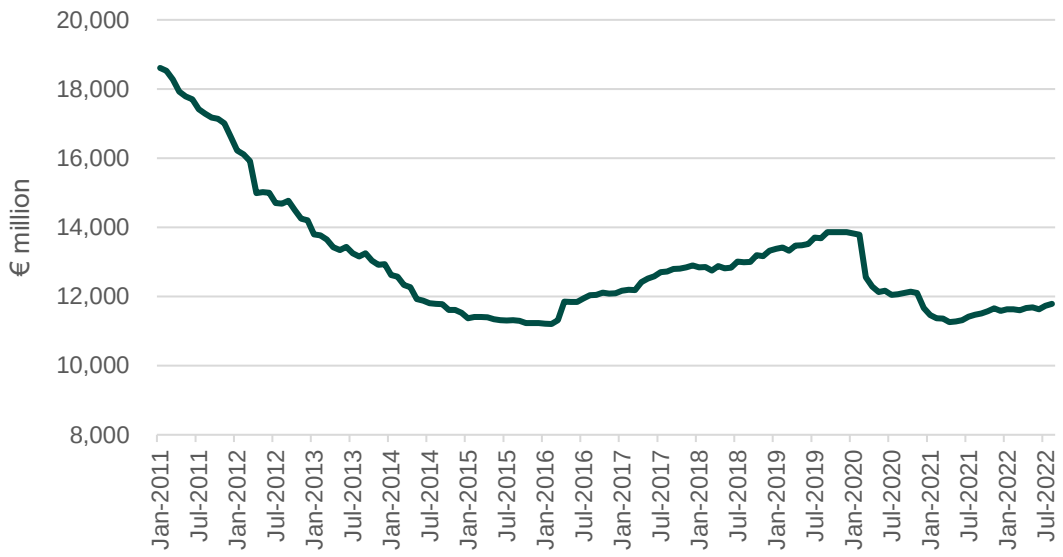
- There is no aggregate data showing the total size of the consumer credit market in Ireland. While the Central Bank publishes regular consumer credit data (in aggregate) for the traditional banks and credit unions, it does not publish data relating to non-bank providers of hire purchase, PCP or BNPL. As such, it is not possible to understand the full scale of the consumer credit market, including concentrations, or whether it appears under or over-served by the current number and range of providers.
- There is no data on lenders' credit activity, including (for example) the number of approvals or declines of credit applications, and the percentage that are decided using automated processes.

Based on data that is available, the Review Team notes the following:

- Consumer credit in the traditional banks and credit unions, which includes hire purchase provided by the traditional banks,[247] has declined 36% since 2011, and stood at €11.8 billion in August 2022. See Figure 19. Due to incomplete data, it is not possible to analyse the extent to which (if at all) the reduction in bank/credit union lending represents deleveraging on behalf of consumers, or if it is a shift to other non-bank providers of credit.
- Personal credit card spending is increasing – total spend increased 25.2% from September 2017 to September 2022.[248] Some of this increase is linked to inflation.
- In 2020, 45.5% of households had non-mortgage loans, 6.7% had overdrafts and 26.8% had credit card debt.[249]
- In 2020, there was €198.1 million of credit advanced by HCCPs, with an average loan size of circa €670.[250]

[247] Both AIB and BOI currently provide hire purchase credit to consumers
[248] https://www.centralbank.ie/statistics/data-and-analysis/credit-and-debit-card-statistics
[249] https://www.cso.ie/en/releasesandpublications/ep/p-hfcs/householdfinanceandconsumptionsurvey2020/debtandcredit/
[250] https://www.centralbank.ie/regulation/industry-market-sectors/moneylenders

Figure 19 - Outstanding Consumer Credit – traditional banks and credit unions



Source: Central Bank

The Review Team considers that the incomplete data represents a blind spot for policy makers, which makes it difficult to properly determine the trends and potential risks in the area of consumer credit. The Department will liaise with the Central Bank on this issue to determine the data that is needed and should, if required, consider recommending using the Minister's powers under the Central Bank Act 1997 to request the Central Bank to collect and publish data on credit agreements, consumer hire agreements and hire purchase agreements. This would help ensure that any future policy interventions, if required, can be informed by more complete data.[251] In addition, and as outlined below, the Review Team is recommending amendments to the reporting requirements to the Central Credit Register (CCR) to ensure the CCR captures more data on lower value credit in the market.

Incomplete data represents a blind spot for policy makers

11.3.Legislative and regulatory framework

There is a strong legislative and regulatory framework in place to protect consumers of credit. Ensuring the best interests of consumers are protected, particularly given the increasing diversity and digitalisation of credit, is a key focus for the Department and the Central Bank.

[251] Inserted into the Central Bank Act 1997 by section 9 of the Consumer Protection (Regulation of Retail Credit and Credit Servicing Firms) Act 2022.

Key developments in the past decade include:

- In 2022, the Oireachtas legislated[252] to ensure additional providers of credit to consumers are regulated, including hire purchase, PCPs and BNPL providers. In practice, this means that the Central Bank supervises and regulates such firms providing credit to consumers, ensuring they adhere to conduct of business requirements.[253] The Central Bank produced an addendum to the CP-Code to reflect the requirements in the new legislation.[254]
- The same legislation capped the cost of consumer credit at a maximum of 23% APR. In addition, there is already legislation[255] that requires banks and retail credit firms to notify the Central Bank if they are proposing to increase fees or charges to consumers, or impose new fees or charges. The requirement to notify the Central Bank also applies to new entrants after they have operated in Ireland for three years.
- In 2022, the Government introduced separate legislation[256] to cap the interest rate that HCCPs can charge. This followed the introduction of new Central Bank regulations[257] that came into effect in January 2021 which placed new requirements on HCCPs to protect consumers.
- The Credit Reporting Act 2013 established the CCR. One important purpose of the CCR is to provide factual information on a borrower's credit history, including details of a borrowers' overall indebtedness and their payment track record. Lenders are obliged to report up-to-date credit information to the CCR where the credit exceeds €500, and lenders are obliged to consult the CCR when a borrower is seeking new credit exceeding €2,000. Lenders are expected to use the information on the CCR to assist them assess the credit worthiness of existing or prospective borrowers. Later on in this chapter the Review Team recommends reductions to these current limits.

Looking forward, there are significant legislative and regulatory developments in the pipeline, including:

- The new Consumer Credit Directive (CCD) – this revised directive, when finalised, will repeal and replace the current 2008 directive on consumer credit agreements. According to the European Council, the revised CCD "aims to promote responsible and transparent practices by all players involved in consumer credit, for example, by ensuring that credit information is presented in a clear and understandable way, and is adapted to digital devices. In addition, to protect consumers from irresponsible lending practices that could lead to over-indebtedness, the directive promotes financial

[252] Consumer Protection (Regulation of Retail Credit and Credit Servicing Firms) Act 2022, signed into law on 11 April 2022
[253] The Central Bank has produced a guide to short term credit: https://www.centralbank.ie/regulation/industry-market-sectors/credit-servicing-firms/buying-goods-and-services-short-term-credit
[254] https://www.centralbank.ie/docs/default-source/regulation/consumer-protection/addendum-consumer-protection-code-2012-may-2022.pdf?sfvrsn=1a9e901d_5
[255] Section 149 of the Consumer Credit Act (1995) https://www.irishstatutebook.ie/eli/2022/act/5/enacted/en/print
[256] Consumer Credit (Amendment) Act 2022: https://www.irishstatutebook.ie/eli/2022/act/13/enacted
[257] https://www.irishstatutebook.ie/eli/2020/si/196/made/en/print

education and debt advice, and lays down stricter rules for assessing whether or not a consumer will be able to repay their credit."[258] It is expected that agreement on the CCD by the Council of the European Union and the European Parliament is imminent, after which the final directive will be adopted. Transposition of the CCD into Irish law will have to be completed within two years of its publication in the Official Journal of the European Union.

- Review of the CP-Code – as already stated, the Central Bank is currently reviewing the CP-Code to ensure it remains fit for purpose given developments in financial services in Ireland, including technological change. A Discussion Paper has been published,[259] which notes how digitalisation is having a significant impact on the provision of consumer credit. The Discussion Paper identifies that:

> *'Many borrowers now access credit online, without any physical contact with the credit provider.'*
>
> *This 'highlights key benefits and risks associated with a move away from a personal interface. The availability of and ease of access to credit can increase the risks posed by irresponsible lending for instance through aggressive and unsolicited marketing driven by online tracking and profiling, which can entice consumers into easily and quickly accessible loans.'*

The Review Team welcomes that the review of the CP-Code, which is expected to be completed in 2024, will, *inter alia*, ensure that consumer protection does not vary depending on whether retail banking products and services are delivered through traditional or digital channels.

11.4.Risks to consumers

In the Public Consultation, the Review Team highlighted that the increased availability of credit from more diverse and digital sources can improve access to credit, and thereby financial inclusion, but there were also risks which included over-indebtedness.

The Public Consultation document highlighted concerns and risks being raised by other stakeholders, including the EBA, which included:

[258] https://www.consilium.europa.eu/en/press/press-releases/2022/06/09/consumer-protection-council-adopts-its-position-on-new-rules-for-consumer-credits/
[259] https://www.centralbank.ie/docs/default-source/regulation/consumer-protection/consumer-protection-code-review/consumer-protection-code-review-discussion-paper.pdf?sfvrsn=f75c951d_12

- Consumers have 'greater difficulty assessing and understanding pre-contractual information when using an online sales channel.'[260]
- Increased digitalisation may lead to personalised unsolicited advertising, which 'may encourage consumers to borrow beyond their means.'[261]
- Poor creditworthiness assessments by credit providers 'may lead to mis-selling of credit to consumers,' as amongst other things, lenders may only consider income levels and not overall expenditure levels. The EBA has found that poor creditworthiness assessments are one of the main trends in consumer credit across the EU.[262] Other common issues identified by the EBA included excessive interest rates and fees and shortcomings in regulatory compliance.[263]

The Public Consultation stated that it was 'important that consumers have good access to credit, appropriate levels of consumer choice, whilst also being protected from over-indebtedness,' and asked stakeholders what they considered the main risks to be in the area of consumer credit. Of the responses received:

- Circa one third referred to the risk of over-indebtedness, with respondents citing the ease of accessing credit, and new forms of credit such as BNPL as being the reasons for their response.
- Circa one third referred to high interest rates, and the excessive cost of credit.
- Circa one quarter referred to consumer's lack of financial literacy and awareness, which exposed them to greater risk.
- Other risks identified were: lack of microfinance for consumers; the departure of a large moneylender from the market; and credit decisions made by computers and not experienced staff.

On the issue of over indebtedness, the Review Team makes a number of recommendations as outlined below, including a requirement that firms providing credit to consumers are required to consult the CCR for lower value loans as part of their affordability assessment process.

Regarding the responses received on the high cost of credit, the Review Team notes that new legislation, enacted 11 April 2022, imposes a maximum charge for consumer credit.

With respect to financial literacy, this is a cross-cutting theme that emerged strongly as the Review progressed. This is discussed in the chapter on consumer protection.

The Review Team acknowledges the role of credit unions in the provision of personal micro credit (PMC). PMC is available through 88 credit unions[264] and the Department is supportive

[260] https://home.kpmg/ie/en/home/insights/2021/07/consumer-credit-responsible-lending-consumer-reform.html
[261] https://home.kpmg/ie/en/home/insights/2021/07/consumer-credit-responsible-lending-consumer-reform.html
[262] https://www.eba.europa.eu/eba-assesses-consumer-trends-20202021
[263] https://www.eba.europa.eu/eba-assesses-consumer-trends-20202021
[264] https://www.creditunion.ie/it-makes-sense-loan/participating-credit-unions/

of efforts to increase the number of credit unions participating in the scheme. The PMC is a low value credit union loan at a low interest rate for people who are getting a social welfare payment. The scheme aims to reduce dependence on HCCPs that charge very high interest rates.[265]

11.5.Protecting consumers of credit

For consumers and for the economy at large, it is critical that sustainable consumer credit remains accessible and available. For consumers, it enables the purchase of essential products and services when they are needed, particularly 'big ticket' items. For the economy, when consumers can borrow money, economic transactions take place efficiently and the economy can grow. Once debt is sustainable, it is a positive feature of economic activity.

Digitalisation has greatly aided the efficient functioning of the consumer credit market, and has ensured consumers can get frictionless, and near instant, access to credit when they need it. However, this increased access comes with risk. In particular there is some concern that vulnerable borrowers may become over-indebted through multiple small loans, in particular at a time when many consumers will face new or increased affordability challenges, due to the current increase in the cost of living.

In this context, it is critically important that lenders act in a responsible manner by maintaining high underwriting standards, ensuring that consumers do not take on debt where it is clear that they cannot afford to repay it. Lenders must, to the greatest extent they can, obtain complete visibility on consumers' financial positions, and overall levels of indebtedness, before granting new credit to consumers. To aid this process, lenders can check a consumer's existing credit obligations on the CCR. However, loans below €500 are not recorded on the CCR, which may limit a lenders' visibility on a borrower's debt levels.

This raises the issue of whether the €500 CCR reporting limit should be amended to help protect consumers against over-indebtedness. Currently a consumer could enter into multiple sub-€500 loans from different credit providers within a short period of time, which could lead to excessive short-term debt with unsustainably high repayments.

There is some concern that vulnerable borrowers may become over-indebted through multiple small loans

Furthermore, the Department has been called upon in the past by the Social Finance Foundation (SFF) to reduce the threshold for recording credit on the CCR to €200. The SFF say this would enable borrowers of lower value credit to build a good credit history and, thereby, enhance their opportunities to obtain credit from cheaper credit providers in the future.

[265] https://www.citizensinformation.ie/en/money_and_tax/personal_finance/loans_and_credit/microcredit_loans.html

Taking into account the risks to consumers, as well as opportunities that the lowering of the CCR threshold could offer, the Review Team recommends, following further engagement with relevant stakeholders, that the threshold for reporting debt to the CCR should be reduced from €500 to a lower level of €200.

In tandem with changing the reporting threshold, the Review Team also recommends that the CCR consultation threshold of €2,000, above which lenders are obliged to request a copy of a potential borrower's credit report, should also be lowered, potentially to €1,000. The actual new threshold should be determined following engagement with relevant stakeholders. An initial review of the Credit Reporting Act 2013 suggests that primary legislation may be required to effect these changes but this would have to be determined through legal advice. In making these changes, data protection requirements will also have to be considered.

The Credit Union Advisory Committee (CUAC) has previously recommended that the fee to access a prospective borrower's credit report be reduced for lower value loans. A lower fee for lower value loans would assist with one of the key objectives of the credit union movement - to provide low value loans to lower income customers at a reasonable interest rate. As this would help increase financial inclusion, the Review Team recommends the introduction of a lower fee for lower value loans. This level of the lower fee should be determined following engagement with relevant stakeholders. Changing the CCR fee structure may require primary legislation.

The Review Team recommends the following:

Recommendation 11-2

The operation of the Central Credit Register should be amended, following engagement with relevant stakeholders, to:

- Reduce the reporting threshold for credit agreements from €500 to €200 and the consultation obligation threshold from €2,000 to €1,000; and
- Introduce a new lower fee for Central Credit Register consultations for low value loans (i.e., loans of less than €1,000, in line with the proposed changes to the obligatory consultation threshold) to facilitate smaller loans, particularly by credit unions.

The Department of Finance should draft legislation, if the proposed amendments require it.

12. Current and savings accounts

Access to a current or payment account is essential in modern life.[266] Individuals and SMEs use these accounts to receive and make day-to-day payments, which are increasingly being made using digital means. Due to innovations in payments technology and changes in European regulation[267] which expanded the range of entities that can provide payment services, consumers and SMEs in Ireland have greater choice in the range of providers available to them. Technological innovations include speed of execution and additional product features.

12.1.Current accounts

Almost every adult in Ireland (98%) holds a current account.[268] Traditionally, the current account was the gateway for banks to develop a long-term relationship with a customer that facilitated cross-selling of other banking products and services. By having access to a customer's lodgements and payments history, banks could also assess a customer's repayment ability. ESRI research commissioned by the Department, which will be published in due course, found that in choosing a mortgage, personal loan or credit card provider, a key factor influencing a consumer's decision was the fact that they already had a product with that provider.[269]

In recent years, An Post and the credit unions entered the current account market. Consumers can open current accounts in all 912 post office branches, and of the 204 credit unions, 77 offer current accounts to consumers. In addition to Central Bank authorised payment and electronic money institutions, EU firms have also used passporting opportunities to enter and compete in the Irish market.[270] Some of these providers also offer other products, such as credit, to their current account customers.

Innovations in current accounts relate mainly to digitally enabled access online or via an app, and faster transfer times when making payments. Within Europe, the Single Euro Payments Area Instant Payment scheme (SEPA Instant), facilitates electronic retail payments in real time and can make funds available for use by the recipient in less than 10 seconds.[271]

To date, in Ireland, only the digital banks offer SEPA Instant to their customers. The traditional banks (AIB, BOI, PTSB and KBC) have developed their own instant payment platform (Synch), which has yet to be launched. Meanwhile, the European Commission recently published a

[266] For ease of reading current and payment accounts will be collectively called current accounts throughout this review.
[267] Payment Services Directive 2: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex%3A32015L2366
[268] Consumer Survey
[269] ESRI research commissioned by the Department on switching (forthcoming)
[270] Revolut and N26 have been active in Ireland for a number of years, while Bunq entered the market earlier this year.
[271] There are nine participants in the SEPA Instant scheme domiciled in Ireland, none of which are the traditional banks.

proposed amendment to the SEPA Regulation that will mandate all banks to adopt SEPA Instant in 2023.[272]

The current accounts that are offered by the traditional banks, credit unions and digital banks are eligible for protection under a Deposit Guarantee Scheme (DGS),[273] which means the money held in such accounts, combined with funds held in other accounts with the same institution, are protected up to a value of €100,000 per customer (see Box 3).[274]

Box 3 - Deposit Guarantee Scheme

Administered by the Central Bank and funded by those entities covered by the scheme, the Irish DGS protects depositors in the event of a bank or credit union that is covered by the DGS being unable to repay customers' funds. The DGS protects deposits belonging to individuals, companies, partnerships, clubs and associations. The DGS covers various types of account, including current accounts, payment accounts and savings accounts, to a maximum level of €100,000 per customer per institution.

The Irish DGS covers the domestic Irish banks and credit unions – these are listed on registers published by the Central Bank. Banks licenced outside of Ireland, i.e. Bunq, N26 and Revolut are covered by the deposit guarantee schemes in The Netherlands, Germany and Lithuania respectively, also to a limit of €100,000 per customer per institution.

CHOICE OF PROVIDERS

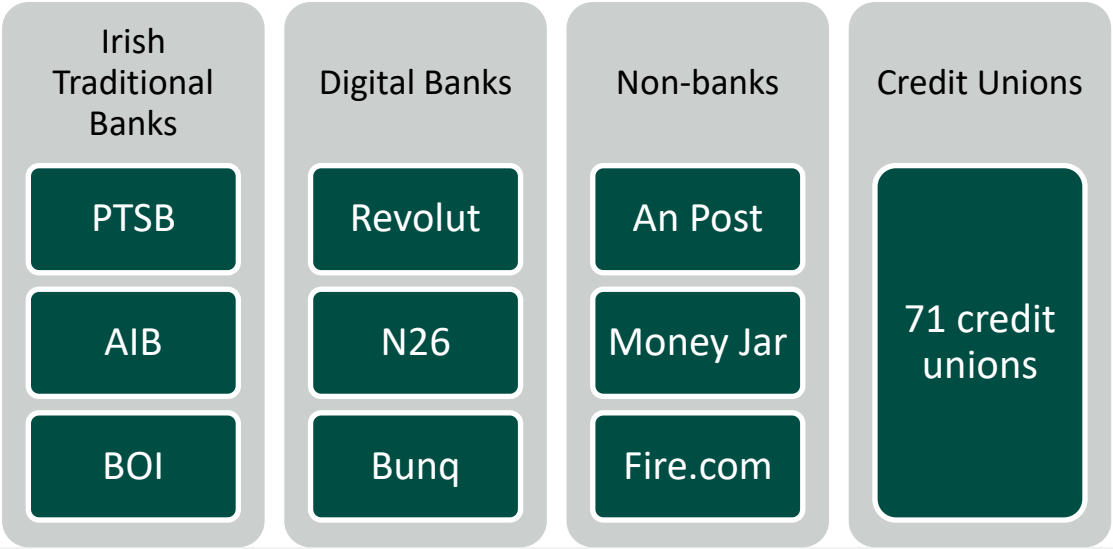
While there are currently ten providers of current accounts in the retail banking sector (see Figure 20), not all provide current accounts to both consumers and SMEs.[275] Of the ten providers, only the traditional banks (AIB, BOI and PTSB), the digital banks (Revolut, Bunq and N26) and one payment firm (Fire.com) provide current accounts to SMEs where the SME is a limited company.

However, for consumers and SMEs who want an overdraft, the choice is limited to those providers that are licenced to provide credit, namely banks and credit unions. Currently the traditional banks and some credit unions provide overdrafts to consumers, however only the traditional banks provide overdraft facilities to SMEs. While all the digital banks are licenced to provide overdrafts, they do not currently offer this product in Ireland.

[272] https://ec.europa.eu/commission/presscorner/detail/en/IP_22_6272
[273] The applicable scheme is determined by the country where the deposit holding institution is authorised.
[274] Some customers are not covered by the DGS, more information on customers who are and customers who are not covered by the DGS is available here: https://www.depositguarantee.ie/en/what-we-cover/protected-depositors
[275] The suppliers of current accounts to consumers are the 3 retail banks, the 3 digital banks and some credit unions, An Post and Money Jar. The suppliers of current accounts to SMEs are the 3 retail banks, the 3 digital and Fire.com.

In the Public Consultation, the Review Team asked if there was an acceptable level of choice for consumers and SMEs when they are choosing a provider of current accounts.

Figure 20 - Overview of providers of current accounts



Source: Department of Finance

Of those that responded, circa four in ten stated there is sufficient choice in the market, whilst the remainder suggested there was not. Reasons given by respondents who answered that there was not sufficient choice were (1) SMEs who want to have their financial needs met by one institution have a more limited choice, as only the traditional banks provide current accounts as well as SME credit (2) a local public bank would provide more choice and (3) the departure of Ulster Bank and KBC will mean less competition in the market.

Consumers continue to prefer to have their main current account with a traditional bank

Among those respondents who stated there is sufficient choice, the feedback suggested this was due to good choice being available beyond the traditional banks, such as from the credit unions, An Post and the digital banks. Notwithstanding the entry into the market of new providers such as the digital banks, it is clear that consumers continue to prefer to have their main current account with a traditional bank. The Consumer Survey found that 92% of consumers have their main current account with one of the five traditional banks, with AIB and BOI accounting for circa 70% of

the total market. Whilst the digital banks have developed a significant market presence,[276] the Consumer Survey found these accounts are secondary to consumers' main bank account.[277] There is some evidence that consumers may be increasingly considering a digital bank for their main account, however a significant majority (73%) of consumers who are currently switching from Ulster Bank and KBC still seem to prefer their main account to be with a traditional bank.[278] This continued strong consumer preference may limit the commercial opportunities for new digital banks to enter the Irish market.

Greater consumer choice could come in the form of the existing digital banks expanding their product range to include business accounts with overdrafts – there are no legislative or regulatory barriers preventing this from happening. Similarly, payment firms can avail of a regulatory regime[279] that is designed to improve competition in order to enter the market and provide consumers and SMEs with more choice, albeit not with overdrafts. Furthermore, all licenced banks within the EU and the EEA can enter the Irish market under the passporting regime. The decision whether or not to enter the Irish market, or expand the product range currently on offer, is ultimately a decision for firms and will be influenced by, amongst other things, the extent of the commercial opportunity they see.

The decision to enter the Irish market or expand the product range, is a decision for firms and will be influenced by the extent of the commercial opportunity they see

Credit unions already provide personal current accounts, and the Central Bank is actively considering expanding its approval to also encompass current accounts for SMEs.

PRODUCT CHOICE

The principal product features of current accounts offered by all providers operating in Ireland tend to be similar. All accounts offer direct debit and standing order payments; debit cards; contactless, chip & PIN and online payments, plus access via mobile apps. The traditional banks' current account offering continues to include cheque facilities and can accommodate an overdraft facility (where approved). Credit unions that provide current accounts can also provide an overdraft facility (again, where approved). Most providers offer some or all of the most popular mobile payment options, including Apple Pay, Google Pay and Fitbit Pay.

There is good evidence of competition and innovation in the area of fees and charges levied on consumer current accounts. There are a range of fee structures in place across all

[276] The Consumer Survey has found that almost 1 in 5 consumers hold a current account with a digital bank despite their relatively recent entry to the market.
[277] According to the Consumer Survey just 1% of respondents using Revolut as their main current account despite the fact that 18% of adults hold an account with them.
[278] Almost 1 in 4 switchers are from Ulster Bank and KBC are considering a digital-only provider:https://www.ccpc.ie/business/research/market-research/ccpc-switching-research-phase-2/
[279] Payment Services Directive 2: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex%3A32015L2366

providers, with some providers offering accounts with no maintenance fees. Some providers offer free banking for people in different age groups, such as children, students, graduates or older age groups. Providers that offer products, other than current accounts, may offer their customers free or reduced fees if they avail of one of these products, such as a mortgage. Some providers do not charge for ATM withdrawals, while some charge for each withdrawal, or charge a fee when withdrawals exceed a certain number per month. Overall, the Review Team considers there is a good range of product choice, based on fees or charges, that enables consumers choose a current account that aligns with their needs, budget or how they use their account, enabling them manage the fees and charges they incur.

With respect to current account fees and charges, banks and non-banks[280] are required by legislation, namely section 149 of the Consumer Credit Act (1995) to notify the Central Bank where they are proposing to increase an existing fee, or impose a new fee. These notifications are assessed by the Central Bank, which may either approve (in full or at lower levels than requested) or reject an application. These legislative provisions also apply to new credit institutions after they have operated in Ireland for three years. The Review Team considered whether the obligation to notify the Central Bank should be removed, amended or retained and concluded that, in the context of a relatively concentrated market for current accounts, and the level of concentration in the retail banking market more generally, it would not be appropriate to remove or amend section 149 at this time. With regard to credit unions, they have to notify the Central Bank of the income they expect to accrue from any charges when they apply for authorisation to offer a new service and these are considered as part of that process.[281]

The Public Consultation, in addition to asking if there is sufficient choice of current account providers, also asked if there was an acceptable level of product choice from the providers, in terms of range and features, available to consumers and SMEs. Of those that responded to this question, almost five in ten stated there is sufficient choice among products with the remainder stating there is not. In general terms, the feedback among the respondents who answered that there is insufficient product choice was as follows:

- Some product features which are available in other European markets, such as SEPA Instant, are not available here.
- There is a lack of Sharia compliant products, though these comments principally related to mortgages;

Among those who considered there to be good choice, the feedback was that the traditional banks, the digital banks, An Post and the credit unions offer good choice, with their products having a range of product features.

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[280] Retail Credit Firms
[281] Payment Institutions and Electronic-Money Institutions are not covered by section 149, this is being examined by the Department.

The product choice is more limited for SMEs who are limited companies that require an overdraft facility. In effect, these customers are restricted to the current account products offered by the traditional banks. However, where an overdraft facility is not required there is a range of products available to SMEs, including innovative offerings from the digital banks and non-banks.

In the course the Review, the Review Team reviewed the offerings and choice that consumers have when looking to open a basic bank account. Under EU law,[282] any consumer who is legally resident in the EU and who does not already have a current account with a credit institution in the State has the right to open and use a current account with basic features. Customers who qualify for a basic bank account do not pay any fees or charges for everyday banking for the first year at least, and possibly for longer depending on their income level. Basic bank accounts are considered important products to ensure financial inclusion.[283]

The Review Team identified that the basic bank account offered by some of the traditional banks did not offer customers features that were on a par with their standard product offerings. For example, the debit card associated with the basic bank account may not have the facility to make contactless payments.[284] The Review Team calls on the relevant banks to offer the same product features, where appropriate, to customers with basic bank accounts as they do to customers with the bank's standard product offering.

It is critical that consumers and SMEs have the choice and ability to switch their account freely and without friction

SWITCHING

In a market that has become more concentrated due to the departure of Ulster Bank and KBC, it is critical that consumers and SMEs have the choice and ability to switch their account freely and without friction to another provider in order for the market to remain competitive. Good levels of switching help to ensure the market remains competitive, and are also important to support new providers enter the Irish market and build scale.

As is also the case with mortgages, historically current account switching levels have been very low in Ireland. Between 2014 and 2021, a total of only 1.32% of personal current account holders switched providers (see **Figure 21**). This is despite a number of initiatives by the Department, the Central Bank and the CCPC to boost switching levels.[285]

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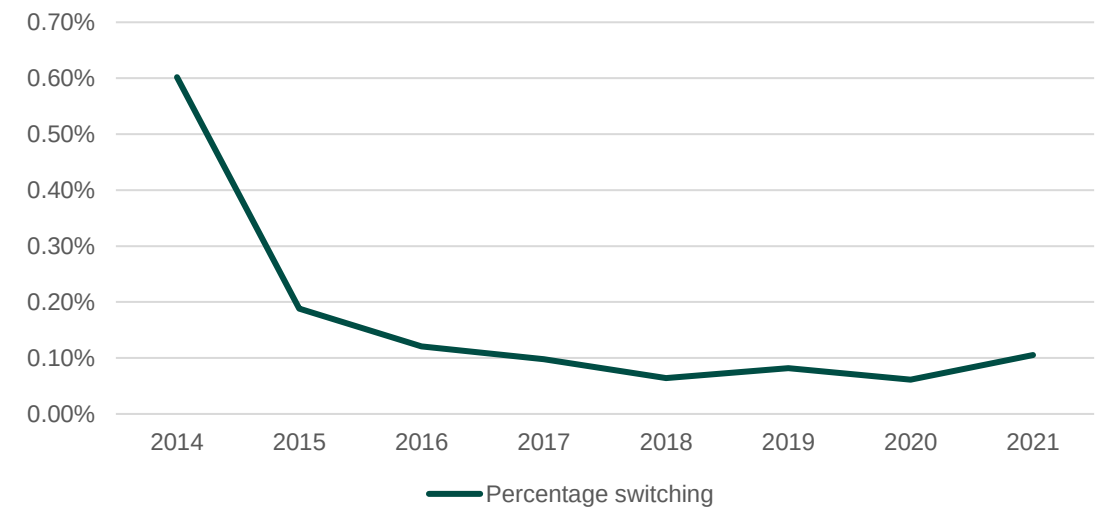
[282] Directive 2014/92/EU of the European Parliament and of the Council of 23 July 2014 on the comparability of fees related to payment accounts, payment account switching and access to payment accounts with basic features: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32014L0092
[283] https://www.centralbank.ie/news-media/press-releases/press-release-consumer-protection-bulletin-20-june-2019
[284] BOI and PTSB provide contactless payment features, whilst AIB does not.
[285] The Department launched the "Switch your bank" website (https://www.switchyourbank.ie/), the Central Bank introduced the current Switching Code in 2016 and the CCPC set up the Money Tools comparison service

The Consumer Survey provided the Review Team with some up-to-date insights on the reasons for the low levels of switching, with respondents appearing to suggest that a general difficulty in the switching process was the principal reason for them not moving their account to another provider.[286] The Consumer Survey also suggested that consumers perceive there to be a lack of alternatives to their current provider and therefore see no reason to switch even if they consider it.

Figure 21 - Personal current account switchers as a % of current account holders



Source: Central Bank

The Central Bank's 2016 *Switching Code*[287] was designed to make the process of switching accounts quicker and easier. The customer's new bank must provide their new customers with a switching pack and information on how to complete the switch.[288] While the objective of the Switching Code is to make the process of switching bank accounts easier for all involved, the process is not always straight forward. For example, while standing orders can be automatically transferred over to the customer's new account and Irish direct debit

While the objective of the Switching Code is to make the process of switching bank accounts easier for all involved, the process is not always straight forward

(https://www.ccpc.ie/consumers/money-tools/). In addition, significant research has been undertaken to better understand the behavioural factors influencing switching levels.

[286] Responses to Q.34 of the Consumer Survey suggested the time it takes to switch and the information required in the process can act as barriers to switching.

[287] https://www.centralbank.ie/docs/default-source/regulation/consumer-protection/45-gns-4-2-7-code-of-conduct-o.pdf?sfvrsn=1b59d71d_6

[288] https://www.centralbank.ie/docs/default-source/Regulation/consumer-protection/other-codes-of-conduct/45-gns-4-2-7-code-of-conduct-o.pdf

originators will be informed of the switch by the customer's old bank, the customer must move incoming payments like salaries and pensions as well as outgoing payments linked to a debit card manually. The customer must also inform non-Irish direct debit originators of their new account details.

The departure of Ulster Bank and KBC from the market is resulting in almost 1.25 million personal and business customers having to move their current and deposit accounts.[289] A key opportunity will exist during 2023 to examine the real and practical challenges encountered by customers' when moving accounts. The lessons that will be learned will be valuable to inform the development of future initiatives to improve switching levels. Based on insights gained by the CCPC to date, it would appear that moving direct debits and regular payments is the biggest challenge currently being faced by Ulster Bank and KBC customers.[290]

The Central Bank's financial stability note, *The Great Account Migration: Lessons from Behavioural Economics*, suggests that Irish consumers show a high degree of entrenched inertia in financial products, with subdued switching rates even where the financial incentive to take action is strong.[291] The paper highlights the need to avoid unnecessary frictions in the consumer journey. As noted in the chapter on Mortgages, the Department has commissioned the ESRI to undertake a three phase project on switching in financial services, including current accounts. The third stage of this work is currently underway and includes a trial on decision aids on switching in large scale field studies. The Department's future work on switching and engagement with the Central Bank on this topic, will be informed by the ESRI findings.

To support customers to switch providers, two potential initiatives that the Review Team became aware of are IBAN portability and a dedicated switching service such as has been implemented in other countries.

IBAN portability

IBAN portability could assist consumers and SMEs to switch their current account provider without having to change their account number. This would be similar to the way mobile phone customers can switch providers without having to change their phone number. IBAN portability could remove many of the frictions from the current account market as an account holder, or their incumbent provider, do not need to contact direct debit originators or organisations sending them payments when they switch providers.

[289] https://www.centralbank.ie/docs/default-source/statistics/data-and-analysis/credit-and-banking-statistics/account-migration-project/account-migration-statistical-release---09-september-2022.pdf?sfvrsn=fdf2941d_4
[290] https://www.ccpc.ie/business/research/market-research/ccpc-switching-research-phase-2/
[291] https://www.centralbank.ie/docs/default-source/publications/financial-stability-notes/great-account-migration-lessons-behavioural-economics.pdf?sfvrsn=6f039a1d_5

IBAN portability would also have benefits for all direct debit originators as they would no longer need to change a customer's account details at the instruction of a payment institution (as they currently do under the Switching Code) or at the instruction of the customer.

However, IBAN numbers include national identity information, for example 'IE' for account holders in Ireland, which are used to route payments to the correct country, to the correct payment institution in that country and finally to the correct account in that institution. The Dutch national competition authority, the ACM, has explored options to support IBAN portability and has proposed a system it calls alias portability, where an alias is used by account holders and businesses, such as a phone number or email address, to identify customers' accounts.[292] These aliases would refer to an IBAN in a database that the payment services provider would use to identify the correct account. Any such solution would need to be explored further and if adopted, must be done so at an EU level. The Review Team welcomes that the Department will advocate for an in-depth study on the feasibility of IBAN portability, including a full cost benefit analysis, at the European Commission level.

Switching service

The Payment Account Directive (PAD) required EU Member States to establish a quick and easy process for consumers to switch their current accounts from one provider to another. In Ireland the Central Bank's Switching Code provides the rules a current account provider must follow to be compliant with the PAD.[293]

Switching services in other countries have built on the requirements set out in the PAD. For instance, some countries have introduced switching services which, among other things, include an automatic rerouting of payments from an old account to the new account.[294] This seeks to allay consumers' fears that something may go wrong in the switching process.

The UK Current Account Switching Service is an example of a switching service in operation in another country. The UK switching service offers users a guarantee that the service is free to use, that all payments including direct debits, standing orders, and payment of salary will be moved by the new provider, that accidental payments to the old account will be automatically redirected, and any interest or charges incurred as a result of an error in the switch will be refunded. While not all customers use this option in the UK, the level of use is far in excess of the use of the Switching Code here in Ireland.[295]

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[292] https://www.acm.nl/sites/default/files/old_publication/publicaties/15948_account-number-portability-2016.pdf
[293] https://www.centralbank.ie/docs/default-source/regulation/consumer-protection/45-gns-4-2-7-code-of-conduct-o.pdf?sfvrsn=1b59d71d_6
[294] For instance the UK switching service https://www.fca.org.uk/publication/research/making-current-account-switching-easier.pdf and the Dutch switching service https://www.betaalvereniging.nl/en/payment-products-services/switching-service/#:~:text=The%20service%20ensures%20that%20payments,of%20the%20new%20account%20number.
[295] In 2021 in the UK a total of 782,223 current accounts switched using the switching service. This compares to a total 5,746 current accounts that switched in Ireland in 2021 using the Switching Code.

Conclusions on switching

The market for current accounts in Ireland is relatively concentrated, but there are a number of providers in this market beyond the traditional banks providing choice for consumers. Innovation in product offerings and competition is evident.

It is important that the lessons learned from the migration of KBC and Ulster Bank customers are reflected in a revised Switching Code

However, the relatively concentrated market for current accounts means measures need to be taken to make the switching process easier. It is important that the lessons learned from the migration of KBC and Ulster Bank customers are reflected in a revised Switching Code for current and payment accounts. The Review Team recommends that once the mass migration of current accounts is largely completed, the Central Bank should review the Switching Code to take account of lessons learnt in the intervening period and that consideration is given to establishing a switching service in line with what has been implemented in other countries.

This will have the twin benefits of making it easier for consumers to switch between the existing providers of current accounts in Ireland and also making it easier for consumers to move to future entrants. This would, in turn, help make the Irish market more attractive to such new entrants. The Review Team also calls on the retail banking sector to use the lessons learnt from the current migration of customers from Ulster Bank and KBC to improve on their own switching processes.

The Review Team recommends that:

Recommendation 12-1

The Central Bank should conduct a review of the Switching Code for payment accounts as soon as possible after the current mass migration of accounts is largely concluded. The review should incorporate input from the sector and other stakeholders regarding lessons from the mass migration. The review should also consider requiring the establishment of a switching service in accordance with the Payment Accounts Directive, including examining the feasibility of automatic or manual routing of credit and debit transfers for a set period after an account has switched.

12.2.Savings accounts

A savings account is a retail banking product that allows consumers and SMEs deposit and store their money while historically earning interest on these deposits.

In order to offer savings products, providers of savings accounts must be a bank or a credit union. Higher regulatory standards apply to entities that hold customer deposits. Deposits held

in banks and credit unions are eligible for protection under the DGS, within the overall limit of €100,000 per customer, per institution.

CHOICE OF PROVIDERS

There are currently eight potential providers of savings products in Ireland, namely the three traditional banks, the three digital banks and the credit unions. In addition, savings products are also available from State Savings, which are fully protected by the State. An Post acts as an agent for State Savings.

In practice however, the choice of provider is more limited. For the most part, the digital banks' product only offers customers the ability to save into ancillary accounts that are directly linked to their current accounts – they are not standalone deposit accounts. Whilst the digital banks are licenced to provide separate deposit accounts, which earn interest, they do not presently offer these products in Ireland even though they offer these products in other countries. The exception is Bunq – it offers standalone savings accounts to Irish consumers.

In the Public Consultation, the Review Team asked if there was an acceptable level of choice among deposit account providers to consumers and SMEs. Of those who responded, just over four in ten said that there is sufficient choice, with the remainder stating there is not. Similar to the responses for current accounts, among those who suggested there was insufficient choice, the feedback was that with the departure of Ulster Bank and KBC there will be less competition in the market. Others suggested that local public banks, with a different stakeholder focus, would provide more choice.

Given the licencing requirements to take deposits, the options to expand the number of providers are:

- Existing EU/EEA licenced banks passport into Ireland to provide deposit accounts.
- The two other existing digital banks expand their product offering to include deposit accounts.
- Future newly licenced EU/EEA banks engage in deposit taking in Ireland either by seeking a licence here or having been authorised in an EU/EEA country passport into Ireland.

PRODUCT CHOICE

In the past, banks who have competed for savings have tended to differentiate their product by offering customers based on the interest rates available, as well as ease of withdrawal.

However, over the past decade, interest rates on deposits in Ireland have been at historically low levels, reflecting the low interest rate environment across the Eurozone. As well as this, the traditional banks have been holding excess levels of deposits, that increased significantly during the pandemic, which meant that there was no incentive for them to compete by

developing or offering innovative and attractive product features, including competitive deposit interest rates. Indeed, for a period, the ECB levied negative interest rates on banks that had excess deposits. This meant that holding these excess deposits came at a real cost to banks and credit unions, and in Ireland banks dis-incentivise some savers by passing these negative interest rates to those with very high deposit levels, whilst some credit unions acted to restrict the level of deposits any one customer could place with them.

A review of the traditional banks' websites suggests they have multiple and varied products, albeit with no or low interest rates. The range includes demand and fixed term deposit accounts, as well as regular saver or lump sum saver accounts. Some accounts target certain consumers, such as children or students, whilst some offer online savings account which consumers can use via internet banking. Some accounts have minimum balance requirements – but this can range from €1 to thousands of euro. State Savings offer fixed term and regular saving products, as well as 'book Based Deposit Accounts' that enable savers to make lodgements and withdrawals at any post office.

For SMEs, there are also a range of options available on the banks' websites including demand and fixed term deposit accounts. Credit unions also offer savings accounts to SMEs. State Savings products are restricted to personal customers.

In the Public Consultation, the Review Team asked if there was an acceptable level of product choice in terms of the range and features available to consumers and SMEs. Of those that responded, circa eight in ten said there was a low level of product choice in the market. Of those that stated there was low choice, the feedback obtained was that product choice will be reduced with the departures of Ulster Bank and KBC; whilst others commented that interest rates are low for all products or that all the products on the market are the same.

Among those who answered that product choice was acceptable, the primary reason was that there are enough products on the market but noting that due to the low interest rate environment, all providers offer low returns.

13. Consumer protection, financial inclusion and literacy

13.1. Consumer protection

Ensuring the best interests of consumers are protected is a priority for the Department, the Central Bank and the FSPO. It has also been a key focus of the Review Team in the course of its work, and this is reflected in the topics that have received particular focus in this Review, as well as in the nature of the recommendations being made, including those outlined in respect to access to cash and customer service standards. A significant number of these recommendations are directed to the retail banking sector, as it is the firms within the sector that have responsibility, in the first instance, to act in the best interests of their customers, and to protect them.

It is the firms within the sector that have responsibility, in the first instance, to act in the best interests of their customers, and to protect them

CONSUMER PROTECTION FRAMEWORK

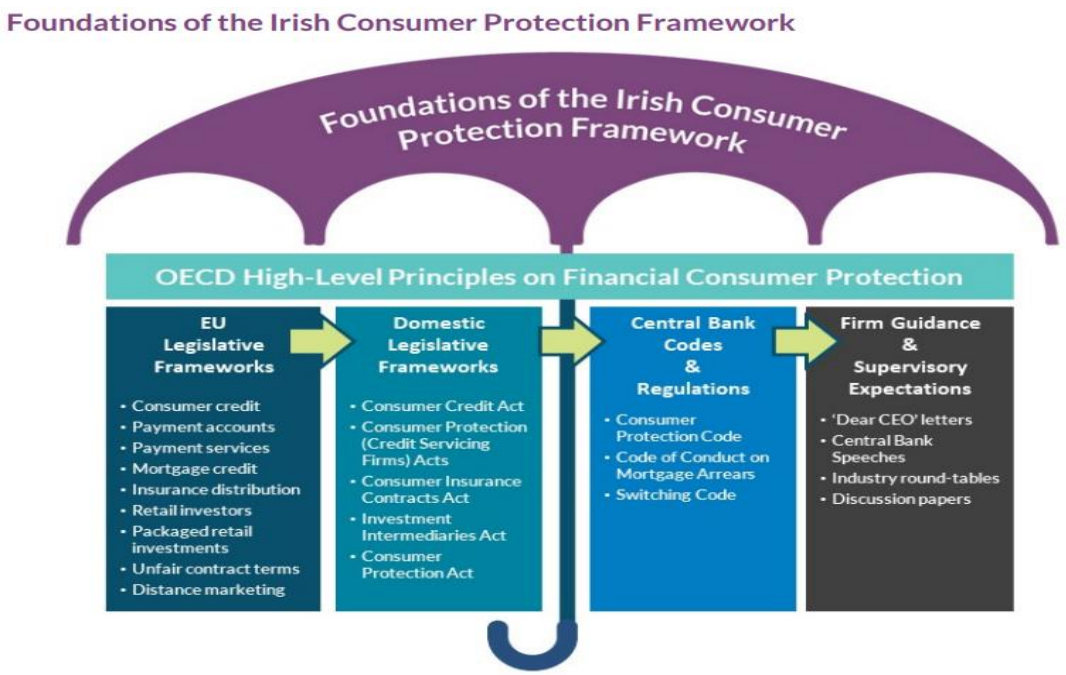
Ireland has a very strong and well developed consumer protection framework. An overview of this framework is outlined in Figure 22 below, and essentially comprises of four core elements, all of which align with international best standards that are set by the Principles.

The four core elements are:

- EU Legislation
- Domestic Legislation
- Central Bank Codes and Regulations
- Central Bank Guidance and Supervision

The Financial Services and Pensions Ombudsman (FSPO) also plays an important role in protecting consumers. The FSPO assists consumers by helping them resolve complaints in relation to financial service providers.

Figure 22 - Overview of the Irish Consumer Protection Framework



Source: Central Bank

INTERNATIONAL BEST PRACTICE

As already stated, the OECD Principles are considered to be the global international standard for consumer protection, and set out foundations for a functioning financial services market which serves the interests of consumers.[296] They were developed in response to the GFC to enhance financial consumer protection.

The OECD Principles are specifically designed and intended to be applicable to any jurisdiction and are cross-sectoral in nature (i.e. they can be applied to credit, banking and payments sectors, as well as others such as insurance, pensions and investments). Many countries, including Ireland, have adopted the OECD Principles in establishing or enhancing their financial consumer protection frameworks.

The Principles contain high-level policy directions based on agreed good practices and aspirational goals. They cover topics such as Competition, Conduct of Providers, Financial Awareness and Complaints Handling. They are not legally binding, but practice accords them great moral force as representing the political will of OECD members, on whom there is an expectation to do their utmost to fully implement them.[297] Since the adoption of the OECD

[296] https://www.oecd.org/daf/fin/financial-education/g20-oecd-task-force-financial-consumer-protection.htm
[297] https://www.oecd.org/finance/high-level-principles-on-financial-consumer-protection.html

Principles ten years ago, the size and nature of the consumer financial services market has grown and changed considerably, with new types of financial products, services and distribution channels. As such, there is a process underway to update the Principles, with the OECD noting that they must continue to reflect best practice globally, and be forward looking.[298]

An overview of the OECD Principles, including proposed amendments, is outlined in Figure 23 below. The OECD has proposed new Principles, which are highlighted in green in Figure 23, in relation to Access and Inclusion as well as the Quality of Financial Products. It has placed renewed emphasis on areas such as culture in firms, and consumer vulnerability. The OECD has also proposed new cross-cutting themes covering the areas of digitalisation, sustainable finance and financial well-being. Many of these themes have emerged in the course of the work of the Review Team. It is important that firms within the retail banking sector step up and make sure that they meet these international standards of consumer protection.

The Review Team understands that the updated text of the OECD Principles will be submitted to the OECD Council for adoption in December.

[298] https://www.oecd.org/finance/high-level-principles-on-financial-consumer-protection.htm

Figure 23 - G20/OECD Principles

Source: OECD
Proposed changes under review are highlighted in green in terms of new principles and new cross-cutting themes.

RECENT LEGISLATIVE DEVELOPMENTS

Irish consumers benefit from a well-developed consumer protection regime. In recent years there has been significant change in the legislative landscape underpinning consumer protection in financial services. Recent legislation that enhances consumer protection includes:

- The Consumer Protection (Regulation of Credit Servicing Firms) Acts of 2015[299] and 2018[300] ensure that borrowers, whose loans were sold, could avail of the protections under the Central Bank codes.
- The Consumer Protection (Regulation of Retail Credit and Credit Servicing Firms) Act 2022,[301] commenced in May 2022, ensures that hire purchase including Personal Contract Plan (PCP), consumer hire and indirect credit (e.g. Buy Now, Pay Later) providers and servicers now need to be authorised by the Central Bank and, as a result, their customers will benefit from the key protections in the CP-Code. It also set a statutory APR cap of 23% on consumer lending provided by banks and retail credit firms thereby protecting consumers from excessive costs of credit.[302]
- The Consumer Credit (Amendment) Act 2022,[303] commenced in November 2022, changed the law governing high cost credit providers (formally licensed moneylenders), by imposing interest rate caps that are lower than the majority of interest rates charged by the sector and which can be reduced further in future years. The Act also limited the maximum term of HCCP cash loans to one year.
- The Central Bank (Individual Accountability Framework) Bill 2022 (IAF),[304] which is currently before Dáil Éireann, will play a key role in driving positive cultural change in financial service organisations for the benefit of consumers, employees and wider society. The legislation will also enhance the Central Bank's existing regulatory powers. It will make individuals in financial services firms more responsive and responsible by enhancing individual accountability in decision-making. It also sets out conduct standards that apply to regulated financial services providers and individuals performing related functions and providing for the sanctioning of individuals who breach these responsibilities.[305]

Ireland's consumer protection regime has been developed over many years from a mix of primary and secondary legislation (the latter mainly implementing EU legislation) and Central Bank regulations and codes. This has led to the legislative and regulatory landscape becoming fragmented and the Review Team is aware of some inconsistencies and anomalies. This matter was raised in a submission to the Public Consultation. The submission highlighted that the regulatory landscape dealing with consumers, and to a lesser extent SME credit, is very complex.

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[299] https://www.oireachtas.ie/en/bills/bill/2015/1/
[300] https://www.oireachtas.ie/en/bills/bill/2018/21/
[301] https://www.oireachtas.ie/en/bills/bill/2021/91/
[302] Credit unions are subject to an interest rate cap under S. 38 of the Credit Union Act 1997. Work on draft legislation to amend the current cap is underway. A provision has been included in the forthcoming Credit Union (Amendment) Bill 2022 which allows the Minister to set the cap by way of statutory instrument. The Minister intends to use this provision to amend the cap from 1% per month currently to 2% per month.
[303] https://www.oireachtas.ie/en/bills/bill/2022/27/
[304] https://www.oireachtas.ie/en/bills/bill/2022/75/
[305] https://www.kildarestreet.com/debates/?id=2022-10-18a.397#:~:text=The%20Central%20Bank%20%28Individual%20Accountability%20Framework%29%20Bill%202022,performing%20controlled%20functions%20and%20the%20duty%20of%20responsibility.

As noted in the chapter on Competition, these legislative complexities have the potential to act as a barrier to entry to the retail banking market. The Review Team recommends that the consumer protection legislative framework be rationalised and streamlined. This would provide potential new entrants with greater transparency and certainty. Simplification would also support the best interests of consumers, as they will be better enabled to confirm and understand their rights.

The forthcoming revised Consumer Credit Directive, which is expected to be adopted in 2023, will have to be transposed by the Department in the two years following its publication in the Official Journal. The Review Team recommends that:

The Review Team recommends that:

Recommendation 13-1

The Department of Finance should rationalise and simplify consumer protection legislation with the objective of eliminating overlapping provisions. This process should take account of the transposition of the forthcoming revision of the Consumer Credit Directive.

THE ROLE OF STATE BODIES IN CONSUMER PROTECTION

The Central Bank and the FSPO are the two bodies with primary responsibility for overseeing and ensuring consumer protection in financial services in Ireland. The CCPC also has functions relating to financial consumer protection under its general consumer protection powers[306] and in providing information on retail banking products.[307]

The Central Bank

In discharging its functions and exercising its powers as part of the European System of Central Banks, the primary objective of the Central Bank is to maintain price stability.[308] The Central Bank also has the function of monitoring the provision of financial services to consumers of those services to the extent that the Bank considers appropriate, for the purposes of protecting the public interest and the interests of consumers.[309]

In addition, the Central Bank is required under Central Bank Act 1942 to perform its functions and exercise its powers in a way that is consistent with the public interest and the interests of consumers. It also has the following objective: the proper and effective regulation of financial service providers and markets, while ensuring that the best interests of consumers of financial services are protected.

[306] https://www.ccpc.ie/business/enforcement/consumer-protection/consumer-protection/
[307] https://www.ccpc.ie/consumers/money/
[308] https://www.centralbank.ie/docs/default-source/tns/about---tns/governance-framework.pdf?sfvrsn=d930b71d_6
[309] S5A Central Bank Act 1942: https://revisedacts.lawreform.ie/eli/1942/act/22/section/5A/revised/en/html

All of the Central Bank's work under its integrated mandate across financial stability, prudential and conduct regulation has the ultimate goal of protecting consumers. The Central Bank protects consumers not only through conduct requirements and conduct supervision of firms, but by protecting the stability of the financial system and financial soundness of individual institutions to ensure that the system is resilient to shocks and can continue to serve the needs of the economy and consumers.

The Central Bank protects consumers not only through conduct requirements and conduct supervision of firms, but by protecting the stability of the financial system and financial soundness of individual institutions

The Central Bank has c. 480 staff working in Financial Conduct, of whom c. 140 are dedicated to consumer protection.[310] Consumer protection work includes direct engagement with certain firm types regarding authorisation, pre-approval of certain senior personnel, day-to-day firm-specific supervisory work, policy and research, and carrying out thematic reviews, such as the review published earlier this year on call waiting times on the customer support phone lines in the traditional banks.[311]

In executing its consumer protection mandate the Central Bank has issued a number of codes some of which have been updated via addenda, including the CP-Code,[312] the CCMA,[313] the Licenced Moneylenders Regulations[314] and the Code of Conduct on the Switching of Payment Accounts.[315]

The Consumer Protection Code

The current CP-Code was brought into effect by the Central Bank on 1 January 2012 and has been subject to 11 addenda. The CP-Code is a cornerstone of consumer protection in financial services in Ireland.[316] It applies to financial services providers authorised by Central Bank,[317] as well as those authorised in another EU or EEA Member State that provide services in Ireland.[318] The CP-Code aims to ensure a consistent level of protection for consumers, regardless of the type of regulated financial services provider they choose or the method of delivery.

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[310] https://www.oireachtas.ie/en/debates/question/2020-11-10/302/
[311] https://www.centralbank.ie/news/article/press-release-central-bank-requires-improvements-to-banks-support-phone-lines-18-February-2022#:~:text=The%20review%20found%20that%3A,the%20excess%20call%20wait%20times.
[312] https://www.centralbank.ie/regulation/consumer-protection/consumer-protection-codes-regulations#consumer-protection-code
[313] https://www.centralbank.ie/docs/default-source/regulation/consumer-protection/24-gns-4-2-7-2013-ccma.pdf?sfvrsn=45fd71d_6
[314] Central Bank (Supervision and Enforcement) Act 2013 (Section 48) (Licensed Moneylenders) Regulations 2020: https://www.irishstatutebook.ie/eli/2020/si/196/made/en/print
[315] https://www.centralbank.ie/docs/default-source/regulation/consumer-protection/45-gns-4-2-7-code-of-conduct-o.pdf?sfvrsn=1b59d71d_6
[316] https://www.centralbank.ie/news/article/central-bank-launches-consumer-protection-code-review-discussion-paper-3-october-2022#:~:text=The%20Discussion%20Paper%20presents%20a,financial%20literacy%3B%20and%20climate%20matters.
[317] There is a separate consumer protection code for moneylenders.
[318] https://www.centralbank.ie/docs/default-source/regulation/consumer-protection/other-codes-of-conduct/4-gns-4-2-7-cp-code-2012.pdf

As part of the wide-ranging requirements of the CP-Code the Central Bank requires regulated firms to assess the suitability of the product for the consumer, as well as the ability of the borrower to repay debt over the duration of the credit agreement. The Central Bank can take enforcement action against a firm by means of an Administrative Sanctions Procedures for contravening the CP-Code.[319]

As already highlighted in the chapter on Consumer Credit, the Central Bank is currently reviewing the CP-Code, and has issued a Discussion Paper with 27 questions that stakeholders, including the public, can respond to. The themes in the Discussion Paper are informed by the OECD's current review of the OECD Principles.

The review of the CP-Code is being conducted in phases. Phase One, which is the Discussion Paper, will run until March 2023. Phase Two will be a formal consultation that will be published in Q3 2023, while Phase Three will be a publication of the feedback and insights received. The information from the process will be analysed and incorporated into the final updated and enhanced consumer protection rules that the Central Bank plans to issue in 2024. The Review Team understands the new rules will be published as regulations.[320]

The Review Team welcomes the comprehensive approach the Central Bank is taking to the review of the CP-Code, noting its focus on 'Availability and Choice: Effective Market Functioning' and 'Firms Acting in Consumers' Best Interests', along with the wide-ranging and critically important eight discussion themes.[321] These align strongly with areas where issues were identified during the Review.

The Review Team also recommends that, in line with its statutory mandate, the Central Bank should continue to prioritise the interests of consumers in terms of enhancements to the regulatory framework (supported with evidence-based findings and research, where appropriate), and through the execution of its supervisory role. As part of the review of the CP-Code, the Central Bank should assess how its integrated mandate across financial stability, prudential and conduct regulation, can be further utilised to ensure the ultimate goal of protecting consumers.

In the course of this Report, a number of recommendations have been made with respect to the CP-Code. The Review Team considers that some of these recommendations need to be implemented in advance of the review of the CP-Code being completed, such as those regarding customer service standards and the need to extend the notice periods that banks must give if significantly amending the services of a branch, or if closing a branch.

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[319] http://revisedacts.lawreform.ie/eli/1942/act/22/revised/en/html#PARTIIIC
[320] Under section 48 of the central Bank (Supervision and Enforcement) Act 2013: https://www.irishstatutebook.ie/eli/2013/act/26/section/48/enacted/en/html
[321] Innovation & Disruption; Digitalisation; Unregulated Activities; Pricing Matters; Informing Effectively; Vulnerability; Financial Literacy and Climate Matters.

The Review Team understands and welcomes that the Central Bank will enhance the impact of the Consumer Advisory Group on consumer related issues by embedding it further in its strategy development and implementation and will continue to maintain a high quality and representative membership. In addition, the Central Bank has informed the Review Team that it will enhance its engagement and outreach activities to ensure that it obtains the views of consumers and their representatives to inform it in carrying out its mandate. This includes the Central Bank continuing to carry out consumer-based behavioural research, with data gathered through both surveys and fieldwork, to inform ongoing regulatory framework change. *The Review Team recommends that:*

Recommendation 13-2

In line with its statutory mandate, the Central Bank should continue to prioritise the interests of consumers in terms of enhancements to the regulatory framework (supported with evidence-based findings and research, as appropriate) and through the execution of its supervisory role. As part of the review of the Consumer Protection Code, the Central Bank should assess how its integrated mandate across financial stability, prudential and conduct regulation can be further utilised to ensure the ultimate goal of protecting consumers.

The Financial Services and Pensions Ombudsman (FSPO)

The function of the FSPO is to resolve complaints from consumers, including SME and other organisations, about the conduct of financial service providers and pension providers.[322] The FSPO commenced its activities in January 2018, following the merger of the Financial Services Ombudsman's Bureau and the Office of the Pensions Ombudsman. Where a customer has a complaint that has not been resolved through engagement with the provider, the FSPO offers an impartial, accessible and responsive complaint resolution process that sits outside the court process, commonly referred to as an Alternative Dispute Resolution (ADR) mechanism. The resolution of complaints through the ADR process can be achieved in a faster manner than alternative forums. In addition, the FSPO's services are provided at no cost to the complainant. The FSPO is not a regulatory body, but it works in cooperation with the Central Bank, and where appropriate, it notifies the Central Bank of breaches of regulation it encounters in the course of its work.

The FSPO has significant powers at its disposal to deal with customer complaints against financial services firms. It can direct such a firm to rectify the conduct which is the subject of the complaint, it can order the financial services firm to pay up to €500,000 in compensation to a complainant and it can publish the names of financial services firms which have had at least three complaints upheld, substantially upheld or partially upheld in a year. In 2021, the FSPO received a total of 4,658 complaints of which 2,660 related to the banking sector. In the

[322] https://www.fspo.ie/

banking sector, the top three reasons for complaints to the FSPO were customer service (28%), disputed transactions (20%) and maladministration (14%). In total, 5,010 complaints were closed by the FSPO in 2021.[323]

Issue with complaints made to the FSPO

The EU Single Market for cross-border services has transformed the financial services landscape in Ireland. An important element of competition and consumer choice highlighted throughout the Review is the role played by passporting institutions in delivering financial services in Ireland, and in driving innovation in the Irish market. In the course of the Review, the FSPO highlighted an issue with complaints made to the FSPO and where the complaint is governed by another jurisdiction's contract law due to the fact the provider is licenced in that other jurisdiction.

Consumers will be familiar with the phrase where financial institutions say they are authorised/licensed by, or registered with, a regulator in another EU jurisdiction and that they are regulated by the Central Bank for conduct of business rules. Conduct of business rules refer to relevant Central Bank codes and regulations, one of which is the CP-Code. Chapter 10 of the CP-Code deals with complaints resolution and requires firms to have written procedures for the proper handling of complaints.

The CP-Code further provides that regulated firms must inform complainants that they can refer the complaint to the 'relevant Ombudsman' if the handling of the compliant is not resolved within 40 business days of its receipt, or where the complainant is not satisfied with the proposed resolution. Out of court dispute resolution process is also addressed under various EU Directives dealing with consumer financial services, including the Payment Services Directive (Directive 2015/2366). This directive includes a requirement to ensure that adequate and effective out-of-court dispute resolution procedures for the settlement of consumer disputes are put in place, using existing bodies where appropriate and that Member States shall encourage those bodies to cooperate in order to also resolve cross-border disputes.

In the course of this Review, the issue of access to out-of-court dispute resolution services has come up in relation to institutions passporting into the Irish market.[324] While, the passporting of retail banking products and services into Ireland from other Member States has not been substantial in the past, it has grown and is likely to become a larger feature of the market in the future.

Where a contract is governed by law other than the law of Ireland, the FSPO has advised that it is not in a position to adjudicate on that complaint, as this would call for the FSPO to interpret

[323] https://www.fspo.ie/publications/annual-report.asp

[324] Passporting into Ireland is where a financial services firm uses the authorisation it has received in another EEA Member State to offer its products or services to consumers in Ireland. For more information see the Central Bank website: https://www.centralbank.ie/consumer-hub/explainers/what-is-passporting-and-what-do-i-need-to-know-about-it#:~:text=%E2%80%9CPassporting%20in%E2%80%9D%20is%20where%20a,products%20and%20services%20into%20Ireland.

and apply the laws of a foreign jurisdiction in the investigation and adjudication of that complaint. In those circumstances, with a view to providing a solution to the parties, it is the practice of the FSPO to seek the consent of the parties to the investigation and adjudication of the complaint, pursuant to the laws of Ireland. Whilst noting that such an agreement by the parties to facilitate the provision of the ADR service, will not in any manner alter the underlying governing law of the contract. In some instances, both parties have provided the required consent and the investigation can proceed in accordance with the laws of Ireland. If consent is not forthcoming, the FSPO will instead refer the complainant to the appropriate dispute resolution body in the relevant Member State, as the competent authority to adjudicate the complaint in relation to the contractual issue arising.

Historically, there was a relatively low level of complaints to the FSPO relating to financial services provided by institutions passporting into Ireland. However, in recent years the volume of complaints being referred on by the FSPO to out-of-court dispute resolution services in other Member States has increased. Several issues arise from this development, including the fact that the process may well be in the language of the relevant Member State, and the criteria for being able to refer a complaint can be different, e.g. in terms of the time elapsed since the issue of complaint happened.

The Review Team recommends the Department should address the issue of access to dispute resolution services for customers of passporting institutions at EU level. The Review Team also suggests in the interest of providing greater clarity to consumers, that the Central Bank amends the current CP-Code to require institutions servicing the retail banking market, as part of their pre-contractual information obligations, and again at the commencement of a complaint process, to clearly set out to their customers which ombudsman/ADR service will deal with complaints in the event the customer is not satisfied with the outcome of the provider's internal resolution process. Passporting institutions that transact with consumers in Ireland could explore whether there are measures within their own power that may address this problem.

The Review Team recommends that:

Recommendation 13-3

The Central Bank should, in advance of its completion of its Consumer Protection Code review, require each institution serving the retail banking market to set out clearly to its customers which ombudsman/Alternative Dispute Resolution service will deal with complaints, where the customer does not accept the decision of the provider's internal complaints process. This information should be provided to the consumer as part of the pre-contractual information obligations and at the commencement of a complaints process.

Recommendation 13-4

The Department of Finance should seek to ensure access to appropriate ombudsman/Alternative Dispute Resolution services for customers of passporting institutions is satisfactorily addressed at EU level.

CULTURE IN RETAIL BANKING

In addition to work carried out by the Department, the Central Bank and the FSPO regarding consumer protection, in response to the failings in retail banking identified in the Central Bank's July 2018 report entitled *Behaviour and Culture of the Irish Retail Banking*, the five traditional banks established the Irish Banking Culture Board (IBCB).

The IBCB's purpose is to work with its member banks to build trustworthiness in order to assist the industry regain public trust. The IBCB states that it is essential that culture and behavioural change are prioritised at the most senior levels in member banks from board level down and it works with members and other stakeholders with the aim of promoting an environment where ethical behaviour lies at the heart of banking; fair customer outcomes are achieved; staff are supported and reputation for competence is rediscovered.[325]

In the context of ethical behaviour and aligning with the forthcoming Individual Accountability Framework legislation the IBCB work programme includes a focus on the Senior Executive Accountability Regime.[326] In the context of improving customer outcomes it includes a survey on public trust in banking, initiatives to support financial inclusion[327] and a financial awareness programme. The latter incorporates modules focused on SMEs and farmers, customers in a vulnerable position and customers who have experienced bereavement.[328]

13.2.Financial inclusion

Financial consumer protection is interrelated with a number of policy agendas, most importantly, financial inclusion and financial literacy to support financial well-being.[329]

The OECD states that financial inclusion generally refers to the 'effective and quality access to and usage of – at a cost affordable to the customers and sustainable for the providers – financial services provided by formal institutions.[330] The World Bank suggests that financial inclusion means that consumers and SMEs have the opportunity to access useful and affordable financial products that meet their needs.[331] In the context of the change that is

[325] https://www.irishbankingcultureboard.ie/work-programme/
[326] https://www.irishbankingcultureboard.ie/work-programme/sear/
[327] This incorporates a Basic Bank account guide which is available in 10 different languages.
[328] https://www.irishbankingcultureboard.ie/
[329] 2022 Report to the Council on the implementation of the Recommendation: https://www.oecd.org/finance/high-level-principles-on-financial-consumer-protection.htm
[330] Ibid
[331] https://www.worldbank.org/en/topic/financialinclusion/overview

currently happening in the retail banking sector, the Review Team considers that this must mean that consumers and SMEs have equal access to appropriate and affordable products and services that they need, and that they are accessible in a timely manner.

The issue of access and inclusion is becoming increasingly important in the retail banking sector due in large part to the process of digital transformation that is currently under way. Whilst digitalisation is an important enabler of access, it can also act as a barrier to access. This is an issue that the Review Team identified in various elements of its work, for example due to the impact of branch closures, poor customer services standards as well as reduced access to cash.

The OECD Principles highlight the importance of Access and Inclusion in financial services. The Review Team considers that responsibility for ensuring consumers and SMEs can access and are included in the financial system lies, in the first instance, with the firms in the retail banking sector. The Review Team has made a number of recommendations to the retail banking sector in this regard, such as to preserving customers' and SMEs' access to cash services at December 2022 levels.

The issue of access and inclusion is becoming increasingly important in the retail banking sector

The Review Team is also making a number of recommendations to the State and State bodies that will improve financial inclusion, in particular:

- Various enhancements to the CP-Code, such as requiring firms to develop Customer Charters that better enable customers access the channels that firms now provide, whilst also delivering better service.
- Legislative measures to protect consumers' and SMEs' access to cash services, including the regulation of ATM providers to ensure people can access their own money at no additional cost.
- Amendments to the cost of accessing the CCR help reduce the cost of credit for consumers who borrow smaller amounts.
- A reduction in the CCR's €500 reporting threshold for credit agreements to help ensure that lenders have necessary information to assess customers' ability to pay, thereby protecting against excessive debt.

13.3.Financial and digital financial literacy

Regulatory consumer protections, placing obligations on firms to act in the best interest of customers and improving the culture of financial institutions are all extremely important and welcome. An equally important step is to try and ensure that consumers have the confidence and capacity to take informed decisions when using financial products and services.

In the course of this Report, the Review Team has outlined various and new retail banking products and services that the sector has developed that provide consumers and businesses with more and welcome choice. Many of these products and services are offered through digital channels, and in some cases, they are offered only through digital channels.

These developments and trends, which are likely to continue, can serve to include customers but may also exclude those consumers who do not have the ability or competency to engage with the new channels of delivery, such as online services. In addition, as previously noted, concerns have been raised that 'consumers have greater difficulty assessing and understanding pre-contractual information when using an online sales channel.'[332] This exposes consumers and businesses to increased risk, as they may find themselves buying products and services they do not need, or worse still, which could cause them detriment.

However, as part of a process to certify compliance with the existing OECD Principles, Ireland was deemed not to be fully compliant in respect of financial literacy, given the absence of a national strategy for financial literacy. Ireland is one of only four EU Member States that does not have such a strategy. Examples of countries that have successfully implemented national financial education strategies are the Netherlands, Portugal and the UK.

The revised draft OECD Principles, which are expected to be adopted shortly, state the following with respect to financial literacy:

> *Financial literacy and awareness should be promoted by all relevant stakeholders as part of a wider financial inclusion and/or literacy strategy. Appropriate mechanisms should be developed to help consumers develop the knowledge, skills, behaviours and attitudes to be aware and understand risks and opportunities and make informed choices, know where to go for assistance, and take effective action to support their own financial well-being and resilience.*

A submission[333] received as part of the Public Consultation highlighted some important facts regarding adult literacy in Ireland:

- The most recent CSO adult literacy survey,[334] albeit from 2013, showed one in six adults struggle with reading and understanding everyday text, one in four adults has

[332] https://home.kpmg/ie/en/home/insights/2021/07/consumer-credit-responsible-lending-consumer-reform.html
[333] From the National Adult Literacy Agency
[334] https://www.cso.ie/en/media/csoie/releasespublications/documents/education/2012/piaac2012.pdf

difficulty using maths in everyday life, whilst 42% of adults struggle with basic digital tasks.

- A more recent survey (2021) found that 'adult literacy rates in Ireland are almost 20% lower when compared with other Northern European countries,' whilst 'financial literacy rates among the 18-44 age group are 20% lower than the 45-64 age group.'[335]

In the course of its work, the Review Team identified various initiatives being undertaken by the State and others to address financial and digital literacy, in particular the Government's 10-year adult literacy strategy 'Adult Literacy for Life'[336], which is being led by the Department of Further and Higher Education, Research, Innovation and Science (DFHERIS). In addition to addressing all streams of adult literacy, the strategy includes a specific stream for financial literacy, which it defines as 'a combination of awareness, knowledge, skill, attitude and behaviour necessary to make sound financial decisions and ultimately achieve individual financial wellbeing,'[337] whilst digital literacy refers to the ability to use digital technologies.

The CCPC has a statutory function to promote personal financial education and provide personal finance information[338] which it does through its Money Hub on its website. The CCPC has developed a number of financial education initiatives including junior cycle and leaving certificate school programmes and a workplace programme. The CCPC is also involved in advocacy[339] and conducts research in this area.[340] The CCPC, in collaboration with the Department, is developing educational consumer resources to support consumers to harness the opportunities and benefits of fintech while highlighting the potential risks to consumers in accordance with the *Ireland for Finance Action Plan 2022.*[341]

In conjunction with the BPFI, the traditional banks have also been doing work in this area, including making a guide available on safeguarding your money, provision of expert training to assist customers who may be subject to financial abuse and the provision of information for vulnerable customers.[342] There are also a range of other financial literacy/education initiatives led by industry aimed at different sectors and age groups, such as school children. For example, the BPFI and SME representative bodies jointly promote a free online learning tool

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[335] https://moneysherpa.ie/financial-literacy-survey-data/
[336] https://www.gov.ie/en/publication/655a4-adult-literacy-for-life-a-10-year-literacy-strategy/
[337] Measuring Financial Literacy: Questionnaire and Guidance notes: https://www.oecd.org/finance/measuringfinancialliteracy.htm
[338] Under Section 10(3)(j) of the Competition and Consume Protection Act 2014, the CCPC has a statutory role in "providing information in relation to financial services, including information in relation to the costs to consumers, and the risks and benefits associated with the provision of those services, and promoting the development of financial education and capability."
[339]The CCPC has made submissions to the National Council for Curriculum and Assessmenthttps://www.ccpc.ie/business/business/research/submissions/ccpc-submission-to-the-national-council-for-curriculum-and-assessment-in-response-to-updating-aistear-the-early-childhood-curriculum-framework/2021-12-01-ccpc-submission-to-the-ncca-in-response-to-updating-aistear/ and the https://www.ccpc.ie/business/business/research/submissions/ccpc-submission-to-the-national-council-for-curriculum-and-assessment-consultation-on-the-draft-primary-curriculum-framework/
[340] CCPC (2018), Financial Capability and Well-being in Ireland in 2018: https://www.ccpc.ie/business/research/market-research/financial-capability-and-well-being-in-ireland/
[341] https://www.gov.ie/en/publication/8eac2-ireland-for-finance-action-plan-2022/
[342] https://bpfi.ie/insights/safeguarding-your-money/

for SMEs to improve their financial management skills, BOI launched a nationwide drive to improve the financial literacy of primary school children in 2019 and Irish Funds recently launched a pilot transition year financial literacy programme.[343]

Given the importance of financial literacy and also to ensure that Ireland achieves compliance with OECD Principles, there should be a coordinated and integrated approach that leverages all of the existing work on financial literacy, especially the financial literacy stream of the Government's Adult Literacy for Life Strategy, being led by DFHERIS. This would reduce the risk of there being different or even inconsistent standards and messages between financial literacy strategies for adults and children.

To deliver this, the Department should engage and participate fully in the financial literacy stream of the Adult Literacy for Life Strategy and work with all stakeholders to seek to ensure Ireland is compliant with the OECD Principles and the recommendation on financial and digital financial literacy. The Review Team also suggests that the DFHERIS should bring other relevant agencies and stakeholders into that process, particularly the CCPC in light of its statutory function in this area.

At a schools level, different industry bodies and firms are offering financial literacy programmes at both primary and second level. The Review Team welcomes this, but believe a more co-ordinated approach should be taken by the retail banking sector in order to broaden the reach of these programmes across the country and include digital financial literacy as well.

It is also important that the sector seeks to leverage the work of financial literacy stream of the Adult Literacy for Life and engage with the relevant State bodies in the expansion of such programmes.

As outlined in the chapter on SME Credit, DETE is already working on the issue of SME financial education, including financial literacy.

Whilst this work is underway, the Review Team considers that the retail banking sector can do more to assist its customers develop the skills they need to transition to the more digital future that the sector itself is moving towards. In its submission to the Public Consultation, the National Adult Literacy Agency recommended a number of actions for the retail banking sector, including:

- New measures to help customers work online. Services should be put in place to support customers, particularly vulnerable customers, to transition from offline to online financial services.

[343] https://www.irishfunds.ie/news-knowledge/news/irish-funds-pilot-transition-year-financial-literacy-programme/#:~:text=As%20part%20of%20our%202022,the%202022%2F2023%20academic%20year.

- Using a consistent approach to support and build customer confidence by using, amongst other things, standard language and terms (using plain language) and ways of displaying key information (e.g. APR).
- Training for staff on financial literacy and exclusion.
- Training and instruction materials for the public for using online banking services should be made available in plain language, through video and audio guides, and accessible for vulnerable groups.

The Review Team recommends that:

Recommendation 13-5

With regard to financial literacy and digital financial literacy:

- The Department of Finance should
  - Engage with and participate fully in the financial literacy stream of the Adult Literacy for Life Strategy; and
  - Seek to ensure that all stakeholders work together so that Ireland is compliant with the OECD High Level Principles on Financial Consumer Protection and the Recommendation on financial literacy.
- The retail banking sector should:
  - Build on the work already done by the BPFI and the Irish Banking Culture Board to ensure that its offerings are appropriate to cater for the needs of adults at risk of harm or abuse and empower them to safely manage their own money and financial affairs. The sector should become more responsive to the needs of these ‘vulnerable’ customers and harness the opportunities that advancements in technology provides to assist them.

14. Staffing in the retail banking sector

People, talent, skills and professional standards at all levels of an organisation are considered fundamental to the future success of retail banking in Ireland.

There are currently substantial job losses in retail banking arising from the departure of Ulster Bank Ireland and KBC. Banks also report challenges in retaining existing staff, even where there is no threat of job loss. There is strong competition for talent both within Ireland and notwithstanding recent developments internationally, Ireland's performance as a leading destination for the world's most successful international companies is resulting in staff leaving banks and the retail banking sector to pursue job opportunities in other sectors such as IT and professional services as well as with other international banks.

This trend is resulting in skills gaps and shortages in critical roles, especially the risk and IT functions, across all sectors of financial services, including in retail banking. In order to ensure that the retail banking sector continues to be led by people with the skills and experience needed to manage their businesses in a prudent and sustainable manner, with an embedded culture that delivers good outcomes for customers and staff, as well as the environment, it is critical that the sector can grow, develop and retain its staff and senior management This is particularly important in a sector that is experiencing extraordinary change, and where the need to re-skill and up-skill staff will become increasingly important in a more digitalised and more climate focussed banking sector.

14.1.Skillsets and training

As retail banking becomes more digitalised, it is important that personalisation of the customer experience does not weaken, as it is clear that it remains a core customer expectation. This requires management and staff to have strong and specialist skills.

Similarly, as Ireland progresses to a carbon neutral economy and works to achieve the commitments under its Climate Action Plan, management and staff in retail banking will need the skills and knowledge to develop appropriate products and to support their customers in the transition.

As business models change, and competition increases from new and niche providers, the success of retail banking will have a high dependency on the vision, quality and effectiveness of its leaders, who along with their boards and staff, decide and execute strategy and create an effective culture, the achievement of which must be supported by the latest thinking, knowledge and standards.

In its response to the Public Consultation, the Institute of Bankers (IOB) recommended the establishment of a Financial Services Skills Framework ('the Skills Framework'), the objectives

of which would be to build skills and competencies in the financial services industry that enables:

- Identification of current and emerging skills gaps.
- Retention and recruitment of talented individuals to the industry.
- Supports employers in strategic skills planning, including re-skilling and skills upgrading.
- Supports education and training providers in designing programmes to respond to the emerging skills needs of the industry: and that
- Assists industry professional bodies and Government in analysing skills gaps and initiatives appropriate to address them.

The IOB proposal would involve a cross-industry collaboration between education and professional bodies, employers and Government enterprise development and education agencies. The IOB proposed that the initiative would be lead and sponsored by the Department.

The Review Team sees the merit of the Skills Framework, and supports its objectives. To ensure the retail banking sector continues to serve as the means to help households and firms achieve their financial, economic and social needs, it is important that it is lead and staffed by people with the appropriate skillset, culture and vision to achieve good outcomes in a more complex and dynamic industry. The retail banking sector needs to be able to recruit and retain staff because the sector is seen as a good and rewarding place to work, in terms of the opportunities that it offers and the benefits that people get for achieving good outcomes.

In addition, elsewhere in this Report, the Review Team has already outlined how customer experience can be improved where staff have the ability and skillet to develop new and innovative products, deal with customers more effectively in branches and in call centres, as well as identify and help customers who are at risk of financial exclusion or dependency due to ongoing digitalisation. For example, in the context of SME credit, feedback received as part of the Dialogue and Public Consultation suggests that a greater focus is required on maintaining and developing strong lending skills. The uncertainty that currently prevails in the external environment, and which is likely to persist, also requires a greater degree of expert judgement to be applied to all credit exposures, including requests for new debt.

It is incumbent on the retail banking sector to ensure its own leaders and staff are skilled to achieve good customer, climate and other corporate objectives, including protecting and maintaining the financial resilience of the sector

However, the Review Team considers that the Skills Framework needs to be developed by the retail banking sector, for the retail banking sector and should be led by the retail banking sector. It is incumbent on the retail banking sector to ensure its own leaders and staff are

skilled to achieve good customer, climate and other corporate objectives, including protecting and maintaining the financial resilience of the sector itself. The Department will support the development of the Skills Framework by contributing to its work, as appropriate.

The Review Team recommends that:

Recommendation 14-1

The retail banking sector should work with the Institute of Banking to consider the development of a Financial Services Skills Framework to build the skills and competencies needed for the future and sustainable development of the retail banking sector.

14.2.Remuneration

The traditional banks have reported that existing restrictions on staff pay and incentives are posing difficulties for them as they seek to recruit and retain talent. These restrictions, which were introduced by way of contract with the banks recapitalised by the State following the GFC, include the following:

- A cap of €500,000 on any individual's annual aggregate remuneration, (the 'pay cap') excluding the employer's standard pension contribution.
- A ban on variable pay/bonuses ('variable pay').
- No new or additional fringe benefits, such as healthcare.

In addition to these restrictions, the Finance Act 2011 introduced a 'super tax,' meaning that if variable pay were to be paid, a marginal rate of tax of 89% would be applied to amounts above €20,000.

When introduced, the contractual restrictions had no expiry date or sunset clause, and were only applied to the remaining banks that were recapitalised by the State following the GFC, namely BOI, AIB (including EBS) and PTSB. Since September 2022, the State no longer holds a shareholding in BOI and has significantly reduced its shareholdings in AIB and PTSB.

SUBSEQUENT REGULATORY AND LEGISLATIVE DEVELOPMENTS

After the GFC, and subsequent to the Irish Government introducing the restrictions, the European Commission proposed changes to align remuneration policy with sound risk management and requires institutions to have clear remuneration policies that differentiate between fixed and variable remuneration. These changes were agreed in Directive 2013/36/EU[344] (known as CRDIV) and transposed into Irish law in Statutory Instrument 158 of 2014.[345] These requirements do not include a pay cap but include binding limits on variable pay as a percentage of fixed pay i.e. variable pay shall not exceed 200%; restrictions on what

[344] https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex%3A32013L0036
[345] https://www.irishstatutebook.ie/eli/2014/si/158/made/en/print

type of instruments may be used to make up variable pay i.e. 50% has to be paid in equity or similar instruments; vesting periods for a portion (40%) of the variable pay; and malus and clawback provisions were introduced.

More recent amendments to sound remuneration policies were made in Directive EU 2019/878 [346] (CRDV), including a requirement that remuneration policies should be gender neutral. These changes were transposed into Irish law by Statutory Instrument 710 of 2020.[347]

In 2021 the EBA issued updated guidelines on sound remunerations policies that provide more detailed guidance on the remuneration principles set out in the legally binding directives CRDIV and CRDV. Taken together, the Directives and the EBA guidelines aim to ensure that the failings in the structures and focus of remuneration packages that contributed to the GFC could not arise again.

These guidelines specifically state the aim as ensuring 'remuneration policies are consistent with and promote sound and effective risk management, do not provide incentives for risk taking, and are aligned with the long-term interests of institutions across the EU.'[348]

Separately, in Ireland, legislation[349] is currently being progressed which will see the introduction of an Individual Accountability Framework incorporating a Senior Executive and Accountability Regime (SEAR).

THE IMPACT OF THE RESTRICTIONS

The legacy restrictions on variable pay impact the c.20,000 staff working in BOI, AIB, and PTSB, irrespective of grade or pay level and therefore apply to the lowest paid staff in the banks as well as those that are paid more. In practice, the €500,000 pay cap applies to the few within the banks that hold the most senior management positions, such as the CEO and other senior executives.

The restrictions do not impact staff who work in the wider retail banking sector, such as other banks, payment providers or non-banks, even though those staff may be performing the same job, with the same responsibility and within the same regulatory frameworks, as the staff that are in BOI, AIB and PTSB.

Given the uneven application of the restrictions, the banks[350] report that they are losing well-qualified and good staff to firms that offer more competitive and market-facing remuneration

[346] https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32019L0878
[347] https://www.irishstatutebook.ie/eli/2020/si/710/made/en/print
[348] https://www.eba.europa.eu/sites/default/documents/files/document_library/Publications/Guidelines/2021/1016720/Draft%20Final%20report%20on%20GL%20on%20remuneration%20policies%20under%20CRD.pdf
[349] Central Bank (Individual Accountability Framework) Bill 2022: https://www.oireachtas.ie/en/bills/bill/2022/75/
[350] BPFI – response to the Public Consultation

packages. The three banks are not just competing for talent with firms in the wider banking sector, but also with technology companies, the fintech sector and, indeed, across all sectors of the economy.

It is reported that competition is most intense for staff that are qualified and experienced in the IT, cyber security, risk, compliance and legal functions. It has also been widely reported that many senior executives of the three banks have left to pursue new opportunities in other banks or firms, including competitors, where the remuneration is determined by the market.

The three banks are quoted on the Irish and London Stock Exchanges and international investors would prefer to see normalised remuneration arrangements in place as it removes a specific risk they have to consider when making investment decisions.

PUBLIC CONSULTATION FEEDBACK

The Public Consultation asked for feedback on whether the Government should retain, amend or remove the Irish restrictions that currently only apply to the three banks.

Feedback from employee representative groups, amongst others, supported the removal of the restriction on variable pay up to €20,000 per annum and standard workplace benefits. These bodies favoured the retention of the pay cap and the 'super tax' of 89% because they considered them a proportionate and necessary condition for taxpayer support for the banks and have served the public interest well.

The BPFI made the case that a "normalisation of pay and employment conditions at Ireland's retail banks – to allow the banks compete for people on a level playing field with other corporates – is needed if they are to attract the skills and employees that are necessary for their future and for the provision of services expected by Irish consumers." BOI referenced research[351] that highlighted that Ireland is the only country that applies pay prohibitions to all employees in specific banks within a market.

The IMF in its 2022 Financial System Stability Assessment, carried out as part of the five yearly Financial System Assessment Programme (FSAP), stated: "Policies introduced at the time of the Government bailout significantly handicap critical talent acquisition and retention, especially for key risk management and compliance positions, and should be ended. The measures include caps on executive pay, a penal tax on all employee bonuses (89%). These policies also result in an uneven playing field for the retail banks, which are in a catch-up game with more nimble and digitally advanced non-banks."[352]

[351] BOI – response to the Public Consultation
[352] https://www.imf.org/en/Publications/CR/Issues/2022/07/07/Ireland-Financial-System-Stability-Assessment-520469

14.3.A way forward

It is important that all providers within the retail banking sector are able to compete effectively. Given the changing retail banking landscape, where technological innovation and increasing digitalisation are driving changes to banks' business models, the skills composition within banks needs to evolve to enable the banks operate and compete effectively.

As the restrictions only apply to the three retail banks, who have most of the Irish population and businesses as their customers, there is potential for these customers to lose out if banks cannot recruit and retain staff with the skillsets to develop new and innovative products that create better choice, and which meet customer's needs and expectations.

At present, the three traditional Irish retail banks are at a competitive disadvantage to their domestic and international competitors, which in the long run, could undermine the sustainability of the only remaining retail banks with branch networks in the Irish market.

Furthermore, while some see the restrictions as proportionate and necessary given the conduct of the banks in the lead up to the GFC and the resulting taxpayer support, it raises the question of why the staff of the three remaining banks are bearing the burden of these restrictions. It is also pertinent that in the case of BOI, the State has received back more in cash terms than the support it gave to that bank.

Indeed, in light of this, an exercise is underway in the Department to review the Credit Institutions Financial Support Scheme and Eligible Liabilities Guarantee Schemes to provide for revocation of the obsolete and duplicative reporting obligations therein by way of Statutory Instrument, and to remove related contractual obligations. This work, which will apply to all three banks, is expected to be completed during 2023.

Based on the points above and the length of time that has now passed since the GFC, the Review Team is of the view that it is appropriate to consider amending or removing the remuneration restrictions. A further factor that needs to be considered is that the State holds no shares in BOI since September of this year.

However, the level of support provided by the State and its citizens to the Irish banking system was significant and resulted in substantial hardship for many. Therefore, the concerns that some have in removing the restrictions in full are understandable, particularly where the State remains a majority shareholder.

Notwithstanding this point, given the operational challenges and the need to attract and retain staff that will help the traditional banks provide effective service and products to their customers, the Review Team recommends that the remuneration restrictions for all three traditional banks should be amended to allow;

- variable pay per employee of up to €20,000 per annum, consistent with the limit set by the 89% super-tax, which will remain in place; and
- the provision of standard non-pay benefits for all employees.

Recognising that the State is no longer a shareholder in BOI, the Review Team also recommends that the maximum pay cap of €500,000 for an individual is removed. With regard to AIB and PTSB, the pay cap should be removed in the future when the State's shareholding in them is at an appropriate level.

The Review Team recommends that:

Recommendation 14-2

The pay restrictions should be amended by:

- Permitting variable pay per employee of up to €20,000 per annum;
- Allowing the provision of standard non-pay benefits for all employees; and
- Solely for Bank of Ireland, removing the maximum pay cap of €500,000 for an individual.

15. Future Outlook for the Sector

The Review Team considers that many of the existing trends and developments and issues that were identified in the course of the Review Team's work will continue into the future. Much of what is happening is positive, though the departures of KBC and Ulster Bank are certainly regrettable. In some cases however, it is clear that intervention is needed to better manage the impact of the change that is happening, in particular to ensure consumers and SMEs are protected, remain included and can continue to access the retail banking system. Timely actions are needed to address certain areas of concern. These actions are set out as recommendations throughout the Report, and, in the main, are addressed to the Department, the CCPC, the Central Bank and, of equal importance, to the retail banking sector.

Technology has played a major role in the evolution of financial services delivery, as well as bringing some innovative product features to the market. The Review Team expects this to continue. Legislative changes at EU level have expanded the range of providers of retail banking products and services, thereby providing greater competition and more product choice. The evolution of digitally enabled products and services will continue, as well as further innovation, however it is likely that in a drive to strengthen financial performance and build scale, consolidation amongst newer providers will occur during the coming 5-10 years. BigTech may also engage further in the sector, either as a regulated provider or in partnership with regulated firms. In addition, the credit unions and An Post are expected to continue to provide a range of products and services, mainly, but not exclusively through their extensive local presence throughout the country.

Conditions in the external environment will be less favourable than they have been in the past five years, as a phase of significant global uncertainty will continue to play out. Inflation, geopolitical tensions and the war in Ukraine are key concerns. Rising interest rates will impact many borrowers, leading to reductions in lenders' overall credit quality profiles, with consequent increases in lenders' loan loss provisions and actual losses. In recent years lenders have placed a greater focus on fixed rate mortgages, which will reduce the impact of rising interest rates on many mortgage holders in the coming years. The traditional banks' have 37% of their current mortgages fixed for three years or longer, with a further 14% fixed for between one and three years.[353] A rising interest rate environment is good for deposit-holders, albeit this is counter-balanced by the impact of inflation. Cyber risk will remain a key threat to individuals, companies, financial service providers and the financial system more generally.

The traditional banks, who are the principal providers of retail banking services, are entering the next 5-10 years with strong fundamentals. So too is Ireland, leading the Review Team to

[353] As of 30 June 2022.

consider that the outlook for the sector is largely positive. For example, normalisation of interest rates, while negative for many borrowers, is beneficial for the traditional banks and better aligns to how they generate sustainable levels of net interest income. In addition, demand for housing will drive further growth in demand for mortgages.

The traditional banks' profitability will continue to recover due to the impact of rising interest rates, acquisitions and the improvements they have made to their business models and cost bases. A key area of focus will be on customers impacted by a less benign economic environment, how loan portfolios perform over the cycle and the potential consequences for profitability.

Given enhancements to risk management frameworks, albeit that further work is necessary, better underwriting standards and much improved capital and funding profiles, the Review Team expects the banks to trade successfully through the cycle. To diversify their income streams away from interest income the traditional banks may increase their focus on fee income and charges. Any changes to fees and charges fall within the remit of the Central Bank. Improved profitability, strong levels of capital and liquidity, and continued intensive supervision by the SSM and the Central Bank, should ensure the retail banking sector remains resilient and stable.

In line with Government policy of returning the banking sector to private ownership, there will be further sell down of the State's shareholdings in AIB and PTSB.

While the traditional banks are expected to retain a dominant and pivotal role in the market, the Review Team also expects competition from newer providers. With the potential for a larger number of newer competitors, due to lower costs of entry (e.g. apps based providers) and ease of access (e.g. via passporting), competition will become more fragmented.

The Review Team believes the retail banking market is unlikely to become more concentrated in the coming 5-10 years, and expect digital banks and non-banks will take market share as their product bases grow and they become more embedded in the Irish market.

Given the Review Team's expectation that the market will remain concentrated, it could trend towards being less competitive. Accordingly, the Review Team recommends that the Department, in conjunction with the Central Bank and the CCPC, should closely monitor competition levels and take appropriate and timely action if issues are identified.

Firms across the sector will increasingly offer products and services using digital channels, and the opportunities for consumers and SMEs to access in-person retail banking services will continue to reduce. This development is already a cause for concern to many consumers and SMEs. It is envisaged that for certain customers/certain situations in-person engagement (including via telephone and other remote channels), will always be necessary. Products and services should be developed with this in mind. Changes required include a need for material

improvements in how technology is deployed so that it better meets customers' expectations, as well as the need to address challenges resulting from insufficient levels of digital and financial literacy amongst large sections of the user community. The Review Team calls on the retail banking sector to take note of the current issues and address them as a matter of priority, as well as embedding more customer centric features into future developments in product and service delivery. The sector is also called upon to actively engage to support customers to increase their digital and financial literacy levels.

The Review Team expects access to consumer credit will remain widely available, with the potential for it to become easier if more retailers offer consumers the ability to obtain credit, including for lower value goods. This may give rise to an increase in unsustainable debt amongst certain borrowers, particularly in view of the less benign economic environment. As in the previous 10 years, the Review Team expects the SME sector will remain cautious when it comes to borrowing. To ensure SMEs have continued and sufficient access to credit, the Department should continue to monitor the market via the Credit Demand Survey and engagement with stakeholders, including representative bodies, the ESRI and the banking sector. The Department should also work with other Government departments and the SBCI to ensure that any market failures are identified and addressed appropriately.

The traditional banks have committed to maintaining their current branch networks for an undefined period of time. PTSB starts the period with a larger network due to the acquisition of 25 branches from Ulster Bank. The fact no new entrant has come in to take over the operations of KBC and Ulster Bank, and the trend of departures by foreign owned traditional banks since the GFC, suggests policy in the retail banking sector should not presuppose the entry of a new large retail bank with or without a large branch network, even if such an event would be welcome.

Some of the existing/new providers will provide stronger competition to the traditional banks by expanding their product range as they develop their brands and seek to build scale e.g. digital banks moving from personal payment accounts to deposit taking, term lending and perhaps into mortgage lending, as well as extending their product offering to SMEs. The sector is also expected to provide strong support to consumers and SMEs to make investments to support achieving our climate targets and our transition to carbon neutral by 2050.

Certain non-banks are likely to continue to offer lower risk products (e.g. asset backed lending) and focus on lower risk borrowers (e.g. mortgage switchers and mortgage borrowers with higher incomes and lower LTV/LTI metrics).

Open banking, IBAN portability, if feasible, and efficient switching processes should all reduce frictions in the market, making it more attractive for potential new entrants. Following a slow start, it is expected that open banking will embed within the market and facilitate greater consumer choice, and act as a further means for new and diverse providers to gain market

share. The Review Team expects that lessons from the current mass migration will inform improvements in the switching process. Developments in these areas will be monitored by the Department. The Department will also engage at EU level regarding the feasibility of IBAN portability.

New entrants to the payments and credit markets could include BigTech, as these firms could use their brand/scale to provide new services/products to Irish consumers and SMEs. Given our market size and the need for regulatory approval, should such firms decide to expand their retail banking activities, it is likely they would enter the Irish market as part of a wider pan-European strategy, or by partnering with a regulated entity. To date market commentary suggests that BigTech firms are cautious regarding the extent to which they engage in regulated financial services.

The traditional banks will continue to invest in technology so that they can better compete with digitally-based competitors. They will also continue to make investments to upgrade their core IT systems.

The ECB is currently considering how a digital euro could be designed and distributed, as well as the impact it could have on the market. This work started in October 2021 and is expected to conclude in October 2023. While we await the findings, it is clear that a digital euro, if launched, will likely have a material impact on retail banking and payments.

In the absence of changes to the remuneration restrictions, due to the availability of more competitive packages from competitors, the traditional banks will find it increasingly difficult to attract and retain staff across all disciplines, especially individuals with core competencies in areas such as IT, cyber security, data analytics, risk and compliance. Competition for resources will come from a range of firms, including a growing cohort of Irish based international banks that serve the European market from their Irish headquarters, non-banks trading in the market, and Irish based firms that operate outside the retail banking sector who require staff with similar skills.

Furthermore, the senior leadership of the traditional banks is likely to continue to churn at relatively short intervals, with adverse consequences for the development and delivery of long-term strategies and embedding effective customer-centric cultures.

Traditional banks are likely to develop further their outsourcing relationship with An Post for the provision of counter services, particularly cash. The capacity to deliver current and potential increases in business to the requisite standards, will be important for An Post. The Review Team believes banks will also seek out additional outsourcing opportunities to enable them to streamline their internal operations further and to better focus on core banking activities. Outsourcing risk will increase as a result.

Where appropriate, the traditional banks are also expected to seek to collaborate collectively and with other firms so that costs are shared, within the bounds of completion law.

Customer behavioural changes are likely to become more relevant, particularly as younger consumers and SME owners and managers comprise a larger segment of the market. Commentary suggests that younger customers have a propensity to be more transactional and are more likely to avail of and purchase the product that is the cheapest, and which can be acquired with the least friction and most efficiently.

It is possible that the desire to develop a relationship with the service provider may become less relevant, or not important at all, to the consumer or SME that is acquiring the service. Anecdotal evidence also suggests that for certain products and in certain circumstances all customers value a relationship-based approach, and therefore certain providers may continue to derive competitive advantage on the basis of a relationship-focused delivery strategy, which may, or may not, include in-person engagement.

Mortgage pricing and the price of SME credit will remain above the EU average, albeit the differential is likely to narrow. The traditional banks pricing should benefit from cost efficiencies, while competition from non-bank mortgage providers should ensure consumers have reasonable choice of provider and a good, competitively priced product range.

The RWAs of the traditional banks will not reduce significantly, however the differential between Irish and EU peers will narrow as average RWAs across the EU increase due to the implementation of the Basel III output floors.

Notwithstanding the material number of customers who have a preference for cash, consumers', SMEs' and retailers' use of cash will continue to decline, however not to the point where there is no longer a need for cash. Given the fact that cash handling is a relatively high cost activity, the economics of maintaining the cash infrastructure become more challenging as cash volumes continue to fall.

An unstructured or unplanned reduction in access to cash would impact all those who prefer cash, and it would also most likely have disproportionate impacts on rural communities, where transaction volumes will invariably be lower. As the costs of cash services are ultimately passed on to consumers and SMEs, reduced levels of acceptance of cash could occur as retailers and other firms seek to better manage their costs. However, the legislative actions arising from this Review will help ensure consumers and SMEs have continued access to cash, and there will be a greater focus on the resilience of the cash system.

The retail banking sector will remain highly regulated, and we expect the regulatory environment will continue to evolve. In line with developments whereby the provision of credit to consumers has been extended to bring in newer forms of finance into the regulatory perimeter, we expect that in due course all SME lenders be regulated. For those firms that are

regulated, regulatory requirements vary depending on the entity type, and so firms providing similar, or the same, products and services, will continue to be subject to different regulatory regimes.

In the absence of actions to deliver material improvements, the current challenges regarding digital literacy levels will become greater, as changes in technology continue to outpace society's capacity to keep pace with developments. Low levels of financial literacy will further impede certain customers' ability to engage effectively via digital channels. In this regard, the Department should engage and participate fully in the financial literacy stream of the Adult Literacy for Life Strategy and work with all stakeholders to seek to ensure Ireland is compliant with the OECD Principles and the recommendation on financial and digital financial literacy. Greater digital and financial literacy, coupled with improvements in ease of use of digital products and services, should support further migration to digital channels.

The credit union sector, with its nationwide presence, strong roots in every community and sizeable capital reserves and liquidity has the potential to develop into a community bank, offering a standardised range of retail banking products, at scale, to all members. The Review Team believes the sector's current growth ambitions, as evidenced by developments in the provision of current accounts, SME credit and mortgages, could be enhanced and evolve into a universal product offering.

The Review Team expects that over the course of the coming 5-10 years, consumer protections will improve due to further legislative changes, including the implementation of the Individual Accountability Framework, enhancements to the Central Bank's consumer protection framework (following the completion of the CP-Code review process) and very importantly, resulting from actions initiated directly by the retail banking sector - including in response to issues raised in this Review.

The Review Team believes the sector is well placed as it enters the next 10 year period, and as it continues to evolve it has the capacity and capability to do so in a manner that enhances its offering and how it engages with its customers. The recommendations within the Report seek to address areas of concern and to better ensure Ireland will be served by a retail banking sector with a customer-centric culture, which puts customers at the heart of everything it does and operates to high service standards. This includes offering good choice, fair treatment and competitively priced products and services. The sector will also support continued access to cash and ensure vulnerable customers are a key priority.

Glossary

Retail banking products and services – Defined as current/payment and saving accounts, mortgages, SME and consumer credit.

Traditional bank – Defined as a bank operating in Ireland, who offer retail banking products and services, and which have a physical branch presence. Currently, there are five traditional banks operating in Ireland (i.e. AIB, Bank of Ireland, Permanent TSB, KBC, Ulster Bank), however this will reduce to three following the departures by KBC and Ulster Bank.

Digital bank – Defined as a bank operating in Ireland that offers retail banking products and services online and which does not have a physical branch presence (such as Bunq, N26 and Revolut).

Non-banks – Defined as any provider of retail banking products and services to consumers and SMEs who are not a bank or digital bank. Non-banks include, but are not limited to, credit unions, An Post, retail credit firms, high cost credit providers and unregulated firms lending to SMEs.

Retail banking sector – Defined as banks, digital banks and non-banks who provide retail banking products and services.

Fintech – Defined as the use of technology to deliver retail banking products and services to consumers and SMEs.

Providers – Defined as any firm offering retail banking products and services to consumers and SMEs.

Retail credit firms – A retail credit firm is a firm that provides credit to individuals (natural persons).

Access to cash – Defined as public access to services to withdraw and deposit cash (facilitated by banks and other stakeholders).

Acceptance of cash – Defined as ensuring cash is accepted as a means of payment everywhere (facilitated by financial institutions, retailers and others)

Basic bank account – A current account that is free of charge for everyday banking for at least the first year as long as lodgements made to the account each year are below the earnings of a full-time worker on the national minimum wage.

Current account – A payment account that can be used to pay bills by direct debit or standing order, receive automated payments, transfer money, pay for things with a debit card or digital wallet and withdraw money for ATMs.

The Review – The work of the Review Team, which is used (for example) in the following context: ‘within scope of the Review;’ ‘feedback received by the Department during the Review;’ ‘in the course of the Review.’

The Review Team – the dedicated team in the Department of Finance that conducted the Review of the retail banking sector.

The Report – The Report requested by the Minister for Finance on the retail banking sector.

Providers of retail banking products and services – all firms in the retail banking sector that provide retail banking products and services to consumers and SMEs.

Appendices

APPENDIX 1 – LIST OF ABBREVIATIONS

ACM	Netherlands Authority for Consumers and Markets
ADR	Alternative Dispute Resolution
AI	Artificial Intelligence
AIB	Allied Irish bank
AISP	Account Information Service Provider
AML	Anti-money Laundering
API	Application Programming Interface
APR	Annual Percentage Rate
APRA	Australian Prudential Regulation Authority
ATM	Automatic Teller Machine
BER	Building Energy Rating
BEUC	The European Consumer Organisation
BIS	Bank for International Settlement
BNPL	Buy Now Pay Later
BOI	Bank of Ireland
BPFI	Banking and Payments Federation Ireland
BTL	Buy to Let
CCD	Consumer Credit Directive
CCMA	Code of Conduct on Mortgage Arrears
CCPC	Competition and Consumer Protection Commission
CCR	Central Credit Register
CDS	Credit Demand Survey
CEO	Chief Executive Officer
CET 1	Common Equity Tier 1
CIT	Cash in Transit
CP-Code	Consumer Protection Code

CRD	Capital Requirements Directive
CRDIV	Capital Requirements Directive IV
CRDV	Capital Requirements Directive V
CRO	Credit Review Office
CRR	Capital Requirements Regulation
CRU	Commission for Regulation of Utilities
CSF	Credit Servicing Firm
CSO	Central Statistics Office
DAFM	Department of Agriculture, Food and the Marine
DECC	Department of the Environment, Climate and Communications
DETE	Department of Enterprise, Trade and Employment
DFHERIS	Department of Further and Higher Education, Research, Innovation and Science
DGS	Deposit Guarantee Scheme
DIRT	Deposit Interest Retention Tax
DLT	Distributed Ledger Technology
DSTI	Debt Service to Income
EBA	European Banking Authority
ECB	European Central Bank
EEA	European Economic Area
EIB	European Investment Bank
ESG	Environmental, social, and governance
ESRI	Economic and Social Research Institute
EURIBOR	Euro Interbank Offered Rate
FCA	Financial Conduct Authority UK
FHS	First Home Scheme
FSAP	Financial Sector Assessment Program
FSPO	Financial Services and Pensions Ombudsman
FTB	First Time Buyer

GDP	Gross Domestic Product
GFC	Global Financial Crisis
GNI	Gross National Income
GVA	Gross Value Added
HCCP	High cost credit providers
HHI	Herfindahl-Hirschman Index
HP	Hire Purchase
IAD	Independent ATM Deployer
IAF	Individual Accountability Framework
IBAN	International Bank Account Number
IBCB	Irish Banking Culture Board
IBRC	Irish Bank Resolution Corporation
IMF	International Monetary Fund
INBS	Irish Nationwide Building Society
IOB	Institute of Banking
IT	Information Technology
KYC	Know Your Customer
LCR	Liquidity Coverage Ratio
LDR	Loan to Deposit Ratio
LEO	Local Enterprise Offices
LSRA	Legal Services Regulatory Authority
LTI	Loan to Income
LTMA	Long-term mortgage arrears
LTV	Loan to Value
MABS	Money Advice & Budgeting Service
MBS	Mortgage-Backed Securities
MFI	Monetary Financial Institutions
NFC	Near field communication
NPL	Non-Performing Loan

NPP	National Payments Plan
NSFR	Net Stable Funding Ratio
NTMA	National Treasury Management Agency
NZRB	Reserve Bank of New Zealand
OECD	Organisation for Economic Co-operation and Development
PAD	Payment Accounts Directive
PCP	Personal Contract Plan
PDH	Principal Dwelling House
PI/EMI	Payment Institution/Electronic Money Institution
PIN	Personal Identification Number
PISP	Payment Initiation Service Provider
PMC	Personal Micro Credit
PRA	Prudential Regulation Authority UK
PSD	Payment Services Directive
PTSB	Permanent TSB
RCF	Revolving Credit Facility
RFSP	Regulated Financial Service Providers
ROE	Return on Equity
SBCI	Strategic Banking Corporation of Ireland
SEAR	Senior Executive Accountability Regime
SEPA	Single Euro Payments Area
SME	Small Medium Enterprise
SREP	Supervisory Review and Evaluation Process
SSB	Second and Subsequent Buyer
SSM	Single Supervisory Mechanism
ToR	Terms of Reference
TPP	Third Party Provider

APPENDIX 2 –RECOMMENDATIONS BY THEME

Thematic no.	The Retail Banking Review Team recommends that:	Chapter no.
Access to Cash		
1.	The Department of Finance should develop Access to Cash legislation, and prepare heads of a bill in 2023 to: • Require banks that meet objective criteria to provide reasonable access to cash. "Reasonable access to cash" criteria will be defined in consultation with the Central Bank and other stakeholders and the initial objective of the legislation will be to preserve access at December 2022 levels; and • Provide that the criteria can be changed by the Minister for Finance by regulation, based on research and advice from the Central Bank. This will allow for the further evolution of the cash infrastructure to be managed in a fair, orderly, transparent and equitable manner for all stakeholders.	***7.1***
2.	Pending development of this Access to Cash legislation, the banks should seek to preserve consumers' and business' access to cash services at December 2022 levels.	***7.2***
3.	The Department of Finance should prepare heads of a bill in 2023 to require ATM operators to be authorised and supervised by the Central Bank.	***7.3***
4.	The Department of Finance should prepare heads of a bill in 2023 to provide the Central Bank with responsibility and powers to protect the resilience of the cash system including the authorisation and supervision of cash-in-transit firms in respect of their cash handling activities and related financial services.	***7.4***
5.	The Department of Finance should lead on the preparation of a new National Payments Strategy to be ready in 2024. The strategy should set out a roadmap for the future evolution of the entire payments system, taking account of developments in digital payments, the use of cheques and other issues, and guide how future changes should be made to the legislative Access to Cash criteria. The Strategy should be informed by, and aligned with, the retail payment strategies of both the EU Commission and the	***7.5***

Eurosystem. The Strategy should also consider and consult on whether:

- To legislate pre-emptively to give the Minister for Finance the power to require certain classes of firms, sectors or sub-sectors to accept or facilitate (to an appropriate level) the acceptance of cash; and
- If it should be Government policy that public bodies should accept or facilitate the acceptance of cash for the payment of goods, services, taxes, levies, fees or charges.

Consumer Protection, financial inclusion and literacy

6.	In line with its statutory mandate, the Central Bank should continue to prioritise the interests of consumers in terms of enhancements to the regulatory framework (supported with evidence-based findings and research, as appropriate) and through the execution of its supervisory role. As part of the review of the Consumer Protection Code, the Central Bank should assess how its integrated mandate across financial stability, prudential and conduct regulation can be further utilised to ensure the ultimate goal of protecting consumers.	***13.2***
7.	The Central Bank should, in its review of the Consumer Protection Code and, unless otherwise stated, in advance of the completion of its Consumer Protection Code review: • Require banks to submit robust, board approved, assessments to the Central Bank when they are planning to significantly alter the services provided through branches or when planning to close a branch. These assessments should examine the impact on customers, the suitability of alternative service provision arrangements, and the plans for migrating customers to them, especially at-risk customers. Such assessments, excluding commercially sensitive information, should be published by the relevant bank. • Require ex-post assessments by banks, to include a survey of impacted customers, nine to 15 months after the change or closure and a requirement to rectify material issues. • Increase the minimum notice period required to four months (currently one) for significant banking service changes (e.g.	***8.2***

going cashless) and to six months (currently two) for branch closures and credit institutions leaving the market.

- Require, in the revised Consumer Protection Code, all providers of retail banking products and services to set out and publish customer charters, incorporating service standards. In advance of changes that may ultimately be made to the Consumer Protection Code, the Review Team recommends that all providers of retail banking products and services implement this recommendation on a voluntary basis.

8.	The Central Bank should, in advance of its completion of its Consumer Protection Code review, require each institution serving the retail banking market to set out clearly to its customers which ombudsman/Alternative Dispute Resolution service will deal with complaints, where the customer does not accept the decision of the provider's internal complaints process. This information should be provided to the consumer as part of the pre-contractual information obligations and at the commencement of a complaints process.	***13.3***
9.	The Department of Finance should seek to ensure access to appropriate ombudsman/Alternative Dispute Resolution services for customers of passporting institutions is satisfactorily addressed at EU level.	***13.4***
10.	The Department of Finance should commission an annual survey of consumers' experiences and perceptions of the retail banking market based on the consumer survey commissioned for the Retail Banking Review.	***11.1***
11.	The Department of Finance should rationalise and simplify consumer protection legislation with the objective of eliminating overlapping provisions. This process should take account of the transposition of the forthcoming revision of the Consumer Credit Directive.	***13.1***
12.	The operation of the Central Credit Register should be amended, following engagement with relevant stakeholders, to:	***11.2***

- Reduce the reporting threshold for credit agreements from €500 to €200 and the consultation obligation threshold from €2,000 to €1,000; and
- Introduce a new lower fee for Central Credit Register consultations for low value loans (i.e., loans of less than €1,000, in line with the proposed changes to the obligatory consultation threshold) to facilitate smaller loans, particularly by credit unions.

The Department of Finance should draft legislation, if the proposed amendments require it.

13.	While complying with competition law requirements, the retail banking sector should increase its levels of collaboration, wherever possible, to reduce costs and improve/retain customer service levels. Potential areas include: • Shared banking hubs in locations where all branches have closed; and • Developing utility entities in areas such as ATM provision and operation.	***8.1***

14.	With regard to financial literacy and digital financial literacy:
	• the Department of Finance should:
	  ○ engage with and participate fully in the financial literacy stream of the Adult Literacy for Life Strategy; and
	  ○ seek to ensure that all stakeholders work together so that Ireland is compliant with the OECD High Level Principles on Financial Consumer Protection and the Recommendation on financial literacy.
	• The retail banking sector should:
	  ○ build on the work already done by the BPFI and the Irish Banking Culture Board to ensure that its offerings are appropriate to cater for the needs of adults at risk of harm or abuse and empower them to safely manage their own money and financial affairs. The sector should become more responsive to the needs of these 'vulnerable' customers and harness the opportunities that advancements in technology provides to assist them.
		13.5

Competition

15. With regard to its authorisations and approvals functions, the Central Bank should: ***5.1***

- continue to review its authorisation and approvals processes to identify how these might be improved. This should reflect the importance of a continued flow of high quality new entrants to the financial services markets, while also recognising the importance of gatekeeping activities in mitigating risks to protect consumers and the economy.
- provide guidance for firms on its authorisation and approvals processes to enhance clarity regarding its expectations, processes and timelines (including factoring in any pre-authorisation engagement);
- review the reporting of its authorisation activities. In particular, the Central Bank should enhance reporting of the overall timelines of firms going through authorisation and approvals processes; and
- continue to enhance its strategy and implementation to ensure that its regulatory approach is consistent with realising the benefits of innovation in financial services while ensuring risks are managed and mitigated. In this context, the Central Bank should conduct a detailed review of the Innovation Hub, including peer comparisons, to expand its impact and functionality. Consideration should be given to the types and benefits of regulatory sandboxes adopted in other countries.

16. Taking into account the legislative amendments in the forthcoming Credit Union (Amendment) Bill 2022, the credit union sector and its leadership should develop a strategic plan that enables the sector to safely and sustainably provide a universal product and service offering, which is community based, and which is offered to all credit union members, directly or on a referral basis. ***5.2***

Such a strategic plan should demonstrate how credit unions can:

- Scale their business model in a viable manner in key product areas such as mortgages and SME lending;
- Invest in expertise, systems, controls and processes such that the sector can deliver standard products and services

	across all credit unions, in a manner that manages risks arising and continues to protect members' savings; and • Provide the option of in-branch services for members of all credit unions. Where new or amended legislation is required to achieve a universal product offering and associated business model transformation, the Department of Finance (with guidance and technical advice from the Central Bank) should consider the necessary legislative changes.	
17.	In line with its view and its mandate, the Central Bank should: • In completing its Annual Performance Statement, include an assessment of how the exercise of its functions is consistent with the orderly and proper functioning of domestic financial markets; and • assess how existing domestic regulation impacts competition within domestic financial markets, recognising its importance to the orderly and proper functioning of those markets.	***5.3***
18.	The Department of Finance should prepare heads of a bill in 2023 to amend S.50 of the Central Bank (Supervision and Enforcement) Act 2013 to require the Central Bank to carry out and publish assessments of the costs and benefits of regulations it proposes to make under S.48 of the 2013 Act, where appropriate. The assessments are to consider the potential impacts on consumers and fair and sustainable competition, amongst other issues.	***5.4***
19	The Department of Finance should review the relevant legislation to identify actions, consistent with provisions governing data collection and use in relevant EU Regulations and Directives, to facilitate increased sharing of information between the Central Bank and the Competition and Consumer Protection Commission across all relevant areas of their respective remits.	***5.5***
20.	The Competition and Consumer Protection Commission and the Central Bank should build on existing arrangements and establish closer coordination to share perspectives, information and experience on the orderly functioning of markets, consumer protection and competition in the retail banking sector.	***5.6***

21.	The Central Bank should conduct a review of the Switching Code for payment accounts as soon as possible after the current mass migration of accounts is largely concluded. The review should incorporate input from the sector and other stakeholders regarding lessons from the mass migration. The review should also consider requiring the establishment of a switching service in accordance with the Payment Accounts Directive, including examining the feasibility of automatic or manual routing of credit and debit transfers for a set period after an account has switched.	**12.1**
SME		
22.	The retail banking sector reviews its strategies and delivery models for SME credit, making amendments where required to ensure good customer service standards and to facilitate effective engagement by SMEs with skilled staff, either remotely or in-person, as appropriate.	**10.1**
23.	The Department of Finance should continue to commission the Credit Demand Survey on an annual basis.	**10.2**
24.	The Department of Finance should continue to work with other Government Departments and the SBCI to identify SME credit market failures or gaps and to develop risk sharing schemes to address them. Where possible, this should be done in conjunction with the European Investment Fund.	**10.3**
25.	Following consultation with stakeholders, the Department of Finance should prepare legislation to require providers of credit to SMEs to be authorised and supervised by the Central Bank, so that all SME borrowers benefit from the protections of the Central Bank's SME Regulations.	**10.4**
26.	The Central Bank should review and amend the SME Regulations to take account of legislative changes and developments in the revised Consumer Protection Code, particularly digital/online matters, automated decision making and customer charters and service standards. The Central Bank should also review the regulations applicable to guarantees issued by, or on behalf of, SME borrowers.	**10.5**
Mortgages		
27.	The Department of Finance should work with the Central Bank in 2023 to identify measures and initiatives to build consumer and	**9.1**

	SME knowledge and confidence in the switching process for mortgages and other retail banking products, including taking actions that make switching easier, and that address impediments and gaps identified in the process. This work will be informed by the wider switching research being undertaken for the Department of Finance by the ESRI.	
28.	The Central Bank should, as part of its review of the Consumer Protection Code, consider enhancing requirements on how regulated firms provide information on alternative mortgage products to their customers to improve the take-up by mortgage holders of cheaper options which may be available to them. This should be addressed in a standalone section of the Consumer Protection Code.	***9.2***
29.	The retail banking sector should review their existing mortgage product suite to identify opportunities to enhance and expand it for the benefit of their customers, in particular where this could help reduce the borrower's overall cost of credit.	***9.3***
30.	The Department of Finance should consult with mortgage lenders and the Central Bank to determine if lenders can provide increased transparency in relation to the composition of variable mortgage pricing.	***9.4***
31.	Implementation of the IMF recommendation that the resolution of long term mortgage arrears needs to be considered and addressed in a coordinated way by various agencies, including the Department of Finance, the Central Bank, the Department of Justice, and the Insolvency Service of Ireland in consultation with other relevant agencies. The Department of Finance should, together with all the other relevant bodies, take this recommendation forward.	***9.5***
Other – Climate & Staffing		
32.	As a matter of priority, the retail banking sector should consider how best to expand its products and services so that it provides a competitive and effective financial offering to consumers and SMEs to assist in the transition to a lower carbon future.	***6.1***
33.	The retail banking sector should work with the Institute of Banking to consider the development of a Financial Services Skills	***14.1***

	Framework to build the skills and competencies needed for the future and sustainable development of the retail banking sector.	
34.	The pay restrictions should be amended by: • Permitting variable pay per employee of up to €20,000 per annum; • Allowing the provision of standard non-pay benefits for all employees; and • Solely for Bank of Ireland, removing the maximum pay cap of €500,000 for an individual.	***14.2***

APPENDIX 3 - OVERVIEW OF TECHNOLOGIES THAT ARE IMPACTING FINANCIAL SERVICE PROVISION

Distributed ledger technologies (DLT): DLT is a database technology that allows the creation, secure transfer (finality), and storage of information where the ledgers are not centrally controlled and administered (traditional banking relies on centralised ledgers). To date the application of DLT has been focused on cryptocurrencies.

Big Data analytics: As day-to-day activities have been digitalised, this has created an increased amount of data up to and including very large and complex data sets, commonly known as 'Big Data.' Within financial services big data can be used to develop more granular pricing strategies (due to more broadly based assessments of individual customers' risk profiles), tailor promotional materials and enhance internal risk management (for example, improved fraud detection).

Internet of Things (IoT): The IoT refers to the numerous connected devices that capture information regarding the physical world. IoT sourced data is expected to support increased tailoring of products, risk profiling and pricing.

Cloud computing and storage: Cloud based services provide cost efficient, scalable on-demand processing and storage capacity for data. It has greatly increased financial institutions' capacity to collect and analyse data, which in turn supports the use of data analytics in both customer facing and internally-focused activities.

Artificial intelligence (AI): AI can focus on a range of different aspects of human intelligence including recognition, understanding, learning, problem solving reasoning and decision-making. AI is often used in reference to machine learning – the latter being where machines are trained using historical data to recognise patterns and classify new data.

Biometric technologies: Biometric technologies rely on the recognition of physiological or behavioural characteristics, and can be used for identity authentication. They represent a potential improvement in security compared to standard passwords, albeit risk mitigation is also required to ensure that biometric information is not compromised.

Augmented/virtual reality: These technologies provide new ways for consumers to perceive or interact with their environment.

APPENDIX 4 – COMPONENTS OF A BANK'S CAPITAL REQUIREMENTS

The capital requirement for a bank is made up of a number of components:

Pillar 1 – the minimum capital ratio every bank must maintain which is set at 8%. Of this 8% minimum requirement, at least 4.5% must be Common Equity Tier 1 (CET1); and at least 6.0% must be Tier 1. Tier 1 comprises CET1 and Additional Tier 1 (AT1). A bank meeting this Tier 1 requirement can use up to 2% of Tier 2 capital to maintain the overall minimum Pillar 1 requirement of 8%. The Pillar 1 capital for a bank meeting each of the minimum requirements is:

CET1	4.50%
AT1	1.50%
Tier 1	6.00%
Tier 2	2.00%
Pillar 1 requirement	8.00%

See below for a description of each of the components of capital.

Pillar 2 requirement (P2R) – this is a bank specific requirement which is designed to cover risks which are underestimated or not covered by the Pillar 1 requirement. A bank's P2R is determined on the basis of the annual Supervisory Review and Evaluation Process (SREP) which is carried out by the regulator.

In addition to P2R, the regulator may also recommend bank specific **Pillar 2 guidance (P2G)** indicating the level of capital it expects a bank to maintain to withstand stress. As with P2R, P2G is set as part of the annual SREP. However, unlike P2R, P2G is not legally binding.

Combined buffer requirement – the collective term for the four capital buffers for in CRDIV. The buffers can firstly act as a mechanism to provide capital for a range of cyclical and structural systemic risks so that banks can build up a store of capital during the favourable phases of the economic cycle to provide protection against an economic downturn. If a bank breaches the combined buffer, automatic safeguards apply to limit the amount of discretionary payments it can make (e.g. dividends, coupons, bonuses and discretionary pension payments).

In addition to the capital levels set by the regulator, as a prudent measure banks generally add on their own buffer which is commonly referred to as the management buffer.

A recent example of the benefits of these buffers was in March 2020, when the Central Bank reduced the Countercyclical Capital Buffer to 0% following the COVID-19 pandemic. It is estimated that this freed up almost €1 billion in capital for the Irish banking system to help absorb potential losses and maintain a supply of credit to Irish households.

Irish retail banks have higher average risk weights on loans than almost all other European banks. This, is turn, leads to the requirement to maintain higher levels of capital which

contributes to the higher interest rates borrowers are charged. This is discussed in more detail in the chapters on Mortgages and SME Credit.

Capital Buffers

The Capital Conversion Buffer – which is a uniform requirement applied to all banks. It is fixed at 2.5% of a bank's total Risk Weighted Assets (RWA) and was phased-in between January 2016 and December 2018. Its objective is to conserve a bank's capital and all banks are required to hold this buffer.

The Global/Other Systemically Important Institution (G-SII/O-SII) Buffer – which is designed to ensure that such systemically important financial institutions hold a higher level of capital in order to compensate for the higher risk they pose to the financial system. Global Systemically Important Institutions (G-SII) are financial institutions that, by virtue of their size and complexity could pose financial stability risks to the global financial system. Other Systemically Important (O-SII) Institutions are of systemic importance to the economy in which they operate. G-SIIs are subject to a G-SII buffer, however there are currently no G-SII entities headquartered in Ireland. O-SIIs are identified with reference to the size, systemic importance, significance of cross border activities and interconnectedness of institutions. Buffer rates are set at least annually by the Central Bank and can be set in the range of 0% to 2%.

The Countercyclical Capital Buffer (CCyB) – which is designed to make the banking system more resilient and less pro-cyclical. The buffer requires banks to build up a reserve of capital during periods when cyclical systemic risk is rising, which can then be used to absorb losses during an economic downturn. The CCyB is set quarterly by the Central Bank for Irish exposures with reference to the prevailing macroeconomic and credit/lending environment. The buffer can be set in the range of 0% - 2.5% of RWA, or higher if deemed necessary. In June 2022, the Central Bank announced an increase in the CCyB from 0% to 0.5% to take effect in June 2023. The move is seen as a step in a gradual build-up of the CCyB to 1.5%

The Systemic Risk Buffer (SRB) – which is designed to mitigate long-term, non-cyclical risks which may have serious negative consequences for the real economy. This requirement may be applied to all of a bank's exposures or only to exposures to specific sectors (e.g. commercial real estate). Its implementation is a national discretion in CRDIV and to date has not been exercised in Ireland. Depending on how Designated Authorities decide to apply an SRB, a bank could be required to only meet the higher of the G-SII/O-SII Buffer or the SRB, or they could be required to meet the cumulative total of the G-SII/O-SII Buffer and the SRB. The SRB would also apply to banks which are not subject to a G-SII/O-SII Buffer. Before introducing an SRB, the authority must justify why none of the existing measures in CRDIV/CRR would be sufficient to address the systemic risks.

Calculation of capital Ratios

Capital metric	Numerator	Denominator	Note
Common equity tier 1 (CET1)	Shareholders' funds after regulatory adjustments	RWAs	1
Tier 1	Common equity tier 1 plus additional tier 1 (AT1)	RWAs	2
Total capital	Tier 1 plus Tier 2	RWAs	
Leverage ratio	Tier 1 (as above)	Total exposures	3

Note 1 – Regulatory adjustments comprise a number of items such as deductions in relation to deferred tax assets, intangible assets and goodwill, etc.

Note 2 – AT1 securities are hybrid instruments which share features of both debt and equity, i.e. they are similar in nature to debt instruments but convert to equity or can be written down under certain circumstances e.g. they convert into CET1 capital or are written down if a bank's CET1 ratio falls below a certain threshold.

Note 3 – Total exposures include on-balance sheet items, off-balance sheet items and derivatives, and should generally follow the accounting measure of exposure.

APPENDIX 5 – MORTGAGE ARREARS – POLICY AND LEGISLATIVE ACTIONS

Year	Action
2009 - 2013	• Code of Conduct on Mortgage Arrears (CCMA) (statutory code) – provides protection to those in mortgage arrears or pre-arrears. • Revised a number of times to respond to changing circumstances and provide more protections for mortgage holders.
2012	Mortgage to Rent (MTR) introduced.
2012	Personal Insolvency Act, 2012 - a reformed bankruptcy system and the introduction of 3 new statutory debt resolution frameworks, including the Personal Insolvency Arrangement framework (PIA) to cater for secured debt.
2012	Mortgage information and advice scheme was introduced by the DSP.
2013	A revised CCMA making a distinction between 'co-operating' and 'not co-operating' borrowers and provided that a moratorium of at least eight months will be available to 'co-operating' borrowers.
2013	Insolvency Service of Ireland (ISI) established by Personal Insolvency Act, 2012
2014	ISI waived the existing application fees for the three statutory debt relief solutions to remove possible perceived barrier to debtors availing of solutions.
2015	The Consumer Protection (Regulation of Credit Servicing Firms) Act 2015 was enacted, July 2015. It was introduced to fill the consumer protection gap where loans were sold by the original lender to an unregulated firm.
2015	The Personal Insolvency (Amendment) Act 2015 enacted to allow the Courts, where reasonable, to approve a PIA that includes a mortgage secured on a primary home, even where it has been rejected by creditors (including the primary home mortgage creditor). (Bank veto no longer in place)
2016	An enhanced advice and information scheme called 'Abhaile' was introduced and is a Government funded mortgage arrears resolution service, which gives indebted borrowers access to State-funded financial or legal professionals to give advice and assistance on how to resolve their mortgage arrears.

2018	• The Minister for Finance requested the Central Bank carry out a review of the CCMA as soon as possible. • Consumer Protection (Regulation of Credit Servicing Firms) Act 2018 expanded the definition of credit servicing to include, inter alia, loan ownership.
2021	In 2021 the Department of Justice announced the commencement of the main provisions of the Personal Insolvency (Amendment) Act 2021: • Made practical changes to ensure that borrowers have effective access to personal insolvency legislation • The measures will help borrowers at risk of losing their homes • Removed a barrier to borrowers applying for court review, if creditors refuse a personal insolvency proposal that includes their home mortgage arrears • Removed obstacle for people on very low incomes, seeking to resolve debts via a Debt Relief Notice • Removed cut-off date of 1 Jan 2015 so that a borrower whose home mortgage arrears first arose after that date could also to apply to court for review
2022	The Department of Justice is finalising a review of the operation of the Personal Insolvency Acts, in consultation with the Minister for Finance, to review the operation of Part 3 of the 2012 Act, and responds to a commitment in the Programme for a Partnership Government.

APPENDIX 6 - TERMS OF REFERENCE

The Programme for Government contains the following commitment:

We will support the European Central Bank and the Central Bank of Ireland's actions to ensure stability in the banking sector. We will encourage competition within our banking sector and develop the Fintech sector as a source of employment and competition. We do not believe that there is a long-term case for the State to remain as a shareholder in the Irish banking sector. However, we should not sell our current holdings until such a time as we are likely to recoup a significant portion, if not all, of the State's investment.

In support of this objective, the Department's Statement of Strategy has a strategic goal of a ensuring a '*well regulated, sustainable banking and financial sector*'.

The Minister for Finance is already strengthening the regulatory and consumer protection framework through the following legislative initiatives:

- The drafting of the Central Bank (Amendment) Bill to implement an Individuality Accountability Framework (including Senior Executive Accountability Regime)
- The passage and enactment by year-end of the Consumer Protection (Regulation of Retail Credit and Credit Servicing Firms) Bill 2021 to require that any firm which offers indirect credit, hire purchase, Personal Contract Plans (PCPs) or consumer hire agreements to consumers and other relevant persons to be authorised as a retail credit firm by the Central Bank;
- The drafting of the Credit Review Service Bill, to put the current Credit Review Office on a statutory basis and extend its scope to cover more lenders to SMEs; and
- The drafting of the Consumer Credit (Amendment) Bill to implement the first major reform of the licensed moneylending sector since 1995.

Other significant changes in the regulatory landscape flow from EU Directives and Regulations. These include the recent transposition of the Risk Reduction Package, the ongoing transposition of the Covered Bond Directive, the Crowdfunding Regulation and the forthcoming NPL Directive. In addition, further EU legislative initiatives are underway, including the Basel 3 finalisation package and a draft Consumer Credit Directive, which include several significant amendment to the current regime. The role of the Eurogroup and its ongoing work on matters such as Banking Union also needs to be taken account of.

Against the backdrop of a changing landscape for banking in Ireland, and in light of the commitments in the Programme for Government, the Minister for Finance has tasked the Department with preparing a Report:

- Reviewing the current landscape for the provision of retail banking products and services in Ireland, including assessing how the banking system can best support economic activity;
- Assessing how the retail banking sector has evolved over the last two decades and exploring what these market trends might mean for the evolution of the retail banking market over the next 5-10 years
- Considering the size and structure of the retail banking sector and best/recent practices in similar sized open economies in the EU/OECD to see what lessons Ireland can learn from such countries:
- Considering the business model for retail banking in Ireland including among other issues, viability of the sector, size of market, regulatory requirements, capital requirements, cost of doing business and operational issues arising from difficulties with staff recruitment and retention; and in this context, consideration should be given to wider EU and international banking developments;
- Considering the forces for change in retail banking including structural changes stemming from the developments in fintech or digital finance (innovations in technology) (including as a disruptor of traditional models) and regulatory changes (e.g. open banking);
- Taking account of the longer term implications of the COVID-19 pandemic and the post-Brexit financial landscape, including any new banking entrants, which will also be important considerations;
- Considering potential consequences for consumer protection (including for existing and future customers and for vulnerable customers), competition and financial stability objectives;
- Assessing competition and consumer choice in the Irish market for banking services across the range of suppliers, products and channel of provision; and considering if there are barriers to entry, expansion, or the introduction of new products;
- Reflecting on the findings of the IMF Financial Sector Stability Assessment (FSAP) of Ireland (due in June 2022) and examining what changes, if any, are required to the policy and regulatory landscape on foot of the FSAP recommendations;
- In recognition that a key role of the banking sector is in the provision of sustainable credit to the economy, assessing the availability of credit to SMEs from both banks and non-banks as well as considering the impact of State measures in this area and if policy changes are merited; and
- Consider options to develop the mortgage market by –
- Reviewing the range of bank and non-bank providers currently involved in the provision of mortgages in Ireland and assessing their impact on competition, consumer choice and protection, market/regional coverage and any financial stability concerns; and, in this context, the need to make the Irish market more attractive to new entrants;

- Assessing the unique characteristics of the Irish mortgage market, including in terms of competition and consumer protection and surveying the views of stakeholders and potential new entrants on barriers to entry into the Irish mortgage market;
- Identifying how mortgage interest rates are determined in the Irish market, the role that competition between lenders plays in that process along with Irish capital requirements and comparisons with other jurisdictions;
- Setting out a range of options to improve consumer choice in the range of products available such as longer-term fixed rate products and green mortgages; and
- Considering options to make the switching of mortgages easier to underpin competition in the mortgage market.

The Department of Finance will conduct this review by means of a specifically dedicated Review Team. In preparing its report into the retail banking sector, the Review Team will extensively engage with stakeholders and as part of this process will seek the views of the public by means of a public consultation.

The Review Team will present its draft report to the Minister in November 2022.

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