



STATUTORY INSTRUMENTS.

S.I. No. 411 of 2008.



CREDIT INSTITUTIONS (FINANCIAL SUPPORT) SCHEME 2008

(Prn. A8/1654)

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I, BRIAN LENIHAN, Minister for Finance, in exercise of the powers conferred on me by section 6(4) of the Credit Institutions (Financial Support) Act 2008 (No. 18 of 2008), hereby make the following scheme with respect to which, pursuant to section 6(5) of that Act, a draft has been laid before each House of the Oireachtas and a resolution approving of the draft has been passed by each such House:

Citation

1. This Scheme may be cited as the Credit Institutions (Financial Support) Scheme 2008.

Scheme

2. The terms of this Scheme are as set out in article 3 and the Schedule.

Definitions

3. In this Scheme,

3.1 “covered institution” means a credit institution or a subsidiary of a credit institution—

(a) that stands specified by order by the Minister under section 6(1) of the Act of 2008; and

(b) that has joined this Scheme in accordance with paragraph 5 of the Schedule;

3.2 “Act of 2008” means Credit Institutions (Financial Support) Act 2008 (No. 18 of 2008);

3.3 “covered liabilities” shall be construed in accordance with paragraph 10 of the Schedule; and

3.4 “guarantee acceptance deed” means a deed referred to in paragraph 5 of the Schedule entered into between the Minister and a covered institution and, if required by the Minister pursuant to paragraph 5 of the Schedule, any of the covered institution’s subsidiaries or its parent or both.

Notice of the making of this Statutory Instrument was published in “Iris Oifigiúil” of , 2008.

SCHEDULE

TERMS OF SCHEME

Scope

1. The Minister makes this Scheme in the public interest because the Minister is of the opinion that:

1.1 there is a serious threat to the stability of credit institutions in the State generally, or there would be such a threat if he or she did not provide the financial support;

1.2 the provision of the financial support to a specific institution faced with financial difficulties is necessary, in the public interest, for maintaining the stability of the financial system in the State; and

1.3 the provision of the financial support is necessary to remedy a serious disturbance in the economy of the State.

This Scheme may apply to any covered institution where it is necessary to further the financial stability objectives in section 2(1) of the Credit Institutions (Financial Support) Act 2008 and including in particular the maintenance of the systemic stability of the banking sector in the State.

2. The Minister makes this Scheme having regard to the following objectives in particular:

2.1 maintaining financial stability in the best interests of the public and the economy of the State;

2.2 remedying a serious disturbance in the economy by safeguarding the financial system and economy of the State from the threat caused by the unprecedented turmoil in the international financial markets and the particular macro-economic conditions in the State;

2.3 providing lasting systemic stability in the banking system and ensuring its long-term sustainability;

2.4 preventing abuse of the guarantee;

2.5 ensuring compliance with the requirements of EU State aid and competition law; and

2.6 minimising the potential cost to the Exchequer and taxpayers; in particular where the guarantee is called upon and a payment is made but the financial support cannot be recouped in full from the covered institution to which it was provided, the principle is that it would be recouped in full from the covered institutions by the State over time in a manner consistent with their long-term viability and sustainability.

3. The institutions eligible under this Scheme are those systemically important credit institutions which the Minister specifies by order under section 6(1) of the Act of 2008 in the exercise of his or her powers under that Act as requiring financial support and fulfilling the objectives of the Act of 2008. The Minister may consult with the Governor prior to making any such order.

Where the Minister specifies a credit institution by order, the credit institution so specified will have a limited period of time as determined by the Minister to join this Scheme pursuant to paragraph 5 before it loses the opportunity to join the Scheme.

4. Each covered institution must comply with the regulatory requirements of the Regulatory Authority and the Governor.

5. A covered institution specified by order under section 6(1) of the Act of 2008 joins this Scheme by executing a guarantee acceptance deed in the form to be specified by the Minister. The Minister may also require that a parent or any other company within the covered institution's group execute such guarantee acceptance deed in respect of itself or any other company within the group.

6. A covered institution and any group company party to a guarantee acceptance deed shall be required to comply with all the terms and conditions of this Scheme and the relevant guarantee acceptance deed and all directions given and requirements made by the Minister or the Regulatory Authority under this Scheme. The Minister will apply the terms and conditions of this Scheme and each guarantee acceptance deed on an objective basis: (i) taking into account the role of each covered institution in the State's banking system and the overall economy of the State; and (ii) in a non-discriminatory fashion so as to avoid undue distortive effects on neighbouring markets and the internal market as a whole.

7. By entering into a guarantee acceptance deed, a covered institution and in certain circumstances a group company party to a guarantee acceptance deed, shall agree to:

7.1 pay the quarterly charge as referred to in paragraph 16 below;

7.2 indemnify the Minister in respect of any payments of covered liabilities made by the Minister following a claim made under the guarantee or any other liabilities incurred by the Minister in that regard; and

7.3 indemnify the Minister in respect of any costs, claims, losses or liabilities incurred by the Minister in connection with the provision of the financial support to the covered institution or a subsidiary;

together, in all cases, with interest accrued to the date of payment at a rate to be specified in the guarantee acceptance deed.

8. The Minister may review and vary the terms and conditions of this Scheme from time to time, at no later than six-month intervals, to ensure that it is achieving the purposes of the Act of 2008. At such a review, the Minister shall consider, *inter alia*, the continued requirement for the provision of financial support

under this Scheme with regard to the objectives of this Scheme and section 2(1) of the Act of 2008. The results of any such review shall be provided to the European Commission.

9. Subject to the terms and conditions of this Scheme and the relevant guarantee acceptance deed, the Minister stands as guarantor of the covered liabilities of a covered institution for the period from 30 September 2008 to 29 September 2010 inclusive. No call can be made under the guarantee after 29 September 2010.

10. The covered liabilities are those liabilities existing from 30 September 2008 or at any time thereafter up to and including 29 September 2010, in respect of the following:

10.1 all retail and corporate deposits (to the extent not covered by existing deposit protection schemes in the State or any other jurisdiction);

10.2 interbank deposits;

10.3 senior unsecured debt;

10.4 asset covered securities; and

10.5 dated subordinated debt (Lower Tier 2),

excluding any intra-group borrowing and any debt due to the European Central Bank arising from Eurosystem monetary operations.

The Minister shall publish the total covered liabilities of the covered institutions in aggregate quarterly in *Iris Oifigiúil*.

11. The Minister shall impose specific restrictions on a covered institution in respect of dated subordinated debt (Lower Tier 2) covered by the guarantee, so as to prevent the unwarranted expansion of capital and lending activity during the guarantee period. Such restrictions shall include but not be limited to those set out at paragraphs 36 to 43.

In particular the Regulatory Authority shall require that where new dated subordinated debt is covered by the guarantee, the covered institution benefiting from such a financing will also maintain at least the solvency ratio initially obtained when this financing takes place during the whole duration of the guarantee period.

The details of the restrictions imposed by the Regulatory Authority on a covered institution benefiting from a guarantee on new subordinated debts will be transmitted each six months to the European Commission.

12. The covered liabilities of a subsidiary of any parent credit institution which is not regulated by the Regulatory Authority (being a subsidiary which is a covered institution) shall include only such covered liabilities of that subsidiary: (i) which relate to its own business; and (ii) in respect of which there is no

recourse to any other entity within or outside its group and shall not include liabilities which, in the absence of the guarantee, would normally be those of other members of the covered institution's group. The Minister shall monitor the use of this Scheme by such subsidiaries to ensure the purposes of the Act of 2008 and this Scheme are achieved and that the guarantee is not being abused, not being used in a manner irreconcilable with the purpose of the guarantee or not being used for the benefit of any entity other than the relevant covered institution. The Minister may, at any time during the period of this Scheme, impose specific obligations under this Scheme or the guarantee acceptance deed given by the covered institution or its parent or any subsidiary to appropriately ring-fence the activities of a covered institution from its parent to minimise the covered institution's financial exposure to its parent credit institution.

13. The Minister may revoke the guarantee in whole or in part in relation to a covered institution if:

13.1 the covered institution is acquired by or merges with another institution or person not themselves benefiting from this Scheme, subject to the Minister's discretion, after consultation with the Governor and the Regulatory Authority, or

13.2 in the Minister's opinion, after consultation with the Governor and the Regulatory Authority, the covered institution is in material breach of its obligations under this Scheme; or

13.3 if the Minister, after consultation with the Governor and the Regulatory Authority, is of the opinion that the matters set out in section 2(1) of the Act of 2008 no longer apply; or

13.4 if the covered institution, with the consent of the Minister, withdraws from this Scheme.

14. The Minister shall give public notice in *Iris Oifigiúil* at least 90 days before revoking a covered institution's guarantee.

15. After any revocation in whole or in part of its guarantee, a covered institution shall continue to pay a charge for the period of the remainder of this Scheme in proportion to any amount of its liabilities which continue to be covered by the guarantee. If a covered institution's guarantee is revoked in whole or in part, covered liabilities with a fixed term outstanding at the date of expiry of the guarantee shall continue to be covered by the guarantee to their maturity date or 29 September 2010, whichever is earlier.

Charge

16. Each covered institution shall pay a charge to the Exchequer for its guarantee. The charge will be calculated separately each quarter for each covered institution having regard to, *inter alia*;

16.1 the realistic assessment of the risk it is assessed to represent on the basis of all the relevant factors (including the credit quality of the covered institution, the covered liabilities, and the duration of the guarantee);

16.2 the steps the covered institution has taken to reduce that risk consistent with the objectives of this Scheme;

16.3 the fact that the charge imposed seeks to make this Scheme self-financing, so far as possible having regard to the circumstances of the covered institution and the purposes of this Scheme;

16.4 the need to ensure that the covered institutions are not unduly advantaged by the guarantee;

16.5 the likely risk of default;

16.6 the administrative costs of this Scheme; and

16.7 the provision of an adequate return for taxpayers.

17. Each covered institution shall pay the charge quarterly, in advance, to the Minister, payable no later than five working days after the beginning of each quarter, during the period the covered institution avails itself of a guarantee, except that the payment in respect of the first quarter shall be payable at the end of that quarter. The charge shall be calculated by reference to the composition of the covered institution's average month-end covered liabilities during the preceding quarter. The first payment shall be made in respect of a covered institution's outstanding covered liabilities as at 30 September 2008.

18. The Minister in his or her sole discretion shall specify the guarantee charging model.

19. Without prejudice to paragraph 18, for convenience of reference, there is set out in the Annexe to this Scheme a summary of the guarantee charging model. The main principle is that the Minister estimates an aggregate cost that the State will bear as a consequence of the guarantee and each covered institution will pay its share in accordance with its risk profile and the guarantee charging model. In case the actual cost for the State is higher, the charge will be adapted accordingly.

20. The amount of the charge payable by a covered institution in respect of each quarter shall be calculated by the covered institution and independently verified to the Minister in writing at the same time by the covered institution's external auditors.

21. The charge will be credited to a designated account to be maintained at the Central Bank as a reserve for any payments to be made under this Scheme. Any amounts standing to the credit of such account at the expiry of this Scheme will be paid to the Exchequer.

22. The Minister may in his or her sole discretion review the application of the guarantee charging model every six months and may take such advice and

make such adjustments as the Minister in his or her sole discretion deems necessary to support the achievement of the purposes of the Act of 2008 and the recovery of the aggregate cost to be borne by the State as a consequence of the provision of the guarantee and any change in the level of the aggregate charge where the actual cost to the State exceeds that estimated.

23. The Minister shall report to the Oireachtas Committee on Finance and the Public Service every six months on the level of charges received from covered institutions and progress in relation to the purposes of the Act of 2008 and the compliance with the terms and conditions of this Scheme.

Transparency and Enforcement

Information and Monitoring

24. A covered institution shall submit such reports as are requested by the Regulatory Authority on behalf of the Minister which the Regulatory Authority considers are necessary to monitor compliance with the terms and conditions of this Scheme and the achievement of the purposes of the Act of 2008. These reports shall be submitted with such frequency and in such form as the Regulatory Authority shall determine and shall address, *inter alia*, liquidity requirements, capital ratios, asset quality, risk exposures and funding costs.

25. The Regulatory Authority shall submit reports on the compliance by covered institutions with the terms and conditions of this Scheme to the Minister in such form, containing such information and at such frequency as the Minister shall determine.

26. Each covered institution shall, at such frequency as the Minister shall determine, confirm in writing to the Minister its compliance with the Irish Banking Federation Code of Practice on Mortgage Arrears and the Consumer Protection Code issued by the Regulatory Authority.

27. Every quarter each covered institution shall provide the Regulatory Authority on behalf of the Minister with compliance certificates, in such form as may be required by the Minister, from: (i) its auditors; and (ii) its chairman and chief executive jointly, confirming compliance with all of the terms and conditions of this Scheme. The Minister may direct the Regulatory Authority to require any report or other information to be provided by a covered institution pursuant to this Scheme to be audited by an independent auditor at the cost and expense of the covered institution. A covered institution shall comply with any such requirement.

28. The Minister, after consultation with the Governor and the Regulatory Authority, may direct a covered institution to draw up a restructuring plan to ensure compliance with the objectives of this Scheme. The Minister shall do so, in case that a covered institution's solvency ratio falls below the minimum regulatory standards on a material basis. Such plan shall be submitted for the Minister's approval within such timeframe as he or she may specify. Any such plan shall be required to comply with EU State aid and competition law. The Minister, in consultation with the Governor and the Regulatory Authority, may

direct the covered institution to make changes to such restructuring plans and implement the plans (including any changes) within a specified timeframe as determined by him or her. A covered institution shall comply with any such direction.

29. The Minister may direct the Regulatory Authority to require such other reports from a covered institution as he or she may consider necessary.

30. Subject to the requirements of the Treaties governing the European Communities (within the meaning of the European Communities Act 1972 (No. 27 of 1972)) and the Statute of the European System of Central Banks and of the European Central Bank, and in accordance with applicable law, the Minister, the Governor and the Regulatory Authority may disclose to each other any information which they receive (including information relating to a period before the covered institution availed itself of the guarantee under this Scheme) concerning a covered institution or its subsidiaries and may use such information in respect of the performance of this Scheme or in the case of the Central Bank (including the Regulatory Authority), the performance of its statutory functions. All covered institutions shall consent to any disclosure of information and provide such information as the Minister requires to perform his or her functions under the Act of 2008 and this Scheme. All such information shall be treated as confidential.

31. Each covered institution shall consult with the Regulatory Authority with a view to preparing a code of practice for effective risk management, in furtherance of the purposes of the Act of 2008. This code of practice shall be completed and provided to the Regulatory Authority by each covered institution by 31 March 2009.

Board representation and executive management

32. In order to promote the public interest, a covered institution shall, at the direction of the Minister, take all reasonable steps to appoint at least one but no more than two non-executive directors to its board from a panel approved by the Minister during the period of the guarantee. The covered institution shall remunerate those non-executive directors. The Minister will also have the right to appoint persons to observe all meetings of the remuneration, audit, credit and risk committees of a covered institution. Such observers shall have the right to attend all meetings and have access to necessary committee papers and other relevant information.

33. The board of a covered institution shall represent an appropriate balance between executive and non-executive directors. The Regulatory Authority following consultation with the Minister may require changes in the composition where such a balance is not in place. A covered institution shall comply with such a requirement.

34. A covered institution shall comply with any direction from the Minister or the Regulatory Authority or both to take specified steps to restructure its

executive management responsibilities, strengthen its management capacity and improve its corporate governance.

Enforcement

35. If in the opinion of the Minister a covered institution is in breach of its obligations under this Scheme in a manner which is material in the context of the provision of the guarantee, the Minister may by notice in writing:

35.1 increase the charge payable under paragraph 16 by the covered institution; or

35.2 impose additional conditions on the covered institution; or

35.3 revoke the guarantee for the covered institution in accordance with paragraph 13.

Commercial Conduct

36. The Regulatory Authority in consultation with the Minister may regulate the commercial conduct of covered institutions strictly in order to achieve the objectives of this Scheme as described in paragraph 2. The Regulatory Authority in consultation with the Minister shall impose conditions regulating the commercial conduct of a covered institution's business, having regard to capital ratios, market share and balance sheet growth, in order to minimise any potential competitive distortion that may otherwise arise and to avoid any abuse of the guarantee or any use in a manner irreconcilable with the purpose of the guarantee.

In particular the Regulatory Authority in consultation with the Minister shall monitor and review the expansion of the activities of covered institutions benefiting from the guarantee in order to ensure that their aggregate growth in balance sheet volume is not excessive and does not in any event exceed:

36.1 the annual rate of growth of Irish nominal GDP in the preceding year; or

36.2 the average annual historical growth in their balance sheets of Irish credit institutions during the period 1987-2007; or

36.3 the average growth rate of the balance sheet volumes in the credit institution sector in the EU in the preceding six months,

whichever is the higher. In case of any breach of this obligation, the Regulatory Authority shall adopt, within four weeks, appropriate measures to restore the situation and inform the European Commission thereof.

37. A covered institution shall conduct its affairs in a manner that progressively reduces the risk to the Exchequer under its guarantee. In particular, a covered institution shall be required to do one or more of the following:

37.1 appropriately manage its balance sheet in a manner consistent with the purposes of the Act of 2008 and the need to avoid significant distortion of financial flows;

37.2 put in place improved structures to ensure long-term stability of funding;

37.3 take steps to restructure its executive management responsibilities and strengthen its management capacity and corporate governance;

37.4 improve liquidity, solvency and capital ratios in circumstances where this is required;

37.5 take measures to minimise any risk of recourse to the guarantee,

as directed by the Governor and the Regulatory Authority, after consultation with the Minister.

38. No covered institution shall without the prior approval of the Minister acquire shares in any other credit institution or financial institution, establish any subsidiaries or enter into or acquire any new business or businesses, where, in the opinion of the Minister following consultation with the Governor and the Regulatory Authority, such action would increase the liability of the Exchequer under the guarantee.

39. A covered institution shall comply with any targets on assets and liabilities to be set by the Regulatory Authority, after consultation with the Minister. These targets may include, but are not limited to: loan/deposit ratio, wholesale funding/total liabilities ratio, deposit growth and maximum loans-to-value on new loans; all of which shall be limited to agreed values on new residential mortgages and all other new lending activity. A covered institution shall be required to limit its exposures to any sector, customer or connected customers where in the opinion of the Regulatory Authority, after consultation with the Minister, it is in the public interest, and in the interests of financial stability and confidence in the banking system.

40. Unless it has already done so, a covered institution shall take steps to establish such funding structures as the Regulatory Authority, in consultation with the Minister, thinks appropriate having regard to the purposes of the Act of 2008, within such period as the Minister may direct.

41. A covered institution shall take steps to comply with such liquidity, solvency and capital ratios as the Regulatory Authority may direct, following consultation with the Minister.

42. A covered institution shall comply with rules governing the declaration and payment of dividends made by the Minister after consultation with the Governor and the Regulatory Authority. These rules will take into account the objective of achieving or maintaining the capital ratios referred to in paragraph 41. No new dividends shall be declared or paid by a covered institution before such rules are made.

43. A covered institution shall not engage in buy-backs (public or private) or redemptions of its ordinary or other shares without the approval of the Regulatory Authority given after consultation with the Minister.

44. A covered institution shall not pass on the costs of the guarantee to its customers in an unwarranted manner.

Corporate Social Responsibility

45. Each covered institution shall procure that the Irish Banking Federation, on behalf of all covered institutions, submits a bi-annual report to the Minister on goals and targets laid down by the Minister in relation to Corporate Social Responsibility, including the goals and targets with respect to the objectives of this Scheme, the delivery of the national payments strategy, the promotion of financial inclusion, the development of financial education and the implementation of the next phase of the Government's Social Finance Initiative. This report shall also be published on each covered institution's website within 5 working days of being issued.

Controls on Executive Remuneration

46. The Minister will establish an independent committee called the Covered Institution Remuneration Oversight Committee ("CIROC") comprising three members appointed by him or her to oversee all remuneration plans of senior executives of the covered institutions.

47. Each covered institution shall prepare a plan to structure the remuneration packages of directors and executives so as to take account of the objectives of the Act of 2008. For the purposes of this paragraph, remuneration shall include total salary, bonuses, pension payments and any other benefits received from a covered institution and its group entities, or otherwise received by a director or executive arising from the performance of his or her functions as a director or executive. Such plans shall cover, *inter alia*, executive bonuses including share options, if any. Bonuses shall be measurably linked to reductions in guarantee charges, reduction in excessive risk taking and encouraging the long-term sustainability of the covered institution.

48. Each covered institution shall submit a report to CIROC, no later than six weeks after the relevant covered institution joins this Scheme, demonstrating how its remuneration policies for the year ahead will comply with paragraph 47. CIROC shall prepare a report for the Minister, within 3 months of receipt of such covered institution's report, making a recommendation where appropriate on compliance by the covered institution with the terms of this paragraph. Where the Minister considers, on the advice of CIROC, that the covered institution has not complied with the requirements of this paragraph, he or she may direct the covered institution to amend the remuneration plan so that compliance is achieved.

49. A covered institution shall not enter into any contractual arrangement that provides for termination compensation or equivalent to be payable to any director or executive for the duration of this Scheme.

Compliance and Furtherance of this Scheme and the Act of 2008

50. A covered institution shall manage the business of its group at all times with a view to furthering the purposes of this Scheme and the Act of 2008. As provided in paragraph 12, in consultation with the relevant overseas regulator and subject to the requirements of the treaties governing the European Communities and the ESCB Statute, the Minister may require certain obligations of this Scheme, as he or she may specify in writing to the covered institution, to apply to the parent of a covered institution or any member of its group as a condition of benefiting from this Scheme.

Oversight, Co-ordination and Review

51. The Minister shall consult with the Governor and the Regulatory Authority before exercising any of his or her functions under this Scheme which relate to any of the statutory responsibilities of the Governor and the Regulatory Authority. However, decisions or actions taken by the Minister pursuant to or in relation to this Scheme are in his or her absolute discretion provided that nothing in this Scheme shall prejudice the independence of the Governor or the Regulatory Authority.

52. For the duration of this Scheme, the Governor and the Chief Executive of the Regulatory Authority shall monitor the operation of this Scheme and shall report regularly to the Minister as to the operation of this Scheme and the compliance by covered institutions with this Scheme in a consistent manner and to ensure that in doing so the public interest is protected, without prejudice to the Governor's responsibility for the performance of the functions conferred on the Governor and the Central Bank by or under the treaties governing the European Communities and the ESCB Statute.

Claims under the Guarantee

53. In the event of any default of a covered institution in respect of a covered liability, then:

53.1 relevant creditors may make a claim against the Minister in respect of any unpaid covered liabilities;

53.2 the Minister shall pay the relevant creditors an amount equal to the unpaid covered liabilities having first assessed that such claims are valid;

53.3 pursuant to the guarantee acceptance deed, the Minister shall be entitled to repayment of such amounts from the covered institution; and

53.4 the covered institution shall comply with any direction of the Minister concerning its business and corporate structures and shall draw up a restructuring plan within six months of any such payment under the guarantee. Any such restructuring plan shall be notified to the European Commission and shall comply with EU State aid and competition law.

ANNEX

Guarantee Charging Model

The objective of the guarantee charging model is to put in place a sound, transparent and quantitative mechanism to remunerate the State appropriately for the financial cost and risk of granting of the guarantee provided to covered institutions. The model facilitates the adoption of a risk-adjusted basis based on objective criteria to distribute the charge and is intended to be aligned with the maintenance of the long-term viability of the covered institutions in view of the central importance of the banking system to the Irish economy overall.

The assessment of the guarantee charge is primarily based on the estimated increased funding costs for the Exchequer from the provision of the guarantee. Funding costs of Government Debt as a result of the guarantee are assumed to increase by between 15 and 30 basis points or 0.15% to 0.30% over time.

This approach is informed by the difficulty in determining a market rate for a guarantee of this nature and dimension in the absence of comparable benchmarks and taking into account the potential difficulties in the current circumstances for beneficiaries to bear the amounts that might be estimated should be charged particularly given that in normal economic and financial circumstances, the need for such a guarantee would not arise. The charge for the provision of the guarantee is therefore based on the Government funding costs on the basis that it comes as close as possible to what could be considered an appropriate price in the current financial environment. There is currently no indication that funding costs for the covered institutions have declined on account of the provision of the guarantee.

The model adopted for calculating the distribution of the guarantee charge for each individual covered institution is expected to be based on long-term credit ratings which reflect the risk profile of individual covered institutions. The pricing guarantee mechanism is, therefore, intended to reflect the varying degree of risks and the beneficiaries' different credit profiles to ensure the proportionality of the measure.

It should be noted that in circumstances where the guarantee is activated and a payment is made the legislation governing this Scheme requires that the financial support provided shall so far as possible ultimately be recouped from the covered institution or subsidiary to which the support was provided. In addition it is stated Government policy that where there is a shortfall for the Exchequer, this will be recouped from the covered institutions over time.

The aggregate quantum of the guarantee charge was also determined on the basis of a "going concern" assumption and an assessment of the percentage of total profits of the covered institutions which could be levied consistent with required capitalisation levels as well as the need to support investor and debtor confidence in the Irish banking system overall.

While it is possible, in theory, to estimate a commercial market price for the charge it is important to stress that such estimates are based on a number of important assumptions that do not hold in general or in particular in the current dislocated financial market environment.



GIVEN under my Official Seal,
20 October 2008

BRIAN LENIHAN,
Minister for Finance.

EXPLANATORY MEMORANDUM

Relating to a Scheme

entitled

CREDIT INSTITUTIONS (FINANCIAL SUPPORT) SCHEME 2008

(This memorandum is not part of the Instrument and does not purport to be a legal interpretation)

1. Introduction

The Minister for Finance, having consulted with the Governor of the Central Bank (the Governor) and the Regulatory Authority, has made a scheme (the Scheme) pursuant to Section 6(4) of the Credit Institutions (Financial Support) Act 2008 (the Act).

The primary purpose of the Scheme is to maintain, in the public interest, the stability of the financial system in the State and to provide financial support to certain credit institutions or subsidiaries of credit institutions operating in the State (covered institutions).

The Scheme gives effect to the guarantee declared by the Minister on 30 September 2008. Covered institutions will be specified by an order of the Minister and will be required to execute a guarantee acceptance deed within a specified timeframe in order to join the Scheme. Once a covered institution has executed a guarantee acceptance deed, it will be subject to the terms and conditions of the Scheme, as described below, including the requirement to pay a charge to the Exchequer for participating in Scheme.

In making the Scheme, the Minister has had regard to the fact that:

- there is a serious threat to the stability of credit institutions in the State generally, or there would be such a threat if he did not provide the financial support;
- the provision of the financial support to an institution faced with financial difficulties is necessary, in the public interest, for maintaining the stability of the financial system in the State; and
- the provision of the financial support is necessary to remedy a serious disturbance in the economy of the State,

and has taken into account:

- the extent and nature of the obligations (including degree of control over possible abuse of the financial support) which need to be undertaken by the State in relation to financial support; and
- the resources available to him in respect of the financial support,

and is of the opinion that the Scheme is necessary, appropriate and proportionate to achieve the objectives of the Act in the public interest.

As part of the Scheme, the Minister will stand as guarantor of the covered liabilities of a covered institution in accordance with the terms and conditions of the Scheme for the period from 30 September 2008 to 29 September 2010 inclusive.

No call can be made under the guarantee after 29 September 2010.

The Scheme sets out an enabling framework which equips the Minister to take such action as is necessary to achieve the objectives of the Act. The functions provided to the Minister and the Regulatory Authority under the Scheme focus on the appropriate management of risk in the covered institutions with a view to progressively strengthening the financial system in preparation for the expiry of the Scheme on 29 September 2010.

In accordance with the provision of section 2(2) of the Act, the Minister will consult with the Governor and the Regulatory Authority in the continuing performance of the Minister's functions under the Act and this Scheme in order to ensure that appropriate co-ordination and co-operation takes place.

2. Purpose

The Scheme has been made by the Minister having regard to the following principal objectives:

- Maintaining financial stability in the best interests of the public and the economy of the State;
- Remedying a serious disturbance in the economy by safeguarding the financial system of the State and the economy of the State from the threat caused by the unprecedented turmoil in the international financial markets and the particular macro-economic conditions in the State;
- Providing lasting systemic stability in the banking system and ensuring its long-term sustainability;
- Preventing abuse of the guarantee;
- Ensuring compliance with the requirements of EU State aid and competition law; and
- Minimising the potential cost to the Exchequer and taxpayers; in particular where the guarantee is called upon and a payment is made but the

financial support cannot be recouped in full from the covered institution to which it was provided, the principle is that it would be recouped in full from the covered institutions by the State over time in a manner consistent with their long-term viability and sustainability.

The realisation of these objectives will help promote sustainable lending practices that support the appropriate availability of credit and favour enterprise in the economy of the State, especially trading activities that contribute to the export of goods and services. The manner in which the Scheme is implemented is intended to support the long-term sustainability of the banking sector of the State.

The Scheme has been approved by the European Commission as being compatible with EC Treaty state aid rules.

The Scheme will be applied on an objective basis: (i) taking into account the role of each covered institution in the State's banking system and the overall economy of the State; and (ii) in a non-discriminatory fashion so as to ensure that there are no undue distortive effects on neighbouring markets and the internal market as a whole.

3. Overview of Scheme

Application

The institutions eligible under the Scheme are those systemically important credit institutions which the Minister specifies by order under section 6(1) of the Act in the exercise of his or her powers under the Act as requiring financial support and fulfilling the objectives of the Act. The Minister may consult with the Governor prior to making any such order.

Where the Minister specifies a credit institution by order, the relevant credit institution will have a limited period of time, as determined by the Minister, to join the Scheme before it loses the opportunity to join the Scheme.

A covered institution specified by order under section 6(1) of the Act of 2008 joins the Scheme by executing a guarantee acceptance deed in a form to be specified by the Minister. The Minister may also require that a parent or any other company within the covered institution's group execute a guarantee acceptance deed in respect of itself or any other company within the group.

The principal feature of the Scheme is the provision of a guarantee to covered institutions. The Scheme provides for a charging mechanism for individual covered institutions. The Scheme includes the application of strict terms and conditions on covered institutions to ensure that the public interest is paramount and that neither the covered institutions concerned nor their shareholders will be unfairly advantaged from the receipt of financial support under the Scheme.

Basis of support

The basis on which the financial support will be provided will include:

- A return to the Exchequer for the financial support provided to the covered institutions;
- Measures to ensure that any potential competitive distortion caused by financial support is minimised to the extent possible and that the covered institutions are not unduly advantaged by the Scheme;
- A framework to advance such strategic change as may be required in the financial sector of the State to ensure long-term stability when financial support under the Scheme is withdrawn on 29 September 2010;
- Additional oversight and scrutiny of the covered institutions while they are in receipt of financial support from the State, including the appointment of public interest representatives to the boards of directors of those institutions in receipt of financial support;
- Regular and detailed reporting to the Minister, via the Regulatory Authority, to ensure protection of the taxpayer and the realisation of the objectives of the Scheme;
- Controls on and oversight of the remuneration of directors and senior executives of the covered institutions in receipt of financial support; and
- Promotion of the highest standards of corporate social responsibility in the banking system overall.

Review and monitoring of the Scheme

The Minister will formally review the functioning of the Scheme from time to time, at no later than six-month intervals, to ensure that it is meeting the objectives described above and to consider the continued requirement for the provision of financial support under the Scheme. The implementation of the Scheme will be subject to close ongoing monitoring by the Governor and the Chief Executive of the Regulatory Authority.

4. Overview of Guarantee

As part of the Scheme, the Minister will stand as guarantor of the covered liabilities of a covered institution in accordance with the terms and conditions of the Scheme for the period from 30 September 2008 to 29 September 2010 inclusive.

No call can be made under the guarantee after 29 September 2010.

Covered liabilities

The guarantee provided by the Minister applies to: (a) all retail and corporate deposits (to the extent not covered by existing deposit protection schemes in the State or any other jurisdiction); (b) inter-bank deposits; (c) senior unsecured debt; (d) asset covered securities and (e) dated subordinated debt (Lower Tier 2) of covered institutions, excluding intra-group borrowing and any debt due to

the European Central Bank (ECB) arising from Eurosystem monetary operations.

For clarity, any covered liabilities held as collateral by the ECB and other Central Banks and any deposits made by the ECB with covered institutions as part of the ECB's investment operations fall within the Scheme.

The Scheme does not effect any other rights or claims of creditors.

Regulation of commercial conduct

The Regulatory Authority in consultation with the Minister may regulate the commercial conduct of covered institutions strictly in order to achieve the objectives of the Scheme. The Regulatory Authority, in consultation with the Minister, will impose conditions regulating the commercial conduct of a covered institution's business, having regard to capital ratios, market share and balance sheet growth, in order to minimise any potential competitive distortion that may arise and to avoid any abuse of the guarantee or any use in a manner irreconcilable with the purpose of the guarantee.

For example, a covered institution will be required to:

- Appropriately manage its balance sheet in a manner consistent with the purposes of the Act and the need to avoid significant distortions of financial flows;
- Put in place improved structures to ensure long-term stability of funding;
- Take steps to restructure its executive management responsibilities and strengthen its management capacity and corporate governance;
- Improve liquidity, solvency and capital ratios in circumstances where this is required; and/or
- Take such measures to minimise any risk of recourse to the guarantee.

There will be restrictions on the level of permitted growth in each covered institution's balance sheet. The Scheme contains specific restrictions on covered institutions in respect of dated subordinated debt (Lower Tier 2).

Board representation and executive management remuneration

In order to promote the public interest, a covered institution will, at the direction of the Minister, take all reasonable steps to appoint at least one but no more than two non-executive directors to its board from a panel approved by the Minister during the period of the guarantee. The Minister will also have the right to appoint persons to observe all meetings of the remuneration, audit, credit and risk committees of a covered institution.

The Minister will establish an independent committee called the Covered Institution Remuneration Oversight Committee (CIROC) comprising three

members appointed by him or her to oversee all remuneration plans of senior executives of the covered institutions. Each covered institution will prepare a plan to structure the remuneration packages of directors and executives so as to take account of the objectives of the Act. Such plans will cover, *inter alia*, executive bonuses including share options, if any. Bonuses will be measurably linked to reductions in guarantee charges, reduction in excessive risk taking and encouraging the long-term sustainability of the covered institution.

Each covered institution will submit a report to CIROC, no later than six weeks after the relevant covered institution joins this Scheme, demonstrating how its remuneration policies for the year ahead will comply with the requirements as to remuneration in the Scheme. CIROC will prepare a report for the Minister, within 3 months of receipt of such covered institution's report, making a recommendation where appropriate on compliance by the covered institution with the terms of the Scheme. Where the Minister considers, on the advice of CIROC, that the covered institution has not complied with the requirements of the Scheme, he or she may direct the covered institution to amend the remuneration plan so that compliance is achieved.

A covered institution will not be permitted to enter into any contractual arrangement that provides for termination compensation or equivalent to be payable to any director or executive for the duration of the Scheme.

5. Charge

The covered institutions will pay a charge to the Exchequer for the guarantee, which is summarised in the Annexe to the Scheme.

The main principle is that the Minister will estimate an aggregate cost that the State will bear, and each covered institution will pay its share of the cost reflecting its risk profile, calculated on an individual basis. If the actual cost for the State is higher than the estimated aggregate cost, the charge will be adapted accordingly over time.

By entering into a guarantee acceptance deed, a covered institution and in certain circumstances a group company party to a guarantee acceptance deed, will agree to pay the quarterly charge as detailed in the Scheme.

By entering into a guarantee acceptance deed, a covered institution will agree to indemnify the Minister in respect of any payments made, or costs incurred, by the Minister in respect of the Guarantee.

6. Subsidiaries

The covered liabilities of a subsidiary of any parent credit institution which is not regulated by the Regulatory Authority (being a subsidiary which is a covered institution) will include only such covered liabilities of that subsidiary: (i) which relate to its own business; and (ii) in respect of which there is no recourse to any other entity within or outside its group and will not include liabilities which, in the absence of the guarantee, would normally be those of other members of the covered institution's group.

The Minister may impose specific obligations under the Scheme or the guarantee acceptance deed given by the covered institution or its parent, any subsidiary or any group company to appropriately ring-fence the activities of a covered institution from its parent to minimise the covered institution's financial exposure to its parent credit institution.

7. Branches

Under the Act it is open to the Minister to enter into a guarantee arrangement with any credit institution in the EU. The guarantee or indeed financial support generally under the Act is therefore, in principle, available to systemic branches (e.g. those with a significant retail customer presence). If the need for such a safeguard arose, a guarantee could be extended to a systemic branch in the context of a financial stability issue and in that context the Minister would apply the same principles as contained in the Scheme and the Act as much as possible taking into account that the absence of a distinct legal personality requires a different approach. Individual agreements would most likely be required under the Act to address the specific issues that would arise in seeking to guarantee a branch operating in the State.

8. Regulatory Supervision

The Regulatory Authority has advised the Minister that in light of the severe difficulties faced by credit institutions arising from the crisis of confidence in the global credit market, it will continue to intensify its on-site and off-site supervision of credit institutions. This will build on revised capital and liquidity measures introduced by the Regulatory Authority during 2006 and 2007. The Regulatory Authority will focus on liquidity requirements, capital adequacy, risk management, balance sheet structure and corporate governance. This may involve setting additional regulatory ratios as appropriate in order to reduce the risk in the balance sheet, reflecting the current domestic and global conditions.

In addition, the turmoil in global financial markets has resulted in a major review of the international regulatory systems. A roadmap for regulatory reform addressing the following areas is being developed:

- Enhanced transparency for investors, markets and regulators;
- Improved valuation standards;
- Reinforced prudential framework and risk management in the financial sector; and
- Improved market functioning, including the role of rating agencies.

The scope of the international roadmap of actions is comprehensive and reflects the global agenda of the Financial Stability Forum and work is progressing at international and European levels. The Regulatory Authority will apply the resulting standards and policies to State credit institutions.

The Minister will consult with the Governor and the Regulatory Authority in the continuing performance of the Minister's functions under the Act and this Scheme. This will take the form of liaison with the Governor and the Chief Executive of the Regulatory Authority as well as consultation on specific prudential aspects of the terms and conditions of any financial support provided to a covered institution under the Scheme, in order to ensure a consistent approach by reference to the objectives of the Scheme. In parallel with this, the Regulatory Authority will continue to perform its functions under existing law in relation to any credit institution.

The Minister may, as a condition of providing financial support to a credit institution or subsidiary under the Scheme, require a covered institution to fulfil the requirements for the time being imposed by the Regulatory Authority under its statutory powers (including those in relation to the conduct of its business and its competitive behaviour) and to continue to do so.

The Scheme forms part of an integrated response to the current financial instability from the Government, the Minister, the Governor and the Regulatory Authority. The guarantee of key liabilities of the relevant covered institutions is designed to remove any uncertainty on the part of counterparties and customers of the covered institutions, and will be coupled with continuing, appropriate scrutiny of covered institutions by the Regulatory Authority.

Glossary

As used in this Explanatory Memorandum:

“asset covered securities” means asset covered securities issued by credit institutions designated under the Asset Covered Securities Act, 2001 and the Asset Covered Securities (Amendment) Act, 2007 or other covered bonds.

“corporate deposits” means deposits made with a credit institution by a corporate entity. Such deposits can include certificates of deposit, as well as cash.

“dated subordinated debt (Lower Tier 2)” means subordinated debt, such as a subordinated loan or a subordinated bond, which ranks after unsubordinated debt (i.e. senior debt) should a credit institution be wound-up. The dated element relates to the fact that the debt has a specific life span, for example a subordinated bond with a maturity of 5 years, as opposed to a “perpetual” debt that has no fixed maturity. The Tier 2 element refers to its classification for regulatory capital purposes.

“EU State aid and competition law” means the competition and state aid rules pursuant to Articles 81 to 89 of the EC Treaty.

“guarantee” means the guarantee provided by the Minister pursuant to the Scheme in respect of the deposits and certain other liabilities of named credit institutions.

“financial support” means a loan, a guarantee, an exchange of assets or any other kind of financial accommodation or support provided pursuant to section 6(1) of the Act of 2008.

“interbank deposits” means deposits made with a credit institution by another credit institution. Such deposits can include certificates of deposit, as well as cash.

“retail deposits” means deposits made with a credit institution by individuals.

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