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AN COMHCHOISTE FIOSRÚCHÁIN I DTAOBH NA GÉARCHÉIME BAINCÉI-REACHTA

JOINT COMMITTEE OF INQUIRY INTO THE BANKING CRISIS

Déardaoin, 18 Meitheamh 2015

Thursday, 18 June 2015

The Committee met at 09.30 a.m.

MEMBERS PRESENT:

Deputy Pearse Doherty,	Senator Sean D. Barrett,
Deputy Joe Higgins,	Senator Michael D'Arcy,
Deputy Michael McGrath,	Senator Marc MacSharry,
Deputy Eoghan Murphy,	Senator Susan O'Keeffe.
Deputy Kieran O'Donnell,	
Deputy John Paul Phelan,	

DEPUTY CIARÁN LYNCH IN THE CHAIR.

to you just quite as easily, you know. And that's the kind of culture change I'm taking about ... that's the kind of culture change I was talking about earlier you know. It was mentioned, and I mean it's only testimony - I look like I actually watched all of Kevin's testimony this morning, but I ... I was kind of just picking up documents and stuff like that over in the thing - you know he made reference to the fact that civil servants expect to be kept waiting four hours for a meeting. That shouldn't be happening.

Senator Sean D. Barrett: Was it necessary ... you don't like the split in the Department you say, was it necessary though to do that, to have two Ministers for Finance at a Cabinet?

Mr. John Moran: I think it worked very well, I mean let me be clear. I think that during the period of the crisis that worked very well, but where it is necessary, and I'm not saying you have to put it back together, I'm saying it would be useful to analyse that scenario to make sure that there is an infrastructure, or a forum or whatever it is, that allows what used to happen before within one Department, one Minister, one Secretary General who actually had a much greater understanding of the whole thing, to be able to do it. And the example I gave in my written statement was the housing sector, because that's what you've been looking at. We have housing sector problems at the moment, we've had them for two years, they're what I was talking about when we were talking about repossessions stats. But it's split up all over the place, some of the banking stuff is in the Department of Finance, some ... how do you bring all that together in the current structure, that's just what I was saying in terms of finding a way to do that. And maybe the separation, which is contrary to the Wright report, is actually not a good idea - but I'm not saying it can't continue, you can find an alternative way of making sure that you understand that's there, and bringing it together.

Senator Sean D. Barrett: Thank you very much. Thanks, Chairman.

Chairman: Thank you very much. I'm going to bring matters to a conclusion and in doing so I'll be thanking Mr. Moran for his contribution today, but I want to invite you to make any final comments or remarks that you'd like to make before we conclude, Mr. Moran.

Mr. John Moran: No, I think given what I just said about keeping somebody four hours I am conscious that my successor is probably standing outside the door for the last maybe quarter of an hour longer, I probably should leave it there. I think I've said enough.

Chairman: Okay, thank you very much. With that said I'd like to thank Mr. Moran for his participation today and for his engagement with the inquiry. In doing so the witness is now excused. I don't want to suspend the meeting for a moment, I want to go into private session just to deal with some time management issues to see where we're going to go for the remainder of the evening. So, if I can just facilitate the excusing of Mr. Moran from the room and if we can just come back very, very briefly into private session, we'll see where we are for time management for the remainder of the day. Thank you.

Sitting suspended at 6.12 p.m. and resumed in private session at 6.15 p.m. Sitting suspended at 6.20 p.m. and resumed in public session at 6.39 p.m.

Department of Finance - Mr. Derek Moran

Chairman: So I'm calling the meeting into public session. Is that agreed? Agreed. The Committee of Inquiry into the Banking Crisis is now resuming again in public session and, as

I've said, I'll be asking those members and those in the public Gallery to ensure their mobile devices are off.

Today we continue our hearings with the senior officials from the Department of Finance who had key roles during and after the crisis period. At our present session we will now hear from Mr. Derek Moran, current Secretary General at the Department of Finance. Derek Moran has worked in the Department of Finance since 1989, from July 2003 to July 2014, he was an assistant secretary to the Department while his responsibilities, where his responsibilities included the budget and economic division, the tax policy division, the fiscal policy division and human resources. He was appointed to the role of Secretary General in July 2014.

Before hearing from the witness, I wish to advise the witness that by virtue of section 17(2)(*l*) of the Defamation Act 2009, witnesses are protected by absolute privilege in respect to their evidence to this committee. If you are directed by the Chairman to cease giving evidence in relation to a particular matter and you continue to do so, you are entitled thereafter only to a qualified privilege in respect of your evidence. You are directed that only evidence connected with the subject matter of these proceedings is to be given. I would remind members and those present that there are currently criminal proceedings ongoing and further criminal proceedings are scheduled during the lifetime of the inquiry, which overlap with the subject matter of the inquiry. The utmost caution should be taken not to prejudice those proceedings. Members of the public are reminded that photography is prohibited in the committee room. To assist the smooth running of the inquiry, we will display certain documents on the screens here in the committee room. For those sitting in the Gallery, these documents will be displayed on the screens to your left and right. Members of the public and journalists are reminded that these documents are confidential and should not publish any of the documents so displayed. The witness has been directed to attend this meeting of the Joint Committee of Inquiry into the Banking Crisis. You have been furnished with booklets of core documents. These are before the committee, will be relied upon in questioning and form part of the evidence of the inquiry.

So, with that now said, if I can now call on the clerk to administer the oath to Mr. Moran.

The following witness was sworn in by the Clerk to the Committee:

Mr. Derek Moran, Secretary General, Department of Finance.

Chairman: Thank you Mr. Moran once more and if I can invite you to make your opening remarks to the committee please.

Mr. Derek Moran: Chairman, thank you very much. I don't propose to go through my witness statement, I'm going to keep it through to four or five minutes. I think everybody will be probably grateful for that. The first few comments just basically on two topics, one, on the advice the Department gave pre-crisis, and, secondly, on whether we're in any better position than we might have been then in terms of dealing with future challenges.

It's a notable feature of all the reports to date, Wright, Nyberg and so on, that they find the Department did warn on the adoption of inappropriate macro-fiscal policies. It's equally notable in all the reports that they're critical of the Department for not, for either not heightening the tone of that risk or for linking fiscal and, and, and the financial properly. As I said in my witness statement, this is fair and accurate comment. Nonetheless, warnings were given, and to quote Wright, they were "more direct and comprehensive than concerns expressed by others in Ireland, or by international agencies".

It's also true that external bodies, such as the IMF, warned of the same risks and on occasion in some detail. But as time went by, the narrative tended to soften, commending Ireland, for example for impressive economic performance, and prudent fiscal policy by the IMF or, or citing Ireland as an exemplar of compliance with the Stability and Growth Pact, the EU Commission. And the context here for these international bodies is important. It has to be ... remember that time, and I'm talking about 2005, 2006, Ireland had been growing consistently for a very long period of time and the budget was either close to balance, in surplus and the debt ratio was a low, only around 25% of GDP. These were very impressive headline numbers by international standards at that time.

If we take a step back a bit, in the mid to late 1990s, the objective of Government policy was very clear: run a budget policy that was sufficiently tight to qualify as a founding member of the single currency. You can see this in the numbers. Spending in '97 and '98 were lower than they were at any time for the next decade and the budget started to run a surplus in '97 at 1.3% and growing to about 2.6% by 1999. The introduction of the Stability and Growth Pact at this time was all about governments appropriately managing their key remaining policy lever in EMU, fiscal policy, as monetary policy moved from domestic central banks to the ECB.

The Department advised, from about the start of the last decade, that it was necessary to create a buffer against risks, including from about 2003 onwards ... over-reliance on housing sector. It's important to be clear about what that means. It means telling the Government of the day it should not allow spending to grow or tax be reduced by as much as they might want. In technical terms, run counter-cyclical rather than pro-cyclical policies. While this isn't an easy message, it's one that the Department must deliver. On housing, notwithstanding the warnings, we did not conceive a collapse to the magnitude that actually happened, and I think we have to say that upfront.

It is unfortunate that if you constantly predict a recession year after year and it doesn't happen, then you run the risk of the advice you're giving becoming sort of a debased currency. In the end, it's probably the role for Government to make policy decisions, having considered all the advice given to it. And the failure to run tighter budget policies had profound consequences for the public and for the public finances. Had tighter budgets been adopted in the early and middle of the last decade, it would've reduced significantly the need for very painful expenditure cuts and tax increases during the crisis resolution period.

In terms of the second piece, I think it's better now. Do we have better systems? Have we learned lessons? I believe an answer ... on balance, the answer is "Yes". I think we have ...always have to be aware that systems and processes need to be continually evolved if they are to remain (a) relevant and (b) effective. In terms of external macro-fiscal surveillance, we know that prior to the crisis, the EU Stability and Growth Pact was not sufficient to meet the task. The changes to the pact have been very significant. Its principle elements are enshrined in domestic and constitutional law in member states. It has become much more automatically enforceable - it has real teeth. In many respects, you are now presumed guilty until proven innocent under the revised framework. It is very difficult to under ... overturn a recommendation for action for a member ... to a member state from the EU ... from the Commission. The improvements in the European economic and fiscal governance arrangements over the last number of years should result in the earlier detection and warning of emerging vulnerabilities and the enforcement of earlier action, either by European authorities or by individual member states, as the case might be. These changes are important and to be welcomed.

Domestically, we've also put in place improvements - budgetary rules have taken on a much greater significance than those that applied before the crisis through a target for the structural balance, complemented by an expenditure benchmark. The expenditure benchmark helps illustrate room for manoeuvre available to Government in setting its annual budget. This was presented for the first time in the spring economic statement this year and it's the first time that we have publicly available, six months before a budget, a range of, of room for manoeuvre that's available now for public and commentator and political debate. The advent in the independent Fiscal Advisory Council is another voice charged with specifically overseeing and endorsing the official economic forecasts and comments on the status of policy. They have embraced that role and their independence and, again, this is to be welcomed.

Extensive changes have been made in the organisation of the Department. These are aimed at ensuring the Department has the capacity to do its job and relate properly to its stakeholders. We've increased the publication of technical studies, policy reviews and other relevant papers. We've entered into a research partnership with the ESRI, whereby members of the institute and the Department work together on a number of fiscal and macroeconomic projects. Engagement with the stakeholders, think-tanks and other experts can only improve the quality of advice. We've also participated in a number of public consultations, as the Department, including, for example, on macro-prudential rules, the Low Pay Commission and agricultural strategy.

Many of the other changes in the organisation flow directly from the Wright report. These include: structures to handle corporate affairs; professionalisation of HR; improved communications; cross-divisional work; and so on. We've also, for the first time, formally codified our governance structures and processes in a single document. From my point of view as the Secretary General, there's no fixed target for improving the Department - it's a process. It should be ongoing and continually challenge the organisation to be the best it can be and, where we can, benchmark our performance against others.

Thank you, Chairman, committee, for your time and attention and I hope my contribution will be of some assistance to the committee in its work.

Chairman: Thank you, Mr. Moran, for your opening remarks and if I can commence questioning and invite Deputy Michael McGrath first. Deputy.

Deputy Michael McGrath: Thank you very much, Chair, and you're very welcome, Mr. Moran. Sorry for delaying your evening with the late start. Can I start by asking if you were aware of any contrarian voices or contrarian views inside the Department of Finance in relation to property inflation issues or the issues in the banking system and would you want to elaborate on that?

Mr. Derek Moran: Yes, I mean, in terms of ... I mean, the nature of economics is that it is a, sort of, discursive, collaborative discipline. And, you know, the process that we go through to develop a view of the economy would include discussions across the range of people feeding into the overall view of the macroeconomy. And that would've taken on board very, very different views and it would've ... in the end of the day, you had to come down and develop a central forecast, I suppose. We can only publish one set of forecasts, one view of the economy and that has to be credible to both the external accommodators, to the markets, to the rating agencies and so on. And, I think, during that period, whether we were right or wrong, they were. So, dissent ... or ... or contrarian views, you know, are accommodated within that, sort of, dialogue that goes through the process. We also, I mean ... I mean, within any organisation, I think, where people might have profound difficulties they have opportunities to talk to more senior people, or we used to run each year this, sort of, annual review where the staff met the entire management team and were afforded an opportunity to give their views directly, if they felt they needed so ... so I think we had in place procedures and processes that allowed an appropriate discussion, particularly of the ... of visions around housing and construction and so on.

Deputy Michael McGrath: And I suppose a related question to that would be if somebody below the level of Secretary General or below the level of assistant secretary held quite a strong view which was contrary to the overall view of the Department; was there a mechanism put in place, and is there one now, for that view to be channelled to the level of the Minister so that at least the Minister would be aware: "Look, okay, this is the overall view, but just to make you aware, somebody at a less senior level has quite a different view and we want to make you aware of that"?

Mr. Derek Moran: In terms of, I mean, just within the institution, the door was always open for anybody who wished to make those arguments. Within the institution, there was always the opportunity to articulate that to a more senior level, including collectively in those sessions. But I think the Department's responsibility, ultimately, is to give the ... the Minister the complete view, if you like, the view of the Department, on balance, of the likely prospects.

Deputy Michael McGrath: Okay.

Mr. Derek Moran: So I think the answer is that, you know, people going with their different views to the Minister, no. How do we accommodate that now? We have ... we tend to take major policy issues, including the economic forecast, the economic outlook, to what we call a policy committee, which is a peer review committee within the Department. And we've broadened that over time, not to just be about sections or divisions bringing their policy initiatives for peer review, but to allow horizontal groups of people to bring it in, in terms of cross-divisions, but also importantly, I think, and it's to deal with the sort of situation, among other things, Deputy, that you're referring to, if an individual wants to do it, they can bring their views forward and, sort of, have them peer reviewed, you know, among peers at that fortnightly meeting.

Deputy Michael McGrath: Okay.

Mr. Derek Moran: So very conscious of having a mechanism in which you can do that.

Deputy Michael McGrath: Okay. Given the Department's primary role in terms of fiscal policy and in light of the fact that during your tenure, you would have had considerable experience in the areas of taxation and budgets, can I ask you to comment on the fact that cyclical taxes, including stamp duty, corporation tax, capital gains tax, rose as a percentage of total revenues from about 8% in 1987 to 30% in 2006, and towards the years leading to 2006 a greater acceleration in the growth in the overall percentage of such taxes? How did the increasing reliance on cyclical versus more stable taxes impact on fiscal policy?

Mr. Derek Moran: I mean, the impact ... the impact was profound to the extent that ... first of all, I'd be less concerned about corporation tax as a cyclical tax, because it went up-----

Deputy Michael McGrath: Yes.

Mr. Derek Moran: -----but it was still always ... it was always a very substantial contributor to-----

Deputy Michael McGrath: The reports seem to include corporation tax as one.

Mr. Derek Moran: They do, and, you know-----

Deputy Michael McGrath: Which is debatable.

Mr. Derek Moran: -----which is debatable.

Deputy Michael McGrath: It's debatable.

Mr. Derek Moran: It's debatable. In terms of capital taxes and stamp duties, they went from being 2% or 3% of total revenue-----

Deputy Michael McGrath: Yes.

Mr. Derek Moran: -----to maybe 16% each ... to maybe 16% of total. And the big difficulty was ... ultimately, is that those cyclical benefits, which were transitional and based on transactions, they weren't permanent, there was no underlying ... it's not like income taxes, it's not like corporate tax, it's not like VAT, there's no underlying element to it, they were basically transactions, and once those transactions stop, the money goes. But permanent decisions weren't being made on the back of those transitional ... of the transitional taxes ... that tax relief, tax relief or tax reductions were being made on permanent expenditure increases based on that windfall that came each November from those taxes. So it had a profound effect.

Deputy Michael McGrath: And did the Department sufficiently highlight the risks associated with that strategy to the decision-makers, to the Government of the day?

Mr. Derek Moran: I mean, I ... the Department's approach to this consistently was to recommend probably during the height of the boom no more than indexation of both expenditure and of ... of the tax system, you know, kind of, fairly modest in the context ... increases in ... increase in one and reduction in the other. And that was at the heart of it, about this risk.

Deputy Michael McGrath: Yes, but in terms of the mix of the revenue base? I mean, the Department on fiscal policy can point to budget strategy memos every June, and, typically, the actual budget and the outturn exceeded that. But on the issue of the dependence within the revenue base on transaction-based taxes, and the growing dependence in the early 2000s and mid-2000s, is there sufficient evidence, in your view, that the Department raised those concerns, took them to the level of the Minister, and highlighted the extent of the risks that were being built up because of that dependence?

Mr. Derek Moran: I think at the macro level, it is true to say that we were highlighting the risks, at that micro level of tax head, probably not sufficiently so, Deputy.

Deputy Michael McGrath: Okay. Mr. Moran, each year the Governor of the Central Bank would issue a pre-budget report to the Minister, known as the Governor's letter. You state that these letters did not suggest that the Governor had any concerns about financial stability. Should the Governor's letters, or any other reports from the Central Bank, always be taken at face value, and not subject to challenge from within the Department, or would you put forward a different view on that? And what processes does the Department of Finance have to challenge information that it is being given by the Central Bank, including in that letter, that annual letter?

Mr. Derek Moran: I mean, it's, there's the old thing that the mandate of Central Bank is prices, and its obsession is fiscal policy, and the letter was invariably about the view of the Central Bank on, on running a tighter policy; it didn't raise financial stability issues, other than, I think, 2005, 2006, it might have mentioned concerns about credit growth at that time. In terms of the formalities, my understanding is, the Minister probably meets the Governor on the letter and the Department would brief on, on the details of that. It's, you know, we would have, there would be differences, you know, but it's always important to get other, other views. In terms of the, the financial stability, the guard dog was the Central Bank, you know-----

Deputy Michael McGrath: What was, and is, the Department of Finance's role in the area of financial stability?

Mr. Derek Moran: Financial stability is ... I mean, I think ... financial stability is a matter for the Central Bank, okay, it's their responsibility. I think the one thing that we have learned is that we have to be much more acutely aware of its importance, and to question, and be able to interrogate if we've got a concern. And I think in the period of the crisis, we, certainly, from what I was doing, I would not have been conscious that we were posing those questions, and asking those questions. Certainly in terms of the budgetary process, financial stability issues didn't arise.

Deputy Michael McGrath: And is there any sense that the Governor, in the letter, would hold back to some extent, and then, in a meeting, there might be better flow in terms of a verbal exchange and the risks might be articulated more? Like what would happen when the Governor's letter would come in, would there then be a follow-up meeting, between the Minister and the Governor, to discuss it, and go into more detail?

Mr. Derek Moran: Well, that's my understanding of what happened-----

Deputy Michael McGrath: Okay.

Mr. Derek Moran: A meeting between the Governor ... generally meetings between the Governor and the Minister, are the meetings between the Governor and the Minister, without officials. So, in terms of whether the Governor held back in the letter, or the meetings themselves, I can't give insight.

Deputy Michael McGrath: Okay. Mr. Moran, in page 5 of your opening statement, you state that in general terms, the biggest deficiency of advice prior to the crisis was not linking macro-fiscal and financial stability risks. "The Department shares that deficiency," you said. Can you advise the committee more recently what changes have you introduced to address that issue, and how, can you give us an assurance that that has now changed?

Mr. Derek Moran: Yes. I suppose, if you consider - go back to the middle of the last decade, a lot of the macroeconomic models ... dealt very effectively with impacts on the macroeconomy, but didn't link across to the financial sector. And this has been a big challenge for economics in the intervening period, but how do you make those linkages across? The ESRI is currently at an advanced stage - we would have used the HERMES model, developed by the ESRI. The ESRI are currently at an advanced stage of developing a new model which is called COSMO. I don't know what that stands for, but it's called COSMO nonetheless. It will have this capacity built into it and we're making a staff member available, a PhD student, who we have who's ... who's on special leave doing a PhD but when they come back, they go down to the ESRI and work with them on this and then when it's developed which I believe ... it finishes towards the end of this year, we'll have that capacity within the Department and somebody, you know, at a PhD level capable of using it. So, you know, we have ... in terms of the future solutions, you know, we've been sort of actively involved with the ESRI on that.

Deputy Michael McGrath: Okay. Mr. Moran, Mr. Wright in his report on the Department notes that the transfer of treasury operations to the NTMA "impaired the Department's capacity to respond to the banking crisis". There were, he went on to say, "shortages of skills in the requisite disciplines and inadequate knowledge of underlying developments in the [construction] sector". So, can I ask you for the duration of your tenure as assistant secretary, and you covered at different times, budgetary policy, fiscal, taxation roles, were you satisfied that the Department and particularly the function that you were in charge of, had the requisite skills and expertise for identifying and mitigating those key systemic economic risks?

Mr. Derek Moran: I worked in the Department up to the end of 1999 and then went off for three and a half years and did other things, sometimes, working for the Department and part of that time working for the Department of Health. When I came back in 2003, there had been a lot of change ... that very few of the personnel that I would have recognised and there was a concern at that stage about the economic capacity and that wasn't just me coming in, that was the staff themselves to be fair to them and I don't think I'd be showing any disrespect to them in that regard. Coming in July '03, I did ask them to sit down and sort of self-diagnose, you know, what are the problems they saw, what are the things that we needed to do. And among the things that they sort of came up with is ... and came back to me on is things about getting the right people and having a career path for economists within the Department, the need for training and development. If you can't buy in, if you don't have the wherewithal, the financial wherewithal to buy people in, well then develop your own people. Improved communications - I think it's hard to believe at this stage that for eight years, the economics unit in the Department of Finance was split, one in ... part of it in Mount Street and part of it in Merrion Street and in what's a discursive, you know, set of interactions, that's a very odd and unsustainable thing that some of the organisation structure, some of the economists were mixed in with budgetary policy and they needed to be separated and we used to have stronger links with the ESRI. That ... they were the sort of key things that came back and effectively, you know, over the next period of time starting in early 2004, one of the key things they had ... saw, is that we had a group of good undergraduates who had come in but we didn't have anybody more experienced to develop them and bring them along. I would have gone to Mr. McNally, who was the second secretary at that stage and said, "Listen, there are these range of concerns, you know, and we need to do something about it." And I suppose, the things that we did initially is to bring people into one location, you know, so that you could get that interaction that you'd be missing, to clarify the budgetary and the economic functions, that they weren't mixed and to have some sort of strategic plan around HR and get in the right people. So, for example, just in practical terms, went to the Central Bank and seconded an experienced economist who has since, you know, ten years later became the chief economist in the Department. We recruited a PhD from students ... somebody who was completing their PhD in Trinity at the time and brought her in. Got an experienced economist, who was finishing up tenure with the NDP evaluation unit, and bring them in, to give that core of senior experience to try develop the other people and to also take, I mean again, this thing ... and you have to remember, it's salary levels in the private sector in terms of attracting economists for much higher than they could have been in the private ... in the public sector, is to take some of our very bright younger administrative officers and send them out to UCD to do a masters in ... to bring their skills up ... to do a masters in economic science, which we did with two of them. Incidentally, having spent that money, we no longer have them. That's always the risk you take, you know, that you invest in people and they move on but it's a risk that you have to take and we continue to do. So, there was a blend of them and just a little bit later in 2005 I went on and, you know, went and recruited ten additional graduates and to try build up the capacity. So, there was a capacity issue.

Deputy Michael McGrath: So how many economists roughly in say, when you came back in in 2003 ... how many economists were in the Department and how many do we have today?

Just-----

Mr. Derek Moran: I suppose it's not about ... sorry, I'm not being smart. It's not about-----

Deputy Michael McGrath: I know, I expect----

Mr. Derek Moran: -----it's not about number. It's actually about the skills and that's what the staff themselves are saying-----

Deputy Michael McGrath: Yes, so give us the number anyway.

Mr. Derek Moran: At the-----

Deputy Michael McGrath: I know it's not just about the number.

Mr. Derek Moran: It's-----

Deputy Michael McGrath: It must be my training. Numbers tend to be important.

Mr. Derek Moran: Good ... a good accountant. You'd do well in ... anyway-----

Chairman: Ah come on, will we drive on now guys? Give us the number.

Mr. Derek Moran: The number, 2005 I ... or 2003 I can't remember. It was ten or 12, maybe, people working on the economic side. Now it's ... it's and this goes to quality. There's about 20 posts within it. But the ... the average and the vast majority of those people would see themselves as career economists rather than just somebody working in economics, you know, for a short time to move on to do something else and the majority of them would be at masters level rather than at primary degree level. So it-----

Deputy Michael McGrath: Okay.

Mr. Derek Moran: -----it's about improving the quality as well as the numbers.

Deputy Michael McGrath: Sure. Final question, Mr. Moran, and it's on the issue of the advice that the Department would have been giving to the Minister on fiscal policy and, as you say on page 8 of your witness statement, the Department did give advice to the Minister in terms of the pro-cyclical nature of budgetary policy. But then you ... you cite some of the criticisms in the Wright report:

> ...it is critical of the fact that the tone of warnings did not escalate, that warnings were given within the framework of the Budget memoranda but not much beyond that and that advice was given to the Minister orally without a record being kept. This is on balance a fair comment.

Can you just clarify what your reference to advice being given orally to the Minister is? I assume that's outside of the budget strategy memo and, secondly, the budgetary strategy memo is ... under the old budgetary cycle was around June, as I understand it-----

Mr. Derek Moran: Yes

Deputy Michael McGrath: -----and I suppose, there seemed to be a tendency from the reports I've read that that was viewed as a starting point in the budget process and that, you know, that there would be a natural increase in expectations from there to the budget. But what was the Department doing from June, when it gave that memo to the Minister, to December and all the horse trading that went on in between?

Mr. Derek Moran: The-----

Deputy Michael McGrath: So clarify the verbal advice which was given and then apart from the budget memo in June, what other steps did the Department take to put a control on the fiscal spending?

Mr. Derek Moran: The ... the reference to oral advice is ... is from Mr. Wright himself and that would have been his interviews and discussions with people within the Department ... that while there wasn't a huge written record, that the Minister would have been told and briefed orally on a regular basis. It's no more ... no more than that, Deputy. In terms of ... I mean and I think I do use the ... say it in my statement that you know, you know, the budget strategy memorandum eventually became sort of the starting point, rather than the strategy at the end point-----

Deputy Michael McGrath: Yes.

Mr. Derek Moran: -----and that, in a sense, at that point you recommended a deficit or a surplus target and a spending and a tax parameter. What was held constant in an improving budgetary situation was the deficit target and any additional money came in, that was spent. That ... that's what happened. It doesn't mean that between then and the formulation of the budget that there was nothing happening because the expenditure campaign would have ... it would have initiated the expenditure campaign and there would have been regular briefing and updating through that channel back to the Minster and through the Government about progress on that. So the pressures would have been identified. And the pressures are twofold. I mean, let me be clear about that. The pressures on the expenditure side were overruns on the current year that inflated the base even further from the starting point and additional policy initiatives. And those things would have rolled up over the period. And it was one of those things with a December budget and with a November flow of revenues that came from the cyclical taxes going back to our earlier point, it allowed very late decisions to spend more and to tax less, and goes back to the point, based on largely transitional revenues.

Deputy Michael McGrath: Thank you.

Chairman: Deputy Kieran O'Donnell.

Deputy Kieran O'Donnell: Thank you, Chairman. Welcome, Mr. Moran. Sorry for detaining you. During his hearing in the context phase of this banking inquiry, the well known economist - we are talking about economists - Professor John FitzGerald said:

> There was a culture change in the Department of Finance in the last decade. It became more concerned about the politics of things and less interested in the technical detail. I would like to have had less interaction.

Would you give us your own views on those comments?

Mr. Derek Moran: Yes, I know Professor FitzGerald quite well and I think if you take, I'll come back to those comments ... if you take his overall ... he did say that the people that they dealt with on a regular basis that the interactions were very positive, that the Department made good technical contributions to it and we understood the relative roles and that would have been a lot of my dealings. And I mean, this is ... I mean, I got the sense in reading the extracts from his testimony that this centred around a couple of interactions that we had, I think, a combination of "Nervous Nellie" and - what was the other one? - and "Grumpy", and we are still looking for them within the Department. It's ... the Department's a big organisation. I don't know about the politicisation, I'm not sure that it's a fair comment, you know. I mean, certainly ... I know in the preparation of the 2006 medium-term review, there would have been a round-table meeting between the ESRI team doing it and the Department's team in terms of back and forth and iteration and an input into that. Some of the tension seemed to be over some commentary about the possibility that the capacity to increase corporation tax and on the front-loading of the capital programme. But certainly it wasn't my experience and I've always found that I had a very sort of healthy interaction ... but I mean they're Professor FitzGerald's views and I respect them.

Deputy Kieran O'Donnell: He's talking over a ten-year period which really is from, I suppose, 2004-2005 on, which was the period in which you came back. You came back to the Department in 2003. We won't associate you with the change, right-----

Mr. Derek Moran: All right, thank you.

Deputy Kieran O'Donnell: -----but did you find when you did come back like, what's the ... like when your officials in the Department are ... in terms of their actual terms of reference and what they do, how much of a lead do they take from the Minister of the time and the political aspects that that brings as well, Mr. Moran?

Mr. Derek Moran: It's a very ... it's a difficult question. I suppose that styles get embedded, particularly where you have, effectively, the same Government over a very prolonged period of time, you know, and that, perhaps, can influence the way people think and behave; there's a consistency or a constancy. But I think at the individual, official level, to be honest, there has to be healthy tensions between different commentators and the Department. I think that's the way it should be ... that there are some times - and I give a personal view on this - that the Department relies on independent institutions saying things that possibly the Department can't say in its role. And members here will know that when officials come in to committees, they can't comment on the merits, or otherwise, of policy, you know. And that's the way the system operates, that's the way the parliamentary and democratic system operates. So, therefore, in my view, it is very, very important that you have other voices saying things that perhaps you can't say. So, I-----

Deputy Kieran O'Donnell: But I suppose in your time in the Departments in the last ten years, were there occasions where you felt that a certain course of action should have been proceeded, on a technical basis, and you were overruled on a political basis?

Mr. Derek Moran: I mean it's ... civil servants of their very nature, you know, give advice, and you know, the Minister of the day can accept or reject that advice, you know, because they have an electoral mandate and they have other people advising them and so on. And that's the nature of what we do, and it's unlike, I think, other jobs to the extent that that's what you do. You advise, if it's accepted, fine, you implement it. If it's not, fine, you implement it.

Chairman: So it's not actually overruling; it's-----

Mr. Derek Moran: It's not. It's making it ... it's ... policy making rests with the Minister and the Government.

Deputy Kieran O'Donnell: Can you remember any occasion where you disagreed with the contents of the pre-budget letter from, we'll say, the Governor of the Central Bank, that was sent to the Minister for Finance between '02 and '08? Obviously I'll make that '03 and '08.

And were there challenges within the Department of Finance to these pre-budget letters that were received from the Government?

Mr. Derek Moran: I can't recall, Deputy, to be honest.

Deputy Kieran O'Donnell: You can't recall. You refer in the statement in the Wright report and its findings that the Department did warn against the adoption of inappropriate policies, although not as forceful as it should have been. During your tenure as assistant secretary from July 2003 up to the banking crisis, were any internal analyses undertaken on the growing dependency on property-related tax revenues? Was the matter discussed at management board level? If so, how frequently, and what was the general outcome? Now, I note in your presentation that you do make reference to it on page 10, where you make reference to that you did carry out a report. The question I suppose I'm asking is twofold. Your model was based around that if there was a ... so many ... a 50,000 unit fall in housing output, would give arise to €1.7 billion, how is it we did not model a much deeper collapse than actually happened? So, I suppose what I really want to ask you there is, the type of sensitivity analysis you did there, why wasn't it more in-depth? And, I suppose a kind of, a related area that I ... I suppose, that you might deal with as well, is that when you were looking at that were attempts made to quantify the effects of a soft landing and what impact this would have on Government finance in terms of loss of revenue, increased expenditure? What advice was Government given in this regard? And I'm basing ... because so much was ... of the revenue, was coming in around property.

Mr. Derek Moran: In terms of ... start with ... with soft landing. We would have ... and I know Mr. McCarthy's with you next week who'll, you know, kind of, technically be able to take you through it much better than I ... than I will.

Deputy Kieran O'Donnell: We want to ... we want a practical input from you as well.

Mr. Derek Moran: All right, I'll try and make it as practical as possible. From December '04 onwards, and that would be in the projections we produced for the '05 budget, we started to build in projections for a fall in housing output. And the economics and the projections going forward and the tax revenues around that would have ... would have been ... so, for example, we would have set out in ... for the '05 budget, assuming that 80,000 output. It didn't quite come in at that at the end of the year, because we were doing this before the end of the year. And that would fall to 76,000 in '05 and fall to about 62,000 by '07, so that's about a 22% phase drop. And that's the point at which we started building that through the ... so we were modelling and feeding that ... that through the projections, and that rolled on in the couple of years after that, that I would have still been there. Invariably what happened was that the output ended up being higher in the year that you first slowed it down. Then you need to go back up and calibrate, and come back down again. And, it is ... so ... so, we were doing that.

Deputy Kieran O'Donnell: But you would, Mr. Moran, at the time ... there would have been various bodies stating that that level of housing output was unsustainable.

Mr. Derek Moran: As were we.

Deputy Kieran O'Donnell: Yes.

Mr. Derek Moran: As were we. I mean, just be clear about that.

Deputy Kieran O'Donnell: But ... but you weren't ... the question was, were you not looking at the analysis to come in at a level that was sustainable? You were going down to 50,000 units and you said, for every 10,000 units you'd lose €1.7 billion. The question is, did you not look at levels of 25,000, 30,000, which are the sustainable levels, right?

Mr. Derek Moran: Well, sorry, the estimate of sustainable level at that was ... at that time was about 45,000-50,000, and that was the estimate. It's no longer the estimate. But that was the-----

Deputy Kieran O'Donnell: But I would have thought, if that was the average, but ... but you ... I suppose, Mr. Moran, that, did you not look at below that level?

Mr. Derek Moran: No, we didn't. And that-----

Deputy Kieran O'Donnell: Why not?

Mr. Derek Moran: I ... I think, as we went through the process, it's ... I don't know, is the answer. We-----

Deputy Kieran O'Donnell: In hindsight, should you have?

Mr. Derek Moran: Sorry?

Deputy Kieran O'Donnell: In-----

Mr. Derek Moran: With hindsight ... and, with hindsight, of course we should have, you know ... and, in that exercise that we ... it's interesting, that exercise, that we did, which was modelling the 10,000 reduction, which was a sharper reduction that we were putting into the forecasts, and informing the Minister of that. I think it was a month or two months later, the ESRI did a similar type of exercise in its quarterly review, which said if you went from 80 to 40, or 90 to 50, this is the fact ... and in point of fact, the outcome, the analysis wasn't dissimilar. We were saying that for every 10,000 there was about 0.5% to 1%-----

Deputy Kieran O'Donnell: And when you were doing the budget, on an annual basis, you'd normally, I presume, build in something into the modelling that would take account of, on a conservative basis, if there was a possible fall in housing output? What figures did you build into those budget protections? Ten thousand?

Mr. Derek Moran: Well, that's what I refer ... that's what I ... well, I mean, if you take the '05 budget, what we were talking ... and, I just ... because I have the numbers in front of me, you know, we had it going down by 18,000 over three years. So, it was a more modern ... and this was the-----

Deputy Kieran O'Donnell: That was only 6,000 per annum.

Mr. Derek Moran: Yes.

Deputy Kieran O'Donnell: Was that not, on looking back now ... was that not very, very conservative, in terms of, sorry ... I sort of ... that's not the word I'm looking ... because if it was conservative it would be a lot more ... was that not very much erring on the side of being very optimistic?

Mr. Derek Moran: In the short term it was not, because housing output actually went up in the following two years. But yes, with the benefit of hindsight, it is something deeper, something more catastrophic would have been ... I am not sure how useful, I am not sure how it would have changed the policy outlook, but we should have at least been conceiving of that as a possibility and we didn't.

Deputy Kieran O'Donnell: Okay. Can I just, one final thing Chairman? Page 9, you said, "Finance Departments are by their very nature fiscally conservative." You said, "The Department had been warning of the risks to the Budget and the economy for nearly a decade before the eventual crisis hit in 2008." How were you doing that because clearly it wasn't coming through in terms of the budgets? How were you doing that to the Ministers?

Mr. Derek Moran: We were ... I also say in it and I just look a very quick look at all the memoranda during that period and there was a range of risks highlighted. The view is that this level of growth wasn't sustainable in the long term and that it was going to ease back and that was, I mean it was through that type of forum. We continue with that, you know, it's ... I think one of the memorandum, it sort of refers to the fact that this extraordinary growth phase is now over. But in point of fact the growth phase went on and on, albeit in a different fashion, driven by domestic factors-----

Deputy Kieran O'Donnell: In the one area that was under your direct responsibility, the area of tax incentives, why wasn't the horse pulled up much earlier in terms of the incentives, the tax incentives for property? They were due to end the end of 2004, they ended up going out until four years later, 31 July 2008. How did that arise, Mr. Moran?

Mr. Derek Moran: I suppose it's ... I go back and look at the tax strategy group papers from the late 1990s and there's a series of them which raise questions. They are publicly available and they are the nearest thing to the commentary from the Department. They are already raising by '96, '97 that really the long-term future of these, they've done it and they should be reviewed and so on. It took a terrible long time to get traction on that. It was around late 2004.

Deputy Kieran O'Donnell: That was six years before they were due to end.

Mr. Derek Moran: Yes. Listen, if you are asking me should these have been ended sooner, to have a bigger impact, "Yes" is the answer.

Deputy Kieran O'Donnell: But it was an area that you would have been responsible for at the time and the review didn't start until 2005, and it was extended in the budget of 2004 by further up to the end of 31 July 2006. So finally, can you explain to me was it a political decision that the reviews didn't take place earlier?

Mr. Derek Moran: To advance any policy you have to get political traction. And I did not take over tax until the end of 2006, but certainly these concerns about the longevity of these things and the fact that they were just ... they had probably outlived their useful lives, that they were causing problems. It took time for that to get accepted with the policy of that at Government level.

Deputy Kieran O'Donnell: Would you say at the time there was lack of political will to actually look at-----

Chairman: Can you ask the question rather than state it?

Mr. Derek Moran: Yes I was going to say-----

Deputy Kieran O'Donnell: Was there lack of political will at the time to finish these schemes at the end of 2004?

Mr. Derek Moran: There is in some of the documents, I can't remember where exactly it is, that the real concern ultimately became that if you pull these quickly that you will precipitate problems in the property sector and I think that probably informed the decision as much as anything else. In other words, it became a self-fulfilling process. You pull these very quickly and you have got your very sharp downturn in the economy and I think that informed it as much as anything else.

Chairman: Thank you very much, Deputy. Mr. Moran, if I can maybe just move on to kind of a similar theme with you? You seem to indicate in your statement that for the period of 2003 to 2008, the Department was reassured by the absence of any reference in the letters from the Central Bank Governor to a slowdown in housing, and by favourable assessments from an international body such as the IMF. However, Professor Honohan states that even before the failure of Lehman Brothers in September 2008, Irish residential property prices had been falling for more than 18 months and few observers expected the fall to end soon. We also know from hearing stuff we have had with regard to the financial stability reports, that certain people that were involved in them would say that they were maybe exercises and not frighten the horses and they were maybe not as accurate a reflection as we now know. We know that Professor FitzGerald, in his engagement with the inquiry, was saying that the model that he was using for testing the economy was not measuring the level of bank exposure that was there and so forth. And then you say, on page 5 of your statement, that "In general terms the biggest deficiency of advice prior to the crisis was not linking macro-fiscal and financial stability risks ... [and] The Department shares in that deficiency." Could I maybe ask you to elaborate on that statement, referring, in particular, to the critical features of the deficiency you refer to and to the remedial steps, if any, taken since the crisis?

Mr. Derek Moran: I think I touched on ... sorry, excuse me, a good amount of this already, Chairman. I suppose at one level, there was that point in the late 1990s where the emphasis of policy perhaps moved. The separation of monetary policy going to the ECB and fiscal policy becoming a ... very much the central consideration for governments. The model that Professor FitzGerald was using, which is HERMES model, we would have used as well, which didn't have the capacity within it, you know, and there was, as I say, this ... this sense of the bank and the regulator were doing their jobs and all the external commentary sort of validated that, you know. Now, I ... I mean, I think it is a weakness in the Department that the fiscal piece and ... and the ... the monetary piece, or the credit piece, weren't joined together adequately, but I think some of it is based on this view that the job over here was being done and our job was to concentrate on this piece and that was mistaken. And we are ... you know, and I'll go back to COSMO, the unfortunate COSMO, you know, we are, you know, kind of ... having that capacity, using the structures within the Department where the chief economist is involved and chairs, for example, our housing and construction group, which involves people across the Department, you know, in a much horizontal way, improving some of the risk function in a way that we can actually get the risk function to challenge people and add the pieces together and come back to it. So, I think we've become much better at the horizontal pieces and joining those together and it's probably one of the important things that we've learned out of the crisis.

Chairman: All right. Can I maybe just move on to one other item then? You refer to the December 2005 stability programme update which warned of the economy being vulnerable to the construction sector and that the Department had concluded that reliance on construction was becoming one of the biggest risks to economic development in the country. Could I ask you to elaborate in what way, if any, the Department followed up on that warning and what response, if any, was received, especially from the Minister of the day and/or the Government and was lobbying both internally, within the system, or externally a factor in both of those regards?

Mr. Derek Moran: Yes, I mean, I think the response ... I mean, it's not a coincidence, I don't think, that around the same time there was eventually traction on the phasing out of the fiscal incentives for property. You know, no matter whether you think it was done quickly or not, you know, around budget '04 or ... it was announced in December '04 as part of budget '05 that these were to be reviewed and then, the following year, to be phased out. So, in terms of a policy response, albeit in my view late, I think that's the traction that those sorts of warnings started to get.

Chairman: Okay, and just to tidy up on Deputy O'Donnell's question there in regard to property incentives, how long is reasonable for those things? Do you think the incentives went beyond a reasonable period of time or were they ended in due-----

Mr. Derek Moran: Yes, I mean it's ... I have ... I know in the 2011 budget I tried to ... or, sorry - "I tried" - I advised the Government-----

Chairman: Yes.

Mr. Derek Moran: -----to try and cut off the legacy costs associated with that and it proved profoundly difficult.

Chairman: In what way?

Mr. Derek Moran: Sorry, it ... we produced a piece of legislation that ultimately we couldn't implement and we went out and we probably ... we should have gone to public consultation and tried to work our way through the issues and we do far more of that now. We did that in 2011, we got 700 or 800 responses to that and we found a mechanism by ... which allowed us cut off the legacy at the end. It's not an easy issue. People have vested property rights etc., etc., and you have to unwind those. So, I mean, I know from my own experience that it's not an easy journey to travel. The part ... the weakness I think ultimately in, in the ... the phasing out, and this is just ... this is my view, in the '06, '07, '08 is that, you had a decreasing amount of tax relief available, but all the way up to '08 you'd new people coming in at those lower rates and I think that was a mistake. I think it should have been phasing out with ... with no new entry. But, I think people ... you probably have witnesses who were closer to that at that time, before you.

Chairman: Okay. Thank you very much. Our next questioner is Senator Sean Barrett. Senator.

Senator Sean D. Barrett: Thank you, Chairman, and welcome Mr. Moran. The reforms that you've been introducing, indeed over your entire period from 1989 until your appointment as Secretary General, how have you addressed the perceived shortcomings in areas like fiscal strategy, for example?

Mr. Derek Moran: I mean, I spoke with ... we've been on a ... a journey in the Department, certainly in the last four or five years that, you know, kind of goes well beyond any one piece. But on the fiscal strategy piece, I think the, the ... and the real test Senator, is going to be from here forward. Since '08 we were tied into a set of fiscal targets agreed with the ... with Europe, in terms of getting the deficit, in other words we had to hit nominal deficits and so on, so it was very clear what we had to do. We went into the programme in, in 2010, that continued for three years. And at the moment, we're under what's called the preventative arm ... preventative arm, with the Stability and Growth Pact, where we have to, over the next three years, or out to 2018, get down to a balanced budget in cyclical terms. So, so we've had a map, a very clear map, over a prolonged period of time. In terms of the architecture after that, I think some of the most important things that we ... that are there are the changes in the rules but actually, the integration of those rules into what we do, and I know some people, some people weren't very complimentary of the spring economic statement, but it is an attempt to have a serious discussion about the budget that's coming in six months later. We'll have to see how the national economic dialogue in July works, in terms of actually having a, a proper dialogue around the issues. I've always been concerned ... just to be, is that ... budget day is sort of one of those once-off pieces of theatre, rather than the end to a serious dialogue around important policy, that's important to everybody.

Senator Sean D. Barrett: And budgetary policy, and sorry for rushing you-----

Mr. Derek Moran: Yes, no.

Senator Sean D. Barrett: -----a bit-----

Mr. Derek Moran: No.

Senator Sean D. Barrett: ----- what's changed there?

Mr. Derek Moran: In, sorry I?

Senator Sean D. Barrett: The changes and improvements in budgetary policy.

Mr. Derek Moran: Well, we've got the Fiscal Advisory Council which, you know, kind of, is very happy to exercise their independence and so it should. Internally, you know, we have a much stronger link between budget policy and, and an economic policy. We have ... and it works well, I think, but the separation of the Department between expenditure and tax and the ... it is risky. And we have a memorandum of understanding between us and the Department of Public Expenditure that makes it work reasonably well. So, so overall I think, both in terms of the adoption of external rules, the embedding them into a sort of a revised budgetary framework, that sort of greater professionalisation of economics, I think we've put a lot in place in terms of improving the overall budget framework.

Senator Sean D. Barrett: The relations with the Central Bank, you know that ... shouldn't your predecessors have been saying, "Hey, you know, thanks for all that advice on how to run the Department of Finance and Central Bank. If you guys stopped increasing credit at 25% a year"-----

Chairman: Ask a question, Senator.

Senator Sean D. Barrett: You know, should the advice have been two-way? Would you advise ... would you think now, monetary and fiscal policy should be integrated in a way in which they apparently weren't, leading up to the crisis?

Mr. Derek Moran: I think ... and we certainly are having a ... there is, you know, one of the, one of the legacies that we have is what we call the principals group, which is a once-a-month meeting between the Governor and the two deputy governors, senior people in our own organisation, the NTMA, where we are starting to move that, not just from a crisis management tool, but actually to something where you have those strategic ... more strategic discussions and I think that will, that has the potential to, to help us significantly into the future.

Senator Sean D. Barrett: Are the reforms assured?

Mr. Derek Moran: The one thing about rules is they're there to be gamed and the real risk is a political risk. What happens when a major European country gets themselves in trouble? How sustainable are they? And I think it's much more difficult for them to influence it, but I do ... as I say, you're now guilty until you're proven innocent. You know, you need a reverse QMV to get out, to reverse it, but I'm not ... I've been around long enough to know that these things will evolve and not always evolve in the right direction.

Senator Sean D. Barrett: And, finally, just on page 4 of your witness statement, you refer to the seconded economist from the Central Bank. How does the Department of Finance ensure the independence of a secondee from his or her previous role, say, in the Central Bank?

Mr. Derek Moran: You'll meet John next week. I don't think there's any problem with the individual. It's ... Mr. McCarthy came over in 2004 and has been in the Department ever since. He very much became one of us. We do have another economist on secondment doing specific project work at the moment in the Department and we've a fair amount of movement back and forward. I find that people throw themselves into the job that they have and those issues of conflict or ... they largely don't arise.

Senator Sean D. Barrett: And capture ... you're protected against capture you said, yes.

Mr. Derek Moran: Yes, I think so. And that's important.

Senator Sean D. Barrett: Yes. Thank you very much. And thank you, Chairman.

Chairman: Thank you very much. Next questioner is Senator Susan O'Keeffe.

Senator Susan O'Keeffe: Thanks, Chair. Mr. Moran, do you invite your staff to call you "Derek" or do they call you "Secretary General"?

Mr. Derek Moran: Yes. Derek. I don't think I've been called "Secretary General" by anybody other than in forum like this, you know.

Senator Susan O'Keeffe: Okay. All right. In your statement on page 3, you say that the Department had concerns with the tools used by the Commission for measuring the cyclical stance of the budget, seeing them as inadequate. Can you tell us over what period of time did you have those concerns and if you felt, therefore, that they were inadequate, what did you do about it?

Mr. Derek Moran: The ... what the European Commission does is that it has a single method that applies horizontally to everybody, you know, big economy, small economies; it doesn't matter which. And the model works perfectly well for a large economy. So that cyclical growth goes up and down according to cycle but the trend growth or the ... you know, is still a fairly stable number over time. When you do that for Ireland, it just doesn't work, it bounces around the place. We endeavoured ... we have pointed out, I mean, on numerous occasions, to them that this doesn't work and its results give you bizarre outcomes. And, for example, some work done by the economics division looked at in retrospect applying those rules to some of the more trenchant, deep cutting budgets of recent years and it comes up with a result that the 2011 budget was expansionary. In other words, it didn't really raise billions in taxes and cuts ... it was expansionary in those terms. And we've been engaged on ... and it's got better. Two things: the Commission are far more willing to engage now and we have made some headway in terms of getting them to adjust some other assumptions within the model and we ... but we've got more to do. And it's not clear that it'll, ultimately, work. But what happens now is that they have two. They have the cyclical measure and they have the expenditure benchmark, and it's not quite an either-or, but one can deal with the country specific issues in a ... you know, in a way that it wasn't a tool available ten years ago.

Senator Susan O'Keeffe: Just to be-----

Mr. Derek Moran: And I think they're the main changes. But we have found them much more receptive to engaging on those issues.

Senator Susan O'Keeffe: So it's a work in progress.

Mr. Derek Moran: It's a work in progress and it continues to be a work in progress.

Senator Susan O'Keeffe: Can you just be clear, though, over what period did you ... were they just when you arrived in that job or had those concerns been there? Like, what period of time are we talking about? Can you say? Or was it always this *ad infinitum*?

Mr. Derek Moran: Well, sorry, I mean, I can only talk about the three-and-a-half years there, but, certainly, we would have featured that in the ... in our submitted programme updates by way of commentary. There's a very good article by Jim O'Leary of NUIM which looks back at the assessments carried out by the Commission and the other agencies over time, and it does say in it that they couldn't have been under any illusion that the Department was repeatedly concerned about this as a measure.

Senator Susan O'Keeffe: Given those concerns, how ... why were you happy with the effectively prudent assessment that you mentioned in your statement, if then there were inadequacies?

Mr. Derek Moran: The ... sorry, these were the results that came out of it, and, you know, it's those situations .. you go into a process and the Department gives its advice, and the Government decides what it's doing. That's assessed externally and comes in as being within the parameters of ... and you start again and you say, "We think you should be tighter because ..." and you repeat the cycle but it ... I mean, "happy" is not probably a word that I'd use-----

Senator Susan O'Keeffe: But you did ... you did ... they were "effectively prudent".

Mr. Derek Moran: That's what the assessment said, yes. That's what the assessment said based on that methodology.

Senator Susan O'Keeffe: Okay ... when I think ... Deputy O'Donnell has already quoted this. On page 7 of your own statement, ''The Department had concluded that reliance on construction was becoming one of the biggest risks to economic development especially where some external shock might interact with and affect the construction sector." Now we heard from Tom Considine yesterday, who took some pains to explain how you can advise and Governments decide. So, if you were giving that advice - and you've said in your response that you were - that the Department rather was giving that advice, if you see that some of your advice is not sticking or is not being taken or is being taken in a way that isn't just quite what you thought, what were you doing then to, sort of, correct or to re-correct or to try to go, "Okay, well, if they haven't taken that advice, what are we going to do now?" Or do you just sit back and go, I'm exaggerating slightly, but do you sit back and go, "Well, they haven't taken our advice this time." How do you keep fighting that fight or did you give up? Did the Department give up and go away?

Mr. Derek Moran: I certainly didn't go away because, you know, we kept coming back and the following year and the following year and the following year. A personal view, and it can be no more than that, is I think we're very conservative in our interpretation of where the line between advice administration lies and policy lies, and how far we can go in terms of articulating publicly concerns and I think we've got better at that ... and by that I mean, and this is not because ... no civil servant will cross the line into policy; that is a matter for the Government, you know, we will not offer a view on policy; it's not appropriate. But you can inform, you can publish research, you can participate in political debate. So, I mean, I did reference that ... or not political debate, policy debate. You know I did reference in my few words at the start is that during ... since I took over we have participated in public consultations around policy decisions like the macro-prudential rules, like the Low Pay Commission etc., as the Department, not as the Minister and so on. Now to do that you have to have the support of the Minister because is to publish them in that way, and if they don't give it, then you don't but I do think that there are various ways in which we can have a say and I don't think we leveraged them terribly well in the past.

Senator Susan O'Keeffe: One last question, Chair ... again Mr. Considine when asked yesterday, we were talking about the tax breaks, the property tax breaks and he said I don't see how you could have tax incentives that wouldn't benefit high net worth individuals. We were talking about the outcome of the Goodbody report, and you've mentioned the Indecon Goodbody report. Was that ... is that your understanding? Was that what you understood? That those particular property tax breaks would, in fact ... before they were put up there, did you know that they would benefit high net worth individuals in the manner in which they were shown to have?

Mr. Derek Moran: Well, a lot of those tax breaks have been there for 20 or 30 years just be clear, you know.

Senator Susan O'Keeffe: Yes, I appreciate that, although they were extended.

Mr. Derek Moran: And tax breaks of their nature, you know ... to be relieved of tax you have to have taxable income. To invest, you have to have surplus cash to be able to invest. So, yes they, by definition, go to people with higher incomes. The interesting part was in ... you know, when they were restricted ... so was also introduced in the same budget the restriction of reliefs. The, sort of, minimum tax regime was introduced in 2006. So in other words, not only were you phasing them out but you were also restricting the capacity of people to use them, and that was brought in in 2006 as well.

Senator Susan O'Keeffe: The question was did you know?

Mr. Derek Moran: Everybody knew.

Senator Susan O'Keeffe: But to that extent, to the €6.3 billion extent?

Mr. Derek Moran: What's the €6.3 billion, sorry?

Senator Susan O'Keeffe: That was the amount that Indecon found that those tax breaks had ... the cost to the Exchequer was €6.3 billion.

Mr. Derek Moran: Over their lifetime?

Senator Susan O'Keeffe: Yes.

Mr. Derek Moran: Yes, they would have gone to people with higher incomes.

Senator Susan O'Keeffe: Okay. Thank you.

Chairman: Deputy Higgins.

Deputy Joe Higgins: Yes. Mr. Moran, in 2005, when you were assistant secretary for the budget and economic division in the Department of Finance, the Department of the environment expressed concerns at the effect of the introduction of 100% mortgages, indicating that it could give rise to serious indebtedness of households. And in response, the Department of Finance adopted the position this was a consumer matter, rather than a macro-financial stability one. Were you involved in preparing that response and on what basis was that conclusion arrived at?

Mr. Derek Moran: I wasn't involved in preparing that response.

Deputy Joe Higgins: You can't cast any light on it?

Mr. Derek Moran: No.

Deputy Joe Higgins: Okay, thank you. Mr. Moran, in the course of the bubble period, when you were in the budget and economic division and then in the taxation policy division, we have evidence in the core books - which I'm not going to take the time to put up - but of strong lobbying by construction interests and developer interests. There is an example of a letter refracted through a member of parliament from a developer and then the Irish auctioneers have a strong proposal to a committee, for example, "[opposing] any system in which individual landowners are deprived of the open market value of their land in the interest of favouring other more disadvantaged members of the community."

Chairman: Is there any way, Joe, because we just keep getting longer-----

Deputy Joe Higgins: Yes. That's Vol. 3, page 52.

Mr. Derek Moran: Of-----

Chairman: Financial, you have it.

Deputy Joe Higgins: But, were you keenly aware of the extent of lobbying and pressure by powerful construction or developer interest on the Department or on the political leadership of the Department in the course of that time?

Mr. Derek Moran: I mean, Deputy ... A routine and normal part of the annual budget cycle is that you get, in recent years, somewhere between 700 and 900 individual submissions from groups lobbying around a range of issues and this would've been one of those. It doesn't surprise me in the least. To the extent the vast majority of people that do this lobbying and make submissions don't get access and don't get a meeting with the Ministers. It was the case, up to about 2007, the Minister would've met a much wider range of groups than they do any more. They meet very, very few. It's much more selective and it tends to be the bigger, if you like to call, the social partner type groups, rather than industry ... so, does it surprise me? No.

Deputy Joe Higgins: No, it doesn't surprise me either or it wouldn't surprise anybody, I think, that there would be submissions. But, the point is, were you aware of the impact of more powerful sectors on policy?

Mr. Derek Moran: Could I pick a sector and say that, you know, that this sector got, in some sense, special treatment? Not ... no, not particularly. I mean, I would've viewed that the ... that this type of lobbying, this type of pre-budget submission, is part of the normal process of budget preparation. Indeed, on one occasion, I think it was in the '90s, these submissions were referred for examination to, I think it was the finance committee at that time, and they handed it back the next year because-----

Deputy Joe Higgins: But would you say that the tax break that Senator O'Keeffe mentioned and the extent of that which was significant, would you say that the significance of that tax break and how long it lasted, those tax breaks, and how long they lasted, could be attributed to the power of the construction and developer-led industries?

Mr. Derek Moran: Certainly, it could be. But I can't say. I can't say.

Chairman: Okay. That's fair enough.

Deputy Joe Higgins: Last question, Mr. Moran. From freedom of information and other sources, we believe that the current policy of the Department of Finance is that house prices should rise ... it would be a good thing if house prices went up. And *The Sunday Business Post*, just Sunday gone out, said that there would be a €200 million fund from the National Pensions Reserve Fund to developers in relation to new residential developments. Now in view of the nightmare our society has been through with throwing money at developers with massive house price inflation, etc, is that really the road to take? Is that ... does that indicate that we've learned from the past? And would you say, and this is my last question, that perhaps there would be an argument for thinking, to go back to the '60s and '70s model of public sector provision of badly needed housing, to sort the housing crisis that we have at the present time - would that be a lesson to learn from what we've come through?

Mr. Derek Moran: I'm not ... and I don't think I'd accept that, you know, the Department's view is house prices just should simply go up or should increase. And I think the sort of initiatives that you're talking about, which is assisting, sort of, the change in funding model for construction going forward is actually about increasing supply and taking the pressure off prices, rather than the other way round. One of the things that has happened out of the crisis is that developers can no longer 100% debt fund development. They need to find a mixture of other funding. So they might be able to raise bank loans for 60% of it but they have to have some equity input as well. And so we organised a, sort of, a conference or get-together to try to bring some of that together, to bridge that financing gap. What you're talking about in terms of the NTMA or the ISIF funding is there are certain things that developers can't get funding for, and it's looking at ... and it hasn't been launched, it's still being examined, as far as I know, at how the ISIF can get in and help with that sort of investment and get a return to the State. So it's actually more about encouraging a supply of houses to actually ease the price pressure where the demand is, rather than the other way round.

Chairman: Okay. Thank you. Deputy John Paul Phelan.

Deputy John Paul Phelan: Thank you, Chairman. Goodnight, Mr. Moran.

Mr. Derek Moran: Is it not morning yet?

Deputy John Paul Phelan: You seem ... you seem to indicate in your statement that for the period 2003 to 2008 the Department was reassured by the absence of any reference in the letters from Central Bank Governor to a slowdown in housing and a favour ... and by favourable assessments from international bodies such as the IMF. Professor Honohan, however, states that, and I'm quoting him here, "Even before the failure of Lehman Brothers in September 208, Irish residential property prices had been falling for more than 18 months and few observers expected their fall to end soon." Can you set out your Department's own assessment, if any, of the housing market at the time or did you rely primarily on the analysis of the Central Bank and other external bodies, such as the IMF?

Mr. Derek Moran: I mean, just in ... and I take it that quote from Professor Honohan is from the 2010 report, is it?

Deputy John Paul Phelan: I actually think it's a quote from his appearance here.

Mr. Derek Moran: Here, yes. I mean, I think, to be fair, and I've huge respect for Professor Honohan, that's the analysis looking back. I mean, you know, when you're in the moment, these things aren't as obvious. Perhaps they should be, based on the data available, but they're not as obvious. You know, with the benefit of hindsight and knowing what happened, you know, yes, he's right. At the time ... and incorrectly, let's ... you know, there was a broad-based consensus that, you know, that housing was going to ease back slowly. There was a view that - indeed from the Central Bank itself - that the banks were well capitalised and buffered against a slowdown and even a small fall in prices, and that was reflected in the commentary from other agencies. So they're the things that you had at the time.

Deputy John Paul Phelan: But were you relying on that analysis from other agencies rather than-----

Mr. Derek Moran: Well certainly from ... I mean, from my perspective, you know, kind of sitting, dealing with the macro and the economic as distinct from the banking, yes, you know.

Deputy John Paul Phelan: Okay.

Mr. Derek Moran: Kind of, yes.

Deputy John Paul Phelan: Did you see the evidence of Mr. O'Connell, the former chief economist with the Central Bank?

Mr. Derek Moran: I didn't. I didn't hear it but I heard about it.

Deputy John Paul Phelan: Well, he was discussing how he had been involved in the production of some country reports, particularly OECD reports, and there's just one quote - and this is my final question that I want to put to you - from him, from the transcript, from Tom O'Connell. He said:

> ... we would be discussing or interacting with the IMF and the OECD, in particular with the OECD country reports, it was embarrassing. When I used to go to Paris to … with people to look at the reports, almost every line was parsed, and any, anything of a negative nature needed to be taken out.

Is that your experience of how these reports would be-----

Mr. Derek Moran: I ... well, look, if I can describe the process to you, and I just ... by way of assistance, I mean, the OECD ... and we're currently in the middle ... we're coming to an end of a process again, I think, 16 July, there or thereabouts, the team will go to Paris and go through the process, and it'll be the Department and the Central Bank and so on, as a team. They will make two visits to Ireland, they will meet with the Department, they will have a whole series of questions, a whole series of interactions, but they will also meet with the Central Bank, they will meet with independent economists, they will meet with journalists, they will, and they will take a very holistic view. And through the two of those they generate a report, which we iterate a bit, back and forward, generally what they do is they take factual comments and clarifications and then that's presented to what's called the EDRC, the economic development and review committee, which is a committee in a huge room with all the 30-odd member states in it. And you go through a tortuous day's interrogation during that process, you know; I was at the receiving end of it just once, so, it, it's really hard work. There are three or four lead countries who take you through every line and so on, so forth, and it's open to all the member states including, I think, the IMF are represented and the European Commission are represented at it. And at the end of the day - and incidentally, it also goes through lunch where you sit down with the ambassador and the key examiners, and you get asked questions all through that and don't get a bite to eat, it's a bit like this, actually.

But it's a very prolonged period, and at the end it's down to the chairman to sum up. And the chairman sums up, and it is only within the context of the summing-up of the chairman and the discussion during the course of the day, that you can get any amendments. You know, you can't just go in and say, "I will have that and I won't have that", that's just not the way it works.

Deputy John Paul Phelan: So you don't really, just to sum up, you don't really recognise the last line of his comment, that almost every line was parsed and anything of a negative nature needed to be taken out.

Mr. Derek Moran: Every line was parsed and analysed, but you didn't have the freedom to take out the stuff you didn't like.

Deputy John Paul Phelan: Okay, thank you.

Chairman: Thank you very much, Deputy, and I'm going to move to wrapping things up, if I can invite Deputy McGrath first, and then Deputy O'Donnell.

Deputy Michael McGrath: Thanks Chair, I just have one question for Mr. Moran, and it relates to the various reports, the Wright report, Honohan, Regling-Watson etc. What changes and recommendations set out in those reports, including the Wright report in respect of the Department, are still outstanding, and what plans are there to introduce these changes in the future? So what are the key issues arising from those reports that remain outstanding that affect the work of your Department, which you are still working on?

Mr. Derek Moran: I went through all 50 recommendations of the Wright report, Regling-Watson and the Governor and so on. They're not really very specific about that; they're more about the things that need to be done in a broader context and a lot of that has been delivered. I think that the spirit of virtually everything has been implemented. We've sort of gone for a much more professional HR regime, we've a huge learning development capacity, we've brought in a much greater number of professional people, all of those things. We have huge steps towards codification of our governance arrangements and clarity around that. We look at the ways in which we communicate and so on, so, I'm fairly well satisfied that, you know, we've pretty much implemented them all.

But I go back to my statement: my view is that this is never a finished project. You need to keep doing more and more and more and to the extent possible, benchmark what you're doing against best practice elsewhere. And just recently, we launched a learning development strategy, which is hugely important in terms of keeping the skills levels and so on, at the appropriate level. And we went up, we benchmarked that against industry and out of whatever number of entrants across 250 companies, we came in the top three. So we know we're going in the right direction. Previously we benchmarked tax policy practices in an Oxford study against what other countries did - I'm not sure that was ever completed by the academics doing it but we did participate. And I think that's hugely important. So it's, it's not a fixed exercise, and we keep, we need to do more and more, but it needs to keep relevant and you need to keep it effective and that changes over time.

Chairman: Thank you very much. I'm going to bring matters to a conclusion, Mr. Moran, and I invite any closing remarks that you want to make. But maybe if I could put them in a context, that would create that space for you. The troika have, and the surveillance programme that the country was in ended during your tenure. However, there is still a major deficit, that this country in debt, that this country has to face into, and whilst a very structured programme may not now be involved in, there is still ongoing surveillance. Am I correct in that regard?

Mr. Derek Moran: Yes, yes.

Chairman: Yes, okay. And we have still a set of matrix that we now need to adhere to and the obvious outcome is if we didn't adhere to them, we could potentially be in a bailout programme again. So, I suppose, it's a very simple question is, now that we're out of the programme, are we grown up enough ourselves to do it independently and what action are we taking to retain monitoring and warning controls to ensure that we do not become a country that enters a bailout programme once more?

Mr. Derek Moran: Chairman, I'm always very suspicious when somebody tells me I've got a simple question for you. It's ... I think rather than go back into a bailout, I think the chance ... the risk is that we end up with fines and penalties under the Stability and Growth Pact. In fact, I don't see it. But you're obviously right, we have a very significant sovereign debt overhang to manage, you know, and it's going to take us many, many years to get that down to something that is less troublesome. Look where we came from, we came from a 20% deficit up to 121%, 122%, 123% at the peak in a very short space of time. So, that's where the concentration has to be. Yes, we'll have twice yearly surveillance from the funding partners for the foreseeable future until we've paid them back I think it's 75% of what we owe them. And I have to say, you know, and this is my personal view, in terms of the maturity of our fiscal and economic debate, I'm not sure we're there yet.

Chairman: Okay.

Mr. Derek Moran: I do worry that I'm going back to the various questions about property-based tax reliefs. There seems to be a huge appetite for bringing them back-----

Chairman: So we are still adolescents, if you were to use that term, instead of mature?

Mr. Derek Moran: I wouldn't use such a pejorative term but I do think we've got a way to go. As I say, one of my colleagues said to me, "You know, we're going to have start forming a queue outside the building for people coming in looking for ...". Whether it'd be tax relief to build student accommodation or tax relief to build medical centres. All the stuff that we did in the past and it just doesn't seem to have computed.

Chairman: And just a final comment again, and those concerns are still in the property, construction, housing sector? It's not in somewhere new?

Mr. Derek Moran: There's always the risk and I might finish on this is that, you know, when you're concentrating on what you know you should be ... that there's something emerging over here, you know, that you're planning for the wrong ... But I just do think ... that's why we have to be kind of vigilant and as I said to Deputy McGrath, you know, keep evolving what we're doing, keep refreshing, etc., etc., because as I say, I am a bit concerned is that there is an element of going back to where we were. And a lot of the structures will help us, you know, kind of ... and I just can't see how I could say, you know, introducing investor-led reliefs is a good thing. I just can't see how I could possibly advise, you know.

Chairman: That will be something that we will consider when we move to our recommendations in the course of our inquiry. Thank you very much, Mr. Moran. So, with that said I would like to thank you for your participation here today. Our apologies for delaying in bringing you in but we did bring you in and thank you for your engagement with the inquiry. So, I can now formally excuse you and adjourn the meeting until 3.30 p.m. on Tuesday, 23 June, if that's agreed, is that agreed? Thank you.

The joint committee adjourned at 8.03 p.m. until 3.30 p.m. on Tuesday, 23 June 2015.