HOUSES OF THE OIREACHTAS

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AN COMHCHOISTE FIOSRÚCHÁIN I DTAOBH NA GÉARCHÉIME BAINCÉIREACHTA

JOINT COMMITTEE OF INQUIRY INTO THE BANKING CRISIS

Déardaoin, 10 Meán Fómhair 2015

Thursday, 10 September 2015

The Committee met at 9.00 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.

Chairman: Thank you very much, Mr. Chopra, for those very, very kind comments. Just to acknowledge a couple of items I said at the opening of this morning's session. First of all, you are here as a voluntary witness, being under oath, and you do have the engagement and the responsibilities that come with that. But there was a lot of work put into getting you here today and I very much appreciate your assistance in that regard, but I do think it is a reflection, as I said earlier, of whatever ... one hour of public hearings that we have here, there are hours and hours of work done behind the scenes and I'd like to particularly compliment the investigation team in that regard and also with regard to Mr. Buti who is coming in. But I just think it is one, sort of, example of something that the public actually doesn't get to see ... the type of work that's done in supporting this committee in ensuring that witnesses like yourself are here before us. With that said, I now propose that we bring this matter to a conclusion, that we thank Mr. Chopra for his participation and his engagement with inquiry. We will suspend until 11 ... or, sorry, 12.15. if that is possible - for about 15 minutes, okay, and we will resume then with Mr. Buti.

Sitting suspended at 12.05 p.m. and resumed at 12.28 p.m.

European Commission - Mr. Marco Buti

Chairman: I now propose that the committee of inquiry into the banking crisis resume in public session. Is that agreed? Agreed. Okay, the committee of the inquiry into the banking crisis is now resuming in public session. Can I ask members and those in the public gallery to ensure that their mobile devices are switched off?

We continue our hearings today with Mr. Marco Buti from the European Commission. Marco Buti has been Director General for Economic and Financial Affairs at the European Commission since December 2008. He was an economic adviser to the Commission's President until 2003. From 2003 to 2006 he was director of economies of member states at the Directorate General for Economic and Financial Affairs, where he was appointed deputy director general in September 2006. Mr. Buti, you are very welcome before the committee, and also welcome back as this is not your first time here.

Mr. Marco Buti: Thank you.

Chairman: I would also like to acknowledge that you're appearing here today as a voluntary witness, and that the European Commission has been very co-operative with the committee's requests. This is your second occasion - Mr. Nava has also been here - and I'd just would like to put it on the record that the European Commission has engaged with all the requests that this committee, unlike other institutions that we have, but it has been very very co-operative in its manner with the inquiry. And I just would like to put it on the record that the European Commission has engaged with all the requests of this committee, unlike other institutions that we've had, but it has been very, very co-operative in its manner with the inquiry.

So before we engage in the proceedings, I'd just like 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 of their evidence to this committee. If you're directed by the Chairman to cease giving evidence in relation to a particular matter and you continue to so do, 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'm very, very mindful as well that there are particular terms of reference and lines of inquiry that relate to the Commission that we will be remaining inside today in our engagement with you, Mr. Buti.

In that regard, 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. Therefore, 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 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, and members of the public and journalists are reminded that these documents are confidential and they should not publish any of the documents so displayed. So with that said, if I can now ask the clerk to administer the affirmation to Mr. Buti, please.

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

Mr. Marco Buti, Director-General for Economic and Financial Affairs, European Commission.

Chairman: Once again, Mr. Buti, I thank you for your attendance today, and if I can invite you to make your opening remarks to the committee please.

Mr. Marco Buti: Thank you very much, Chairman. Thank you for inviting the Commission again, as you said, it is my second appearance. I welcome the opportunity to be here in Dublin for the ... for a second time and to contribute to the inquiry as a sign of the Commission availability in the discussion of the Irish crisis and its adjustment. When I appeared before this committee in February, the focus of attention was on the years preceding the crisis. I understand that the statement I gave at the time and the evidence I provided are part of the comprehensive documentation available to the committee. For today, I have been asked to deliver a statement and to provide evidence on the so-called Nexus Phase of the Irish banking crisis, which covers the post-2007 period, including the implementation of the EU-IMF financial assistance programme. With this in mind, in my opening statement I will focus on four subject areas: the first one is the implosion of the Irish economy; the second is surveillance and economic policy initiatives of the European Commission during the crisis years; the third is the reforms to the EU economic governance framework in response to the Irish and euro area crisis; and, finally, the EU-IMF financial assistance programme to Ireland.

Let me stress up front that in my testimony I can only provide evidence on issues that are related to the responsibilities of the institution I represent, namely, the European Commission, in particular its directorate general for economic and financial affairs, so-called ECFIN. In particular, I can provide evidence on matters pertaining to the EU economic surveillance and the implementation of the EU financial assistance programme. I cannot comment on matters of financial supervision or regulation and, linked to that, on matters pertaining to specific individual banks or financial institutions before or during the crisis period.

As pointed out during my first appearance before this committee, the remit of EU economic surveillance prior to the crisis and during the first years of the crisis was fairly limited in scope. It essentially amounted to fiscal surveillance. Other surveillance instruments, albeit available and anchored in the EU treaty, notably the broad economic policy guidelines, had no enforcement power. I made this point during my first appearance plus, all member states were understandably keen on defending their sovereignty in economic policy making. With hindsight, the limited surveillance mandate of the European Commission turned out to be a serious problem. Many crucial events that took place in Ireland between 2008 and end 2010 concerned the banking sector and thus fell outside the then operating range of the European Commission in general, and my DG in particular. More importantly, the European Commission played essentially no role in regulating and supervising domestic banks. I think the point was clarified by my colleague, Mario Nava, who came here to this committee last February. He explained in great detail the supervisory and regulatory set-up in Europe at the time - a set-up that, with hindsight, was far from optimal but which determined the responsibilities of national and supranational actors.

Things obviously changed when Ireland entered the EU-IMF financial assistance programme as the Commission was part of the so-called troika. The involvement of the European Commission also changed with the various waves of reforms of the EU economic surveillance framework. The reform significantly broadened and strengthened the responsibilities of the European Commission and I'll come to that in a moment.

On the build-up to the crisis, the years immediately preceding the Irish crisis were marked by very strong economic growth. I recall the Irish economy was expanding at a pace of 5% or more per year, as opposed to around 2.5% in the euro area as a whole. However, strong economic growth masked important imbalances in several key areas of the economy, notably housing, the banking sector, public finances and the external accounts. A number of observers, including the Commission, noted the build-up of these imbalances. During my first testimony, I indicated the various surveillance documents issued prior to 2007 which highlighted risks linked to both the Irish construction boom and the rapid expansion of Government expenditure during economic good times, but I also made it clear that the key macroeconomic indicators which we had to monitor under our narrow mandate at the time were all satisfactory.

In 2008, against the backdrop of international economic and financial dislocations, the imbalances of the Irish economy started to unwind in an abrupt manner, giving rise to downward spiral of interacting forces: property prices collapsed; budgetary windfalls linked to the property boom vanished and exposed a huge gap in Government finances; banks started making important losses as their real estate exposures went bad; international investors became increasingly worried; and wholesale funding for Irish banks vanished. Liquidity outflows from the banks left them increasingly reliant on the euro system for funding and on emergency liquidity assistance from the Central Bank.

Because of the unprecedented size of the debt-financed housing bubble, its burst gave rise to a particularly strong and persistent feedback loop between the financial system and the real economy. The sharp decline of real estate prices annihilated a large part of the banks' and household assets, which in turn seriously impaired the banks' capacity to intermediate, as well as the households' capacity to consume. The oversized construction sector collapsed abruptly, releasing an army of mostly low-skilled workers. In addition, Government revenues continued to fall and expenditures to rise, not least in an attempt to safeguard the stability of domestic banks. The boom had turned into a daunting bust and policy makers, both domestic and at the EU level, were faced with formidable challenges.

In summary, I very much concur with the conclusions drawn by most witnesses that appeared before this committee. The post-2007 economic and financial crisis in Ireland was domestically generated. Its roots were not only in the banking sector, but also in pre-crisis fiscal policy making. The depth, scope and resolution of the crisis were influenced by the global economic and banking crisis.

As to the domestic policy response, starting in 2008, the Irish Government took a series of measures in response to the crisis. One of the main, and possibly the most emblematic policy action, was a so-called blanket guarantee. To confront the perceived liquidity crisis of the domestic banks in late September 2008, the Government decided to implement a two-year guarantee on banks' liabilities. The guarantee covered almost all liabilities of the domestic banks except for subordinated debt.

It is not for the Commission to judge whether, ultimately, the decision to issue the guarantee was a good one or not. With hindsight, I believe the guarantee was too generous and magnified the fiscal impact of the banking crisis. At the same time ... at the same time, it is clear that the decision was taken in a very difficult situation characterised by great risks and uncertainty. I certainly do not envy those who had to make a decision in late September 2008. The only point of criticism that I can make here is that the Irish Government did not consult with European ... with its European partners. The blanket guarantee heightened competition for bank funding at a moment of growing tension in financial markets across Europe. The blanket guarantee was the first such scheme put forward by a European country during the crisis. In September 2008 there were no specific guidelines for ... concerning the acceptable or desirable features of state guarantee schemes for banks. They were adopted one month later, in October 2008, setting out a fairly strict set of rules. The blanket guarantee was broader than the new rules allowed.

In September 2009, the blanket guarantee was complemented and eventually replaced by the ELG ... so the eligible guarantee scheme. The ELG allowed Ireland to align its guarantee scheme with those in place in other European countries and to limit its exposure towards banks. Importantly, the ELG also allowed Ireland to earn a fair remuneration on the guarantees provided to banks. At the time, the two guarantee schemes provided some relief to the banks but they did not restore their market access for funding. What initially was thought to be a liquidity problem relatively quickly turned into an acute solvency problems ... problem, especially for some of the domestic banks. As a result, and in a bid to safeguard macro-financial stability, the Irish Government made a number of capital injections into banks. Through the cash or promissory notes, the Government provided capital to five domestic institutions, totalling about €49 billion or 29% of GDP in 2009-2010. All capital injections had to be approved by the European Commission, specifically the Directorate-General for Competition.

The economic and financial crisis in Ireland also had a profoundly negative impact on public finances. Starting in 2008, and until the start of the EU-IMF financial assistance programme, the Irish Government adopted and implemented five consolidation packages with a net deficit reducing impact of 9% of GDP in 2008-2010. Still, and because of the particular depth and scope of the crisis, the general Government deficit ballooned to just over 32% of GDP in 2010 and the general Government debt jumped to 87% of GDP, still in 2010, up from 24% of GDP three years earlier. The majority of this was due to one-off banking support measures but also due to the collapse in property-related revenue and structural increases in spending over previous years. The share of property-related revenue in total tax revenue had increased from 8.5% in 2002 to 18% in 2006 and fell to less than 3% in 2010.

Let me turn now to how the EU responded to the Irish crisis. I will start with the policy initiatives for Ireland undertaken under regular EU economic surveillance and then move to the EU response to the euro area crisis more generally. Until end-2011 - when the so-called six-pack entered into force - the EU economic surveillance would have largely centred on fiscal policy, as I mentioned before, notably the implementation of the Stability and Growth Pact. Financial sector developments were not considered to pose a threat to the overall macroeconomic stability. I clearly highlighted this shortcoming in my first testimony before this committee back in February. While the EU has learned the lesson from the crisis and the economic governance framework has been improved significantly, the Commission's surveillance activities for Ireland in 2008-2010 need to be assessed against the backdrop of the framework prevailing at the time.

Once the Irish housing bubble had burst and the economic troubles began, the European Commission deployed the instruments foreseen by existing EU legislation. In particular, it launched the excessive deficit procedure, or, for short, the EDP, for Ireland in spring 2009. Importantly, the EDP for Ireland was embedded in the so-called European economic recovery plan, a cross-country initiative aimed at boosting aggregate demand in Europe and which allowed a considerable amount of flexibility in defining national adjustment paths. I will talk more about this European economic recovery plan in a moment.

Member States with a government deficit in excess of 3% of GDP were given much more time to implement fiscal consolidation. This was also the case for Ireland. When the EDP was opened in spring 2009, Ireland was given four years to correct its excessive deficit, so until 2013. I record that under normal conditions of the rules of the SGP, it would have been one-year deadline. Moreover, in the following years, the ECOFIN Council, upon a recommendation from the Commission, repeatedly extended the deadline for the correction of the excessive deficit, first to 2014 and then to 2015. I think ... I believe the Commission initiative to stretch the period of fiscal adjustment in Ireland was crucial and its importance is probably underestimated in the public debate.

The Commission and the Council were also concerned about the developments in the Irish banking sector. EU surveillance documents issued in 2008 and after included reference to banks. For instance, both the Council recommendations under the EDP of spring 2009 and the Council opinion on the 2009 stability programme mention the fragility of the financial sector and its possible implications for the sustainability of public finances. There were even more extensive references to the financial crisis in Ireland and its implications for fiscal sustainability in the Council opinion on the 2010 stability programme. However, beyond such references, the Commission and, in particular, DG ECFIN, did not have any instruments to help Ireland address the banking crisis. As indicated by my colleague, Mario Nava, here before this committee, financial supervision and regulation was still a national prerogative in the governance framework of the time.

None the less, in early 2009, DG ECFIN stepped up its internal monitoring of the Irish economy. Senior management was updated more frequently on economic and financial developments. The exchange of information between DG ECFIN and DG Competition, which is in charge of support measures for banks, intensified. In addition, in April 2009, DG ECFIN provided input to a dedicated discussion on Ireland in the Eurogroup. As a result of that discussion, the Minister of Finance ... the Ministers of Finance asked the Government to consider a comprehensive reform package to address the serious economic and financial challenges. Ireland reported back in May 2009, including on the supplementary budget it had just adopted in April. However, public communication regarding financial crises is a very sensitive issue. Thus, neither the Commission nor the Eurogroup did publicise this kind of enhanced surveillance.

On the EU response to the systemic euro area crisis, by mid-2008 it was obvious that the euro area and the EU as a whole would be heading towards an unparalleled drop in the aggregate economic activity and employment. It was also evident that the limits imposed by the EU fiscal surveillance framework would become too tight for many EU member states and, second, important elements had been missing in the EU economic governance framework. Thus, starting 2008, the European Commission and, more generally, the EU put in place an array of initiatives. I will not cover the full set of initiatives here. The policy response is well documented on the European Commission Internet webpages. Let me just highlight very briefly the most significant stages which were particularly relevant for Ireland.

At the end of November 2008, the European Commission launched the European economic recovery plan. The main objective of the plan was to provide a co-ordinated boost to aggregate demand across the EU. Hence, the European Commission did not stubbornly implement the commonly agreed fiscal rules. On the contrary, it explicitly encouraged member states to use the available fiscal space to lean against the strong headwinds and many member states implemented fiscal stimulus packages. To ensure credibility, member states were asked to embed the expansionary policies into multi-annual strategies that would ensure the long-term sustainability of public finances. Without the European economic recovery plan, the economic contraction of the euro area would most likely have been even sharper with the usual spillovers to small economies such as Ireland.

The EU also reacted quickly to the emerging sovereign debt crisis. In 2009, the member states and the European Commission began putting in place so-called firewalls or measures to help countries facing temporary difficulties in borrowing from financial markets. In May 2010, the EFSM, the European financial stability mechanism, of the European Union became operational with a capacity to lend up to a total of €60 billion. Shortly afterwards the private EFSF was established with a capacity to provide loans up to €440 billion to the euro area countries. In 2012, the EFSM was replaced ... the EFSF, sorry, was replaced by the permanent European Stability Mechanism, the ESM, with a lending capacity of €500 billion.

The EU, with important contributions from the Commission, also began work on measures to help prevent a recurrence of future financial crises. First, the EU economic surveillance framework was strengthened and extended with the so-called six pack in 2011 and two pack in 2013. I already mentioned these innovations in my first appearance before this committee and am happy to provide further evidence, if so wished, in the discussion. Second, extensive work started towards the banking union with the establishment of the single supervisory mechanism, the SSM and the single resolution board, SRB.

In February, my colleague, Mario Nava, provided a comprehensive overview of how the system of financial supervision and regulation in Europe has changed in response to the crisis. There is nothing that I can add on my part, not least because matters of financial regulation and supervision do not fall under the responsibility of my DG. Let me just say that the banking union represents a natural complement of the economic and monetary union. It addresses severe problems and gaps that were revealed by the crisis, including cross-border financial linkages. The banking union is underpinned by a common set of rules, including for bank resolution, that are designed to minimise costs to the taxpayers.

On top of the key EU reforms there were, of course, also important initiatives taken by the European Central Bank to safeguard the financial stability of the euro area. I will not review them in detail here. They still need to be mentioned because of the interplay between different macroeconomic instruments. In particular the ECB's OMT programme, the outright monetary transactions, was decisive in addressing the sovereign debt crisis in several euro area countries, including Ireland. In combination with other policy initiatives undertaken both on national and EU level, it very much helped to restore confidence and facilitated the return to market funding at sustainable rates.

On the transition to the EU-IMF financial assistance programme for Ireland, from around the spring 2010, the spreads on Irish sovereign bonds over German bunds began to widen significantly and became more volatile due to the increasing worries over the capacity of the Irish to shoulder the mounting level of government debt. There was also contagion from Greece, as it applied for external assistance finance in April 2010. Moreover, we must not forget that these financial jitters went along with very dire economic conditions in Ireland. In 2008-2009, the Irish GNP fell by more than 11%. This was by far the strongest economic contraction in the euro area in those years. The unemployment rate more than doubled from less than 5% in 2007 to 12% in 2009, before rising further to close to 15% in 2011. A small government surplus in 2007 turned into a very large budgetary shortfall of close to 14% of GDP in 2009, with the prospects of a much larger deficit to come. In fact, over the summer of 2010 concerns grew over further losses in the Irish domestic banks, coupled with an imminent end of the two-year Government bank guarantee. Liquidity outflows from the banking sector picked up. At the end of September the Government promised to provide a final estimate of the cost of restructuring the banks, and it announced its intention to strategically withdraw from the markets since it was fully funded until mid-2011. By then spreads had increased to almost 450 basis points.

In an effort to address mounting economic and financial concerns, the Government told the European Commission in September that it was preparing a four-year national recovery plan to be published in November 2010. The plan aimed to reduce the budget deficit to below 3% of GDP by 2014. In the context of the Europe 2020 process - the EU strategy for smart, sustainable and inclusive growth launched in spring 2010 - the Commission undertook a mission to Dublin at the end of September to discuss the challenges facing Ireland and gave input on the reforms envisaged in the national recovery plan. Following this, contacts between the Commission and the Irish authorities continued. As is well known by now, these contacts also encompassed talks about the possibility of a joint EU-IMF financial assistance programme as part of contingency planning. To be clear, at that stage these talks did not involve any negotiations.

During the course of October and November market pressures intensified with further bank deposit withdrawals and the spread of Irish bonds over German bunds widening further. By early November, bond spreads had gone above 680 basis points, a new high and a level that was not considered to be consistent with sustainable public finances. In addition, the announcement by the Government of the fiscal consolidation packages was not enough to calm investor worries. It was against this dire background in mid-November 2010 that more concrete talks began between the Irish authorities, the ECB, the IMF and the Commission in Brussels and Dublin. This was to explore the scope and content of a possible financial assistance programme.

The Irish Government formally requested a financial assistance programme from the EU and IMF on 21 November 2010 and formal negotiations began. In parallel, it published a four-year national recovery plan 2011-2014 on 24 November which, to a very large extent, formed the basis for the policy conditionality of the new programme. I emphasise this point because it was crucial for the ownership of the programme and ultimately for its success. In fact, after the completion of the programme in December 2013, the current Minister for Finance indicated in public that the troika had not imposed one single measure to Ireland. All policy conditions, and certainly the more important ones, had been agreed and put forward by the Irish Government and subsequently included into the programme. This, obviously, is not to say that the troika had not a say in negotiating the programme. Rather, it underscores the fact that the Government programme had identified the right policy challenges, including due to its previous exchanges with the IMF, the ECB and the Commission.

The main objectives of the programme were to restore financial market confidence in the Irish banking sector and in the sovereign, break the financial-sovereign loop and recover market access. In order to do this, the programme was based on three main elements. The first was financial sector reform entailing fundamental downsizing and reorganisation of the banking sector. The second factor was fiscal consolidation to restore sustainability based largely on expenditure restraint, and the third was structural reforms to boost growth and enhancing competitiveness and employment creation. In order to ensure fairness and minimise the social impact, all programme measures were inspired by the overarching principle of protecting the most vulnerable. The European Commission and the other troika partners also showed considerable flexibility in defining the fiscal adjustment path. Most importantly, the programme documents included an extension of the deadline for the correction of the excessive deficit by one year from 2014 to 2015, so this extension allowed for a more gradual and arguably a more growth-friendly fiscal adjustment. Extending the fiscal adjustment turned out to be the right strategy. Fiscal consolidation remained on track throughout the programme period and cumulative GDP growth in 2011-2015, so the period covered by the EDP, has been practically in line with the forecast underpinning programme negotiations. This is quite remarkable actually taking into account the size of the overall fiscal adjustment and the very uncertain economic outlook prevailing at the time.

The implementation of the financial assistance programme was, on the whole, smooth and effective. Most importantly, the EU-IMF financial assistance programme achieved its main objectives. Ireland implemented substantial financial sector repair and fiscal consolidation, regained market access, returned to sustainable economic growth and started to create jobs again. The Irish sovereign recovered market access already in July 2012, well ahead of the end of the programme, when it issued €500 million in treasury bills at a rate of 1.8%. Economic growth, as measured by real GNP growth, returned to positive territory also in the second year of the programme, and last year Ireland was the fastest growing economy in the EU as a whole. The rate of unemployment started to decline in 2012 and has been below the euro area average since 2014. Although less celebrated, the programme also succeeded in containing the impact of the adjustment process on the most vulnerable. Admittedly, the distribution of market income deteriorated significantly in Ireland in 2007-2013. By contrast, the distribution of the disposable income - that is, taking into account taxes and social transfers - remain essentially unchanged. This result is quite remarkable. This is not to say that the adjustment programme had no impact on people's economic conditions. We know ... we know of course it had. However, it shows that fiscal policy was definitely geared toward mitigating the gap between the rich and the less well-off.

The single most important determinant of the programme's overall success was national ownership, as policy conditions were consistent with national preferences. The openness of the Irish economy, the flexibility of its economic institutions and the labour force also played an important role. Last but not least, the EU partners took several important decisions aimed at improving the sustainability of public debt. The lending rate margins on the EFSM and EFSF loans were eliminated and the average maturity extended from initially 7.5 years to 12.5 years in 2011 and again to 19.5 years in 2013. In 2013, with the wind-up of Irish banking resolution company, the promissory note transaction also improved public debt sustainability. This transaction involved exchanging €25 billion of short-term Government promissory notes with marketable long-term bonds.

On post-programme performance, Ireland is now subject to the post-programme surveillance. This is part of the EU surveillance as foreseen by the two-pack regulation. Post-programme surveillance started after the expiry of the EU-IMF financial assistance programme and lasts until a minimum 75% of the financial assistance has been repaid. The Irish economic and financial situation has continued to improve. Ireland is currently among the fastest-growing economies of the euro area. Public finances have recovered significantly and the situation in the three Irish domestic banks is encouraging. Of particular note is also the fact that Irish bonds have suffered little contagion from recent troubles elsewhere in the euro area. This underscores the improvement in fundamentals. While we all welcome the current state of the Irish economy, we are equally conscious of the fact that the adjustment process Ireland went through since 2008 was an extremely difficult one. Nonetheless, many authoritative observers agree that if the ... if programme funding had not been available from international partners, the economic adjustment and the impact for the Irish people would have been significantly stronger. I concur with this assessment, not just because I represent one of the three former programme partners. Rather, I see the financial assistance to Ireland and all the other policy initiatives undertaken at the EU level during the crisis as part of the wider European project, which may not always progress smoothly but which succeeds if we work together.

Chairman, this is my written statement. If you allow me, I would like to add one or two sentences on a more personal ... a very personal basis. I am proud of the work we have done. I think I am proud of my team. I'm proud of the work that we have done with the troika partners, with the Government authorities. I am proud in particular of the Irish people for the efforts they underwent during these very, very difficult times. I think we have learned a lot of this. I think all the institutions - I talk on the ... on our side - we have learned a lot. It was ... it was one of the first programmes - the second for the euro area. We certainly could have done things better in certain extents. I think we have learned our lessons and certain elements clearly could be in the future done better. I think ... nonetheless I think the success of the ... of this undertaking is clear and I think in terms of learning, we have learned I think a lot on the European institutions. I think there is ... the experience has also provided learning for the IMF that dealing with a country in the euro area in a monetary union is not the same as dealing with a country somewhere else in the world, in developing ... especially in developing countries.

The second point is that the job is not done yet. I think it's not done yet for Ireland fully. It's definitely not done yet for the European institutions as a whole. You may have listened yesterday to the state of the Union speech by President Juncker. He said there is not enough Europe in this Union ... there is not enough union in this Union. So the job is still in front of us for several aspects, including matters that are very important for Ireland that we should ... have been mentioned as criticism in the way things have been handled at the European level. I mean we have to complete the banking union, complete the second leg, definitely complete the third leg. The President yesterday announced that we would come forward with proposals for a ... a deposit guarantee ... common deposit guarantee scheme before ... before the matters. At the same time I think we have done a lot. We are not in the same positions as we were when we had to deal with Ireland. And I think we have to avoid, if I may say so, easy *ex post* rationalisations; namely, to judge based on what we know now and what we have now in terms of institutional systems, things of the time. When they set up the institutions ... the institutional set-up was not that. So I think this is important. I hope that the figure that has come out this morning on the Q2 results, which is an extraordinary 1.9% growth, will be confirmed in the future because we know that quarterly growth in Ireland is pretty volatile. But the recovery is well there, creating employment. And I think the future, if everything is done well in Ireland and Europe, is bright for Ireland. Thank you.

Chairman: Thank you very much, Mr. Buti, for your opening remarks and your additional comments. Just for committee members to be mindful as well, you're not a native English speaker. Members might say that I'm not either, but that's a different story. So with that said, if we can get matters under way and if I can invite Deputy Michael McGrath please.

Deputy Michael McGrath: Thank you, Chairperson. And, Mr. Buti, you're very welcome. Thank you for reappearing before the inquiry again. And can I start with your ... your closing remarks there where you acknowledged that some things could have been done better. So, in the context of the Irish crisis, what do you believe the European Commission could have done better?

Mr. Marco Buti: I think the ... I would not, let's say, change in any fundamental way the basics of the programme. I think what we had ... we were confronted with at the time was a crisis which was not only a banking crisis. It was a crisis of, let's say, systemic nature and also a fiscal crisis. So I think the axis of the programme which was, on the one hand, to cure the banking system, to deal with the unsustainable public finances when the true state of the public finances came to the fore with the crisis ... and the overall rebalancing of the Irish growth model I think was the right one. Now, if I take what we could have done better I think we ... as I said, we largely succeeded in, I'd say, very difficult circumstances to reduce the burden on the less well off. With this taken into account, I think we could have done more on that from what we know now in terms of the social consequences. The social consequences, I think, were ... tackled and reduced but we could have had a system which would protect probably even more.

Deputy Michael McGrath: So you're talking there about the fiscal adjustment and how it was implemented but were they not matters for the Irish Government of the day to decide rather than the Commission or the troika ... the detailed elements of the programme and how to arrive at the target deficits? So, in terms of social protection expenditure and so forth, they weren't matters for the Commission, surely.

Mr. Marco Buti: No. Clearly, I think it has been stressed quite ...quite forcefully and I think it is ... it is absolutely the truth is that, as always in the ... in programmes with the EU and IMF, the details of the individual policies are for the government to implement. Clearly, there is open dialogue and there is a lot of ... of interactions. I think on the ... overall on the fiscal, I think you have two issues. One is the speed of adjustment, so how the fiscal ... the inevitable fiscal retrenchment is carried out over time and the other one is the composition. Now, I think on the speed of adjustment I have indicated that already - in the initial EDP decision - we had granted four years adjustment in 2013. These were extended to 2014 and eventually 2015 at the initiative of the Commission. I think this was largely correct. Now, in terms of the composition, one could have looked at, you know, social spending and maybe, let's say, protect even more the less well off. But, overall, I would say that if one looks also at the indicators of market disparity of income, which increased very strongly ... but the *ex post*, after the tax and benefits system operating ... largely preserved the current distribution of income. I think this was a success of the programme.

Deputy Michael McGrath: I'm just not sure I got anything there as to what the Commission could have done better in the Irish context. You went back to the fiscal element and social expenditure programmes and so forth but ... on the Commission, is there anything the commission could have done better in handling the Irish crisis?

Mr. Marco Buti: I think looking at things from where we stand now, certain things could have been ... could have been done better. I think ... what I think one should do at this stage is to see with the ... where we stand now and what has been the development over time.

Deputy Michael McGrath: We'll continue with the questioning and we'll see where it takes us.

Mr. Marco Buti: I think we can be satisfied by the ... by the-----

Deputy Michael McGrath: Can I start by taking you back to November 2010? And you'll be well aware of the letter from Jean Claude Trichet, the President of the ECB, to the late Brian Lenihan 19 November 2010, which made the continuation of emergency liquidity assistance for our banks contingent on the Government applying for a formal bailout programme. So was the European Commission aware at that time of the stance of the European Central Bank and was it a stance that was supported by the Commission?

Mr. Marco Buti: We were aware of the stance of the ECB, obviously. I mean, when we were talking about ... amongst the institutions, we were aware that the worries of the ... of the ECB in this. We were not part of ... or we were not copied in on the letters that Mr. Trichet sent at the time. I think we did not have any possibility or willingness to influence the ... the ECB at the time. I mean, what Mr. Trichet has indicated to you - not precisely in this committee - is that the exposure of the ECB was very, very large and one has to take that ... that into account. So it was an individual decision by the ... by the ECB. I think in ... I think in these matters one has to look at the ... what the real situation is and I think, deep down, independently of the letter of Mr. Trichet, the situation became so difficult. And I mentioned in my written statement that the spreads over the bonds at the time were ballooning, which made it inevitable and right to apply for a bailout.

Deputy Michael McGrath: I suppose the question is: did the Commission support the direct linking of continued provision of ELA to the banks with Ireland entering a programme?

Mr. Marco Buti: No, we have ... I have nothing to say on this. This is a matter for the ECB, not for the Commission.

Deputy Michael McGrath: That's fine. And at that time, in mid-November 2010, prior to formal negotiations getting under way - there had been preliminary discussions - had the European Commission come to a view that Ireland should enter a formal programme at that stage?

Mr. Marco Buti: I think the ... at the time, I think it was evident that the adjustment programme was inevitable and the ... we saw this as ... I think as a good step indeed, considering the decision of the ... to apply by the Irish Government I think was a wise step at the time.

Deputy Michael McGrath: Okay. In his evidence to the inquiry, Kevin Cardiff, the former Secretary General of the Department of Finance said:

> The big question in the public domain in relation to the bailout seems to be whether entering the EU-IMF programme was a free choice or were we pushed. Well, at the moment we entered it we were pushed quite hard [he said].

Have you any comment to make on that?

Mr. Marco Buti: We had intensive discussions in the context of the regular contacts that we have with the Irish authorities at all levels: central banks, the Finance Minister, ministries, the Irish Government. I think at that time the situation was such that the ... it was inevitable I think for Ireland to apply. I have to say that one thing that ... one question that may come is, which may be implicit in your question, is that: was it right for European institutions to have a view on this or not or should it be left completely to the Irish Government, in this case, or to a national government? I think the ... the experience at the time was very clear that, given the potentially dramatic spillover effect and contagion risks, I think we had the right and the duty to have a view ... to have a view on this. And actually, if you look at the *ex post* on the two-pack regulation, the one dealing with the financial ... with financial assistance, there is the provision there that the Commission can recommend the Council to advise a country to prepare an adjustment programme. It doesn't mean applying for the EU ... full EU-IMF programme but ... but in a situation of dire straits, certainly that is something that goes in that direction. So I think it was ... I think it was our duty to have a view and at the time I think it was ... we considered it to be right for the Irish authorities to make that decision.

Deputy Michael McGrath: Can I take you to the bailout itself and the interest rates attaching to the various elements of the bailout programme? The rate on the EFSM was 5.7% initially; the EFSF, 6.05%. Now, the IMF rate seems to have been quite rigid in that it has determined by set rules of that organisation. But can you explain how the EU elements of the funding for the bailout programme arrived at those figures, which were higher than the Government was expecting? Was there an element of negotiation involved or was the Government told, "These are the rates attaching to these streams of funding and that's it"?

Mr. Marco Buti: The IMF has its own way of setting rates and the rules related to their, say, their prerogatives, and we did not have that at the time. It was ... we were in unprecedented territory. I always, when I talk about management of the crisis not only on Ireland but all other countries, is that we were there in a wholly new situation. So we had ... there was an element here of learning by doing and setting the rules as we walked along. Now, at the time the idea was to try to mimic and get to something with a European ... at the European level, which was close to what the IMF had but we did not have the possibility. We don't have the capital that was, you know, that was ... that could be off-lent to the country. So, what we could do ... we did at the time - what we are still doing actually - is that we have to go and borrow on the market and lend back to back to the Government. Now then, on top of that, at the time it was decided that in order to get close to IMF rates, that a margin, which was about 290 basis points, would be .... should be charged.

Deputy Michael McGrath: 290?

Mr. Marco Buti: 292 actually, I think, if I'm not mistaken.

Deputy Michael McGrath: 2.9%.

Mr. Marco Buti: Added to the market ... to the borrowing rate. And here the prevailing opinion at the time was to avoid moral hazard or, you know, too easy, let's say, entering into a programme.

Deputy Michael McGrath: You didn't want to create a financial incentive to get into a programme. You didn't want to reward a country that ended up in a programme.

Mr. Marco Buti: That was in the mind of some at the time the idea. Now, it is clear that this margin was very large.

Deputy Michael McGrath: This was on the EFSF element, is it? The 2.92% margin was on the EFSF element?

Mr. Marco Buti: Yes, the EFSF, exactly. So what we had when it was decided it was too large and then, based on strong ownership and strong implementation of the programme, subsequently in two stages - I indicated before - actually we came to elimination of the margin, which improved, I think, very substantially. If I'm not mistaken, I think between €4 billion and €5 billion saved in terms of interest payments due to the reduction ... to the elimination of the margin. So, this was what was done at the time, initially let's say, to match the IMF rate and then rewarding the good implementation over time and substantially improving the sustainability of public finances.

Deputy Michael McGrath: Okay, but are you acknowledging that, in hindsight, the rate was too high?

Mr. Marco Buti: I think the rate was certainly pretty high and I think the, kind of, incentives that was built into the system with the ... then the tapering of this and the elimination, okay, improved the situation certainly.

Deputy Michael McGrath: Can I take you to the issue of burden-sharing, which featured during the negotiations of the bailout programme as well? We heard evidence this morning from Ajai Chopra, the mission chief from the IMF, and in his view, if Ireland had been allowed to impose losses on senior bondholders at the time of the programme negotiation, savings of up to €8 billion could possibly have been achieved. We know that the ECB was opposed to it at the time, the IMF was supportive of it and it would appear that the Commission sided with the ECB and blocked burden-sharing. Is that the case?

Mr. Marco Buti: Okay, let me say, first of all, this ... I want to go back for a second to what I said at the very end of my written statement, namely, that one should beware of ex post rationalisation in judging, let's say, with what we know today and what the institutions and legal system that we have today. Now, we were at the time for Ireland and for the euro area as a whole in a life-threatening situation. I think the judgment that was made by the ECB, in particular, was that in a situation of unprecedented uncertainty, going into something which would have, or could have, increased substantially the uncertainty ... market uncertainty and possible spillovers effect - and I say "spillovers" here both in terms of cross-country spillovers so to other systems, but also spillovers within Ireland - would have been, I think, too risky. This was a judgment made. At the end of the day, the troika are three partners and we came to the common judgment that this was not the right thing to do. The ECB was very forceful on that. I think overall ... and I think we have documented that in our ex post assessment of the programme that has been made available to the committee, I think we think ... I think with hindsight ... I think it was the right thing to do - not to go for the bail-in of senior bondholders.

One thing that has not been mentioned here so far, I think, is the fact that the legal system that prevailed at the time was not clear. It did not allow this in a sufficiently certain manner. So, the risk of legal systems-----

Deputy Michael McGrath: The Irish legal system or-----

Mr. Marco Buti: No, both at the Irish level because you should have, I mean, a specific *ad hoc* law should have been-----

Deputy Michael McGrath: We have examined that issue, yes.

Mr. Marco Buti: And, even more importantly, at the EU and at global level. So, the FSB guidelines for the global community were issued later on and we did not have what we have now, the BRD, which, you know, allow clear rules for a bail-in. So, this implies that the litigation ... potential litigation costs related to that could have been very high, prolonging the uncertainty and eventually wiping out largely, if not more than largely, the potential gain coming from the direct bail-in of senior bondholders.

Deputy Michael McGrath: But is it the case, Mr. Buti, that the dominant consideration from the Commission and the ECB's point of view was the wider impact on the eurozone , the spillover effect? Because I would put it to you that, from an Irish perspective, Ireland was entering into a programme whereby it had, subject to conditionality, a guaranteed stream of funding from the authorities for a period of three years, so market sentiment towards Ireland was not directly relevant. The key concern was the spillover effect in the eurozone at a time when you were trying to put a lid on the crisis. And so, in that context, I'm putting it to you that Ireland took one for the team.

Mr. Marco Buti: That is ... you are correct in this. So the spillovers, let's say, were, let's say, in particular to the rest of the euro area. However, as I explained before, the EFSF and the EFSM going out and borrowing to on-lend to Ireland in a situation on even potentially larger market unrest and even higher interest rates would have been, I think, damaging for Ireland also. So the effects ... so the negative loop from Ireland to the rest of the euro area and back to Ireland, I think, were certainly present in the assessment.

Deputy Michael McGrath: So it was both. In your assessment, it was the potential impact on Ireland indirectly through the funding channels and then a direct impact on the wider eurozone and the view of the markets towards the eurozone?

Mr. Marco Buti: Yes.

Deputy Michael McGrath: Okay, and today you believe, looking back, that was still the right decision.

Mr. Marco Buti: I think so. Yes, I think so. I mean, I am looking now, obviously, with an exercise of what economists call comparative statics. I mean, I look at the situation of the time, I look where we stand now. And with the situation that we have, both in the economic and financial system at the time for Ireland and considering the very large risks which were there at the time, adding a potential source of uncertainty, further uncertainty, I think would have been unwise. I have to say that this was the view of the Commission. The ECB, let's say, channelled this view in a very powerful manner, but it was also the view of many other stakeholders at the international level. For instance, the ... when we ... even taking the IMF debate into account - we know that Mr. Chopra indicated that the review of IMF was that there was not that view at the IMF board level, which includes, let's say, the older stakeholders at the national level. Some of the very, let's say, powerful stakeholders made their view known.

Deputy Michael McGrath: Yes and we are aware of Mr. Geithner's book and the references that he made at that time. But can I take you to a different issue, and that is the issue of Ireland's corporation tax rate? Again, in the lead up to the negotiations and ... there is a reference in evidence that Mr. Cardiff gave in his lengthy written statement where he refers to a visit, a two-day visit to Brussels that he and the Minister and Mr. Honohan would have made in November, and he refers to yourself:

> Later that evening, [he says] myself and Honohan had dinner with Mr. Szekely [is that how you pronounce your name?] and his boss, Marco Buti. We went over the day's events and the prospects for Ireland and Europe. Walking through narrow side streets on the way

back to our hotel, Honohan told me that while I was washing my hands, Buti had taken the opportunity to tell Honohan that I was unrealistic [on the corporation tax issue] and that we would have to concede on the corporation tax issue.

Is that accurate? Was this your observation, your assessment of the views of other countries or was this a European Commission view?

Mr. Marco Buti: No. Okay. I remember the dinner, I can tell you the menu bilaterally after. It was very cheap, actually. So, very much in austerity mode already.

Deputy Michael McGrath: Who paid for it?

Mr. Marco Buti: On the specific issue, I think what I must convey ... I must have conveyed that time, so I don't deny that. I cannot recall precisely, but I am sure if it has been reported by Mr. Cardiff, I must have done it. What I did at the time was to convey the view of a number of member states which were, let's say, vocal, also in public I believe, on the fact that as they were getting into a programme helping Ireland, they considered it to be unfair tax competition coming from the very low corporate rates. So it was not, and here I'm formal, it was not the preference of the Commission, it was not my own preference, it was making them aware of the fact that the view in some member states in the euro area, this was an issue that could come up.

Deputy Michael McGrath: Okay.

Mr. Marco Buti: In fact, our own preference, and it was expressed then when we came to the negotiation of the programme, was that not in a situation of collapsing growth not to undermine the ... one of the strengths of the Irish system, which is the strong competitiveness of the corporate sector. So this was, let's say, our position at the time.

Deputy Michael McGrath: Did you convey the sentiment from some countries that you were picking up, you were conveying that?

Mr. Marco Buti: Yes. It was not a sentiment it was an explicit statement.

Chairman: Final question, Deputy McGrath.

Deputy Michael McGrath: Okay. Final question is, you say in your witness statement that during the pre-crisis years in Ireland, strong economic growth masked important imbalances in several key areas of the economy, including housing, banking sector and the public finances and I don't think there is any disputing that. But can I put it to you, Mr. Buti, that the agreed measure at the time of the structural deficit for example of member states, that Ireland even then was reporting positive structural balances, I think, bar one year? And when we had testimony here by John McCarthy, the chief economist in the Department of Finance, he stated that the measurement of structural deficits is still a problem today. And he confirmed, when I put it to him are you saying that Ireland was actually complying with the structural balance requirements from Europe at the time, pre-crisis, in accordance with how the structural balance was measured in harmonised terms during all of those years, he said, "Yes". So in acknowledging that imbalances were building up in the system, the agreed harmonised methodology for measuring that in the EU did not detect those imbalances on the fiscal side. Can you comment on that?

Mr. Marco Buti: I think that's correct. When the ... I mean in the evolution of the fiscal surveillance, we have moved from looking only at headline figures, so deficit and debt, to try to understand the underlying. So the automatic stabilisers may, you know, vary with the cycle.

They go up ... the deficit goes up and down for very good reasons, for very good reasons. But the issue here is to try to detect what is the underlying situation of the public finances. And I have to say that at the time, the method did not give rise to particular worries because we had, mistakenly, and I think here I acknowledged that very clearly back in February, we were projecting growth staying high for a very long time. So we thought at the time, mistakenly, that the potential growth rate of the economy would be very high and remaining high.

We have realised, afterwards, that there was an element of reversional exuberance, let's call it like that, with ... behind the figures. This clearly had an impact on the assessment of the structural balance at the time. I think we have changed ... we have learned a lesson. I have to say that in particular for Ireland, but more generally for small open economies, it is very difficult to detect what structural balances, structural deficits are. Here, you have in Ireland, you have a ... one of the elements is the labour component of the Irish potential growth, and we know that you have a highly integrated labour market with the UK. So, it's difficult here to assess what is the structural rate of unemployment. You have also tax elasticities which are very, very-----

Deputy Michael McGrath: Very finally, are you accepting that in the years leading up to the crisis, that the EU's measure of Ireland's structural budgetary position did not detect the growing dependence on property and construction-related receipts and did not detect the impact of that on the underlying fiscal position?

Mr. Marco Buti: I think that is a fair statement and we have corrected a number of things and we started correcting even before the crisis, but we did not apprehend fully the true state of the public finances in Ireland at the time.

Deputy Michael McGrath: Thank you.

Chairman: Thank you Deputy. Deputy Murphy.

Deputy Eoghan Murphy: Thank you, Chairman, and thank you Mr. Buti. You are very welcome. I just want to go back, if I may, to 2008. In your opening statement you say that it is not for the Commission to judge whether ultimately the decision to issue the guarantee was a good one or not. But the Commission had to approve the guarantee for state aid purposes, so was that not a judgment being made by the Commission at the time?

Mr. Marco Buti: The ... I mean, I stand by my written statement saying that it is not for us to judge this. We did not ... I think there was a question in my previous hearing whether we had asked to do so and this was definitely not the case. The European Commission intervenes here in terms of the application of state aid. So it is up to DG Competition to implement the state aid rules. And from that viewpoint, I think the Commission adopted ... and supported the decision. But this is a different thing compared to the ... let's say, to the judgment on the ... let's say, wisdom of having such a large-----

Deputy Eoghan Murphy: You can improve something in terms of state-aid rules but you can remain neutral on the actual decision being made.

Mr. Marco Buti: Okay, I think the ... when I said that the state of affairs - the institutional setting and the legal setting - at the time was not complete ... it would not ... let's say, did not allow to have ... to see all the bits and pieces together. This applies also to this particular case and the guidelines on state aid they were issued, you know, afterwards by the Commission and by DG ... by DG Competition.

Deputy Eoghan Murphy: Okay. Well, what are the judgments you make when you say the guarantee was too generous and magnified the fiscal impact of the banking crisis? You say that in your opening statement. Is that not a view or a judgment from the Commission now?

Mr. Marco Buti: You should read also the rest of my statement-----

Deputy Eoghan Murphy: No, no, I have and I'm going to go through it with you, don't worry, yes.

Mr. Marco Buti: Yes, I think, with hindsight ... with hindsight, I would say that the blanket guarantee was something ... by covering, essentially, all liabilities, was very large - too large - and when we came to the decisions later on at the European level, as a whole, then it was ... the liabilities covered were smaller than the blanket guarantee. At the same time, I have to say, and I repeat it because I try to apply this, let's say, I have this conceptual reflex on not being excessively harsh now, with things that ... with the knowledge of the time, I think, I do not envy - I say it in my statement - those who had to make that decision at the time because it was, you know, in very, very difficult and dire circumstances.

Deputy Eoghan Murphy: But is that not the Commission making a judgment on the guarantee that it was too generous? When you say that in your statement, are you not here - as the Commission - making that judgment?

Mr. Marco Buti: No, what I am saying is that, with hindsight, it was indeed very generous, possibly too generous. At the same time, I acknowledge that those who had to make that judgment in those life-threatening conditions, I think, had possibly good justification for being very risk averse. What we can see, clearly, is that the blanket guarantee intertwined the fate of the banking system and the fate of the public finances in a way which was a perverse one.

Deputy Eoghan Murphy: Yes, so you criticised the Irish Government for not consulting with European partners. What do you mean by European partners, because we know that the Irish Government did consult with the ECB? So what do you mean by that?

Mr. Marco Buti: I mean that, to my knowledge - and I can speak for the Commission - we were not consulted, we were not informed and we knew we were told *ex post*.

Deputy Eoghan Murphy: Okay, but were you aware that the ECB had been consulted?

Mr. Marco Buti: I'm not ... I cannot say.

Deputy Eoghan Murphy: Okay. In terms of the Commission's involvement here, should the Commission not have been consulted? Do you feel that it should have been consulted beforehand, before the decision was made?

Mr. Marco Buti: I think it would have been wise to do so, yes.

Deputy Eoghan Murphy: Okay. And in terms, then, of the Commission's responsibility here ... because you say, again in your opening statement, that there were no specific guidelines in place in September but there were then in October. So, does responsibility fall on the Commission for those guidelines not being in place before the banking crisis in September? Again, given the context, the liquidity difficulties that banks were facing all over Europe through 2008, does the Commission accept responsibility for those guidelines not being in place?

Mr. Marco Buti: No, I cannot answer here. I am representing the ... the Directorate General for Economic and Financial Affairs. This was a matter for the DG in charge of competition policy, so I cannot ... I cannot express myself on this.

Deputy Eoghan Murphy: Okay. Well, was your section slow in getting recommendations to the Directorate General for guidelines to be in place for the kind of crisis that we saw in September, which then came in in October? Was there a delay in realising the seriousness of what was happening in the European banking system at the time?

Mr. Marco Buti: I can only tell you in very general terms that we stood ready - this is the Commission, as a whole - to react as quickly as we could in unprecedented circumstances and putting in place what was needed at the time and this is the only thing I can tell you.

Deputy Eoghan Murphy: Thank you. Okay. You also say that - and you already mentioned it a few times - that the blanket guarantee was a major factor contributing to triggering the need for assistance from the troika. Was this understood in the Commission when the guarantee was put in place? Once the guarantee came in and that measure being put in place, did you understand that what this was going to mean two years from now?

Mr. Marco Buti: The logic and the, let's lay, the underpinning of ... and the rationality of a blanket guarantee was based on the fact that one would consider the problems of the banking system being only a liquidity issue. If you have a liquidity issue purely, then you can do that, then it's about volatility that can be ... can be overcome very quickly and this is ... then you can do that ... you put the big bazooka guaranteeing everybody ... liquidity then is restored and the system continues as it was before. What was ... I think what became clear very quickly is that considering the interactions between the growth model of Ireland based largely on housing growth and the boom and bubble that we ... at the time and the heavy reliance of banks in their portfolio on mortgages, it was clear that the bust there that was ... gave rise not only to a temporary programme of liquidity but there was an issue of sovereignty so the banking ... the banks had to be restructured and, from that viewpoint, the blanket guarantee clearly did not help.

Deputy Eoghan Murphy: Okay, so at what point did the Commission see this problem for Ireland in terms of the bank difficulties being intertwined with the sovereign difficulties, because you note as well the five fiscal corrections and consolidations that the Irish Government had to undertake, you know, from the moment of the guarantee? So at what point are you sitting in the Commission going, "Correction number 3, there's a problem here that's a bit deeper, that these little bites at the cherry isn't going to address. We need to look at something bigger."?

Mr. Marco Buti: I cannot tell you the ... I cannot pinpoint the exact time. I think in the course of 2009 it became increasingly clear that there was a more fundamental issue with the Irish banking system and then leading into the discussion in the course of 2010 and the problem that was evident that one of the pillars of the adjustment programme already in the recovery plan by the Irish Government itself was, let's say, fixing the banking system.

Deputy Eoghan Murphy: Okay. So when Greece entered into difficulties and was seeking a programme, were there any contacts between the IMF and the Commission in relation to who might be next for a programme? Did they come to you and say, "Look, we think there might be a problem with Ireland."? They were talking April-May 2010.

Mr. Marco Buti: I cannot, myself, personally recall this but I do not exclude it. I mean, there was ... we were at the time ... just to get you the picture ... into ... I mean, I defined before the life-threatening situation in which the vulnerabilities of a number of countries came to the fore very quickly. So when the focus was on Greece, I am pretty sure that the discussions went on at the time also on other potentially vulnerable countries, Ireland being one of them.

Deputy Eoghan Murphy: Can you tell me about the proximity of the Commission to the ECB when it came to addressing the Irish situation? I mean, you said to Deputy McGrath that later on in the negotiations the ECB was channelling the view of the Commission. But prior to any, kind of, formal negotiations, how close are the ECB and the Commission in terms of their view of Ireland and their contacts ... their co-operation in addressing the Irish case?

Mr. Marco Buti: Obviously, very, very close. I mean, we are working in the Eurogroup working group where I am, myself, represented. We have teams, we have ... we work at our operational level in an extremely close manner. And I think we have in this ... I can ... there isn't ... we may have a difference of view compared to the IMF. We embodied in our reasoning very strongly the risk of contagion that was present at the time.

Now, on the risks of contagion, Ireland was, let's say, a quintessential candidate because of the size of the banking system and because of the interplay between the Irish banking system and that of the rest of the EU. This was much more the case of, let's say, the initial programmes that we had from non-euro area countries, much more the case than Greece where contagion was more related to, let's say, imitation effects and risks of, you know, in a domino effect. But Ireland, there was a clear interplay between the Irish system and the rest of the EU, also with the US. So, these elements of risks or spillovers, I think, were very present, and rightly so.

Deputy Eoghan Murphy: Okay. Well, I'm talking about the relationship between the ECB and the Commission in addressing Ireland. So we have it in evidence from Mr. Cardiff that in September, when the ECB became aware of the funding cliff... the bank funding cliff, that the president of the ECB phoned the Department of Finance and spoke to the Minister and demanded that the Commission be allowed go to Ireland to see what was happening and what we were doing ahead of this challenge. So, would that be unusual for the ECB to be making those kinds of requests or demands for the Commission to do work?

Mr. Marco Buti: I think, I'm not particularly ... aware, in particular, of this episode ... I have not directly read it myself, as you have done. I think it is ... I don't see that as unprecedented or particularly problematic. I think the ECB has, let's say, its own responsibilities in this. It is worried about the state of the financial system and, more generally, for its implication for monetary policy. And the ECB is also fully aware that a number of other elements on the fiscal and on the structural side, affect this. So, I don't think it is particularly problematic that there would be a suggestion of that sort.

Deputy Eoghan Murphy: So, a team did come from the Commission in September of 2010 and it's been characterised by Mr. Cardiff that the purpose of that mission was to make an initial precautionary assessment of the potential for a bailout programme. Is that accurate?

Mr. Marco Buti: In terms of contingency plan, it is accurate that we did not negotiate at the time with the Irish authorities. We were not in a negotiating mode or mood. We ... in terms of contingency planning at the time, I think it was only normal for a responsible institution to do so.

Deputy Eoghan Murphy: Okay, but could we characterise that then as the beginning of bailout discussions or contacts at a technical level?

Mr. Marco Buti: I would think so, yes.

Deputy Eoghan Murphy: Okay. And then we move to later in September. Minister Lenihan has gone to Brussels for discussions with Olli Rehn. And Olli Rehn communicated to the Minister - this is according to Kevin Cardiff's evidence - that he thought Portugal would be next in line for a bailout but that you told him that you thought Ireland would be next for a bailout. Do you recall that discussion?

Mr. Marco Buti: I do not recall the specifics but I'm not ... I don't deny ... I cannot deny that either.

Deputy Eoghan Murphy: Okay.

Mr. Marco Buti: It may well be.

Deputy Eoghan Murphy: Okay, so ... but that was your thinking at the time, that Ireland would be - this is the end of September - that Ireland would be next for a bailout?

Mr. Marco Buti: I think at the time, the ... after having had the Greek programme, with the mounting tensions and the increase ... rapid increase in the spreads on the Irish Government bonds, I think it was not only ... it was not essentially myself; I think that it was quite, you know, a widespread view that should the crisis not abate by itself - it didn't look like it at the time - that Ireland could be a potential candidate for an assistance programme.

Deputy Eoghan Murphy: Was it easier to manoeuvre Ireland into a bailout given that they had withdrawn from the bond market?

Mr. Marco Buti: Can you repeat that, sorry?

Deputy Eoghan Murphy: Easier to manoeuvre Ireland into a bailout given that they had withdrawn from the sovereign bond market?

Mr. Marco Buti: No ... I don't ... I can ... I do not accept the characterisation of us manoeuvring Ireland into a programme. I think this ... there was an honest, fair, prudent assessment of the state of the situation of the Irish economy and the Irish financial system and the Irish public finances and what was needed at the time. I think we supported very strongly the national recovery plan that the Irish Government had put in place and were elaborating at the time. I think we had good advice on that, as always we do in a ... you know, sharing sovereignty situation as we have in the EU. And that was the... but we did not, you know, manoeuvre or, let's say, push or threaten anybody.

Deputy Eoghan Murphy: Was the Commission involved in the Deauville declaration in October?

Mr. Marco Buti: In what?

Deputy Eoghan Murphy: The Deauville declaration from France and Germany.

Mr. Marco Buti: The Deauville declaration ... we were not involved in the Deauville declaration. We ... it came a bit out of the blue from Germany and France on the famous Deauville beach. And the assessment at the time was that whilst for some, let's say, political reasons, one could understand the Deaville declaration in terms of, let's say, the contribution at the time to the financial stability of the euro area and the EU at large was not the most helpful step.

Deputy Eoghan Murphy: But the Commission wasn't consulted before that declaration was made?

Mr. Marco Buti: We were not consulted.

Deputy Eoghan Murphy: Okay. Can I move forward, then, to November and to the G20 summit? Was the Commission at the G20 summit?

Mr. Marco Buti: Yes.

Deputy Eoghan Murphy: Were you at the G20 summit?

Mr. Marco Buti: I was also there, yes.

Deputy Eoghan Murphy: Okay. We've heard in evidence of the frustrations from Irish ... members of the Government that fellow member states but also either ECB or Commission officials were briefing against Ireland in Seoul and that this precipitated the need, almost certainly, for a bailout. Does that sound familiar? Are you aware of any briefings or conversations or discussions on Ireland at the G20 meeting?

Mr. Marco Buti: Conversations, certainly. We were ... I mean, in the context of the G20 gatherings, where you have all the, you know, the top level economic, let's say, intelligentsia and stakeholders in the world, there were certainly discussions on the state of the euro area, the state of individual countries, and, I am pretty sure, Ireland also. I do not recall and I'm pretty sure that there were not, let's say, press briefings on the specific issue, certainly not in the way you may characterise it as something that is, let's say, messages which were against Ireland, the Irish Government or the Irish authorities.

Deputy Eoghan Murphy: Did you share your view with people there that Ireland would need a bailout?

Mr. Marco Buti: I do not recall exactly but I am pretty sure that the issue came up and the risks of a .. of the, let's say, the need of having to step up and to, let's say, to put Ireland to consider financial assistance, I'm pretty sure they were part of the conversation.

Deputy Eoghan Murphy: Okay, but you weren't party to any informal decisions that were made?

Mr. Marco Buti: No, neither ... and I am not aware of any side meetings, let's say, at the political level on the-----

Deputy Eoghan Murphy: Thank you. I want to move forward, then, just to burden-sharing and the legal advice. Did the Commission get its own legal advice on whether or not it was constitutional for Ireland to impose losses on senior bondholders?

Mr. Marco Buti: I cannot tell about the legal ... specific legal advice sought at the time by the Commission. What I can tell you is what I indicated before, namely, that the institutional system and the legal system at the time did not foresee this in any regulated manner and that's why the risks involved in a unilateral decision on this were not to be disregarded, and, as I indicated before, the potential litigation costs could have been very high for Ireland, in particular, and, more generally, the uncertainty created for Ireland, the rest of the EU not negligible.

Deputy Eoghan Murphy: Was it put to the Commission that Ireland might hold a referendum on the issue in case there was any constitutional uncertainty?

Mr. Marco Buti: Can you repeat this question, please?

Deputy Eoghan Murphy: Was it put to you that Ireland might hold a referendum to amend the Constitution so that it would be legal to burn senior bondholders?

Mr. Marco Buti: I have no comment on this.

Deputy Eoghan Murphy: So you weren't . . . that didn't come up in a discussion that you were party to?

Mr. Marco Buti: I am not aware of that, no.

Deputy Eoghan Murphy: Okay, thank you. If I might just move on then to March 2011 and the new Government is in place. There are negotiations on the interest rate that has been agreed with the bailout programme and the possibility of producing it. Was the Commission of the view as early as March 2011 that the interest rate needed to be reduced?

Mr. Marco Buti: In terms of the margin to be reduced? No, I think we were ... we have been constantly throughout the discussion in favour of lessening the burden on the Irish Government and the Irish people so we have been constantly in favour of reducing and then eliminating the margin. So we have been ... and we have prepared the actual proposals for this. It is clear that one has to understand the logic of the, and the institutional setting for, the EU-IMF assistance programme. In these programmes, we are largely in an intergovernmental setting. So it is ... we are not in the typical Community ... with a typical Community method in which the Commission has the right of initiatives, puts forward the proposal and then the government votes, essentially a majority or they adopt the ... the Commission has the ... in case of substantial changes to withdraw the proposal, we were not in that setting. We are in an intergovernmental setting in which the Commission, in particular, was in charge of implementing the programme. Believe me, we do not do that in a blind manner and, as I indicated and I stress, we were, let's say, behind the scenes, pushing for creating conditions and for the governments to consider reducing the margin.

Deputy Eoghan Murphy: This is my final question Mr. Buti. We have it in evidence that in March of 2011 the new Irish Government was in discussions with the Commission about reducing that interest rate but that this had to come off the table because France and Germany raised again the issue of the Irish corporate tax rate. Is that what happened? Is that why those negotiations were postponed until later?

Mr. Marco Buti: I cannot confirm this. What I can say is that I repeat what I have just indicate, namely that, as far as the Commission is concerned, but here more in a persuasion mode, not as institutional responsibility, we were in favour of reducing the margin and eventually we were extremely happy that it was decided eventually to not only reduce but also to eliminate down the line.

Deputy Eoghan Murphy: Thank you, Chair.

Senator Susan O'Keeffe: Thank you, Chair. Mr. Buti, Ireland obviously contributed from the National Pensions Reserve Fund, its €17.5 billion. Was this part of the deal? Was this a precondition for the bailout?

Mr. Marco Buti: It was not a precondition. I think I can be very formal on this; it was not a precondition. It was a proposal by the Irish Government to do so and I think it was wise to have this national component. I think there were a number of reasons behind this decision. Okay, first of all, I think it was important to, as always in these cases, impress the markets. So we tend, when we fix the financial envelope not to be too stingy because I think it would be problematic if then you realise that you have been excessively cautious and you have to go back to the table and increase it later on. So, it is better to err on the largesse side than on the ... so, I think this element here, this additional €17.5 billion helped to make the envelope more substantial. I think there was also a consideration, I believe, on the part of the Irish Government that - to go back to the issue of interest they charged on the loan - that it would be economically not very rational at the time to have in a sense to pay quite substantial interest charges on the EU assistance whilst this €17.5 billion here was remunerated at a very low ... I think so. I think it made sense in a sense to offer this element here. So this I think was the decision was made and I think that it was the right decision. And, again, I stress that it was not an insistence on the part of the troika, on the part of other governments to say, "Well, this is a precondition for granting the assistance".

Senator Susan O'Keeffe: Going back to the time of the guarantee in 2008, you said that there was no contact from Ireland to you. Was there any . . . sorry, why did the Commission not contact Ireland? I mean, you would have been aware, obviously, of the seriousness across Europe, across the world, in fact, so why could you not have initiated contact? I don't mean you personally, Mr. Buti.

Mr. Marco Buti: We were in contact and we were discussing with all member states at the time given the pretty dramatic evolution of the situation. The only thing I can say is that we were communicated ex post that this decision was made by the Irish Government and we were not consulted beforehand.

Senator Susan O'Keeffe: I do understand that, Mr. Buti, but in terms of conversations that might have been ongoing how . . . if you were . . . you've said you were in touch, how could it be then that this literally falls out of the sky? I mean, if you're having conversation or were the conversations of a different kind? And were you saying, or was the message, "No bank should be allowed to fail"?

Mr. Marco Buti: As I indicated in my previous testimony, that was never a suggestion, a recommendation on an imposition by the Commission on the no bank being allowed to fail. And on the guarantee, I mean, we have to go back to the historical moment at the time. Declarations, decisions, not only by the Irish Government but by several others, came overnight in certain cases. So it was not that we had, as in normal circumstances, long periods of gestation which give rise to a certain ... I think the announcements fuelled by dramatic developments, sometimes panic, came in a pretty, let's say, sudden manner. It was not only the case of Ireland. I can cite other cases in which there was not consultation with the Commission. As I said, and I go back to the prerogatives that we had at the time, which is different than the system we have now with banking, with the ESM, where it deals with responsibilities that, clearly, are different than it was at the time. There was no obligation on the part of the Irish Government to consult the Commission. I simply say that it did not take place.

Senator Susan O'Keeffe: Were you aware that the IMF had made contact with Ireland and that Mr. Mody had come to Ireland in February 2009 to talk about the crisis?

Mr. Marco Buti: We are in close contact with the IMF. We have ... when the IMF, under their regular procedure - an Article IV mission - take place, we are in touch with them and we know that what is the schedule and what is the calendar of these meetings. As far as I'm aware, we must ... we may have talked with them at a very technical desk level, as we always do. I was not personally aware of, let's say, the specific content of the discussions. But I'm not ... given the situation at the time, I'm not surprised by the fact that these ... these discussions could have taken place. And Mr. Mody was responsible for the Article IV mission, so I think it's all natural that that would take place.

Senator Susan O'Keeffe: And that was February '09 and there was more contact in May '09 and, again, in May '10. So was the view of the Commission that, really, Ireland should have come earlier to seek assistance? Was it, by your estimation, at the time, now, I don't mean on reflection, I mean, at the time, did you think, "Are Ireland ever going to come looking for assistance?" Was it clear to you that Ireland needed assistance and would you have preferred for them ... the country to have come earlier?

Mr. Marco Buti: Look, I think the decision to apply for an EU assistance programme with the IMF on top of that is politically a very difficult decision. I mean, there is-----

Senator Susan O'Keeffe: I appreciate that, Mr. Buti, and it's always going to be difficult, but I'm asking what the European Commission's view was ... leaving aside, if you like ... there's always a political dimension, but would you have wanted Ireland to have come sooner?

Mr. Marco Buti: No, I think ... look, the ... we have situations in which countries have waited - I can quote you a couple of examples, even a very recent one - have waited 'til the very, very last moment where they have two stare into the abyss and they could not pay pensions and salaries any more before coming to apply for assistance. This was not the case of Ireland. So, I am not saying that it was ... I don't have a value judgment on this. I'm not saying that when they came, it was exactly the right time ... or, certainly, they did not wait till when it was too late. And, I think the judgment was that the situation became increasingly difficult and, I think, it was good that they came when they came.

Senator Susan O'Keeffe: In fact, Professor-----

Mr. Marco Buti: They could have come a bit earlier. I would have not advised to go much later than that, given the tensions, even though they had a buffer ... still a buffer in the fiscal coffers. But I think it was ... I appreciate the difficulty in the decision. And it was, let's say, the decision to apply at the time did not strike me as being neither too late nor too early.

Senator Susan O'Keeffe: Can I ask you ... can I go back to the letter that Mr. Trichet wrote? I think you said in evidence to my colleague that you were aware of that letter. That's what you said I think, yes?

Mr. Marco Buti: I was aware of the position of the ECB.

Senator Susan O'Keeffe: Yes.

Mr. Marco Buti: I had not ... I did not see the letter at the time.

Senator Susan O'Keeffe: Okay.

Mr. Marco Buti: But I know what the position of the ECB was and, I think, when we have seen the letter published afterwards, it basically reflected the position of the ECB. So there was no ... no real surprise there.

Senator Susan O'Keeffe: So, knowing the position and sharing the opinion are two different things. Did the European Commission share that view? Because, after all, you were going to be in a troika together, you, the ECB and the IMF. Did you share the view that the ECB held at that time that that was the position ... that that should be said to Ireland at that time?

Mr. Marco Buti: I mean, the troika is three institutions-----

Senator Susan O'Keeffe: Yes.

Mr. Marco Buti: -----and we constantly talk together. And it was very clear, in the discussion within the troika, what the position of the ECB was. Us ... we, I think, appreciated that position and, as I indicated, it was not so much for us to say. But the ECB was trusted not only because of their prerogatives and, you know, institutional duties but also because more than the other two components of the troika had the pulse of the market. So when the ECB comes forward and indicates that there is a very substantial risk of dramatic spillovers coming from certain decisions, that cannot be belittled. And if we come to the benefit of doubt, I give the benefit of doubt the ECB.

Senator Susan O'Keeffe: So putting pressure on Ireland in that way was the right thing to do?

Mr. Marco Buti: No, no. What I am referring to is the assessment of the risks involved at the time and, I think, the assessment was, at the time, and is still now, that there were very, very substantial risks involved in the situation.

Senator Susan O'Keeffe: Thank you.

Chairman: Thank you very much. Senator MacSharry.

Senator Marc MacSharry: Thanks very much and thank you, Mr. Buti, for being here again today. Programme monitoring and warning controls are now being undertaken by Government agencies to reduce the risk of returning to a programme. What, in your opinion is the greatest risk that you see to Ireland having to return to a programme of assistance?

Mr. Marco Buti: In the future?

Senator Marc MacSharry: Yes.

Mr. Marco Buti: I think Ireland is in a much stronger position than it was during ... obviously, during the programme. It was in a much stronger position than it was before the programme ... the programme started and, even, I think I would say, even before the financial crisis erupted. Now, the job is not done. I mean, there are still challenges. I mean, we ... for instance, we have a post-programme surveillance which extends in the future - it's going to last, actually, for quite a long time - and we still have important challenges. I mean, the first one is public debt is very high. It has to be brought down in a gradual manner. I don't think that there is a risk, frankly, at this stage of Ireland having to --- having a relapse and going back to a programme. Clearly, we are going to continue to monitor very closely Ireland, as we do with all the other countries - and particularly those that have undergone such a huge adjustment - to make sure that there is good behaviour in the future.

Senator Marc MacSharry: So, what's the risk?

Mr. Marco Buti: I cannot quantify any risk here.

Senator Marc MacSharry: Okay.

Mr. Marco Buti: I say that it's not likely.

Senator Marc MacSharry: You said, in the opening statement that, quote:

> I very much concur with the conclusions drawn by most witnesses that appeared before [the] committee. The post-2007 economic and financial crisis in Ireland was domestically generated. Its roots were not only in the banking sector, but also in pre-crisis fiscal policy making.

You said, in your opening statement, that you believe that Ireland's crisis was domestically generated. Do you agree with Professor Paul Krugman's following statement that:

> The truth [in] [...] the story is mostly monetary. By introducing a single currency without the institutions needed to make that currency work, Europe effectively reinvented the defects of the gold standard[s] - defects that played a major role in causing and perpetuating the Great Depression.

Mr. Marco Buti: I don't agree with Paul Krugman.

Senator Marc MacSharry: You don't agree with the statement.

Mr. Marco Buti: No.

Senator Marc MacSharry: Okay. So would you say it's ... that the single currency's design was flawless and did not contribute to the crisis?

Mr. Marco Buti: No, I have not said that. I don't agree with that either.

Senator Marc MacSharry: Okay.

Mr. Marco Buti: It is ... I referred to, at the end of my statement, that President Juncker said that we still have to continue to build the architecture of - and complete the architecture of - economic and monetary union. There is still a lot to do. We have done a lot with the institutional ... and the reforms done also in ... as a response to the crisis involving Ireland as well. There is still a lot to do. At the same time, if you imply that Ireland would have been better off outside the euro or-----

Senator Marc MacSharry: No, no. I didn't do that.

Mr. Marco Buti: No, you don't say that ... and someone you refer ... to whom you refer to may actually think that. I don't think that would be a statement that I would definitely ... that I would support. I think Ireland has the potential, now, having undergone a very steep and important adjustment, to benefit fully from the advantages of sharing a single currency. And I think the Irish people know better than anybody else what is the right path for Ireland within the euro area.

Senator Marc MacSharry: You said in your opening statement that one of the only points of criticism that you might have is that "the Irish government did not consult with its European partners." You also said that the blanket guarantee, in your view, while on one hand saying the Commission didn't have a view, but then you quickly pointed out that your view was that it probably added to the fiscal cost. Is that a fair assessment?

In John Hurley's opening statement to us here, he said:

> As a result of contacts with the ECB, it was the view at the time that an overall European initiative of which Ireland might be part was remote and that any decisions in relation to Irish banks would ... [have] to be made by the Irish authorities. The Government was expected to stand behind its banks and a Lehman-type situation was to be avoided.

He also said - I continue quoting - again:

> There was a strong view on the night that the Government ... [has] one opportunity to assuage the markets. If the decisions taken were considered inadequate and failed the consequences for the banking system would be devastating and lead to very serious economic and social fallout for the country as a whole.

You said in your statement, again, that the Government should have consulted with the European partners before the guarantee decision, while John Hurley, as I have said, the Governor, believed that there was no help from Europe coming and that Ireland expected ... was expected to stand by its banks and that phrase, "no bank should fail." Would you take issue with Mr. Hurley's statements?

Mr. Marco Buti: It was a very long statement.

Senator Marc MacSharry: It was infinitely longer than that, I can assure you.

Chairman: We don't have all day, though, so if you can respond, please, Mr. Buti.

Mr. Marco Buti: Thanks for summarising. As I said, if one looks now with the benefit of hindsight, the blanket guarantee was a very large coverage and it clearly increased the risks of the perverse loop between the banks and the public. At the same time - at the same time - I think I indicated there, I understand also that the situation at the time was unprecedented and I do not envy those who had to make that decision, having in mind what was in the statement you just ... you've just read. So this is ... I try to apply this type of reasoning of trying to take into account the - let's say the situation at the time, and not judge only on the basis of what we know today, and in particular, not judge on the basis of a successful outcome of the adjustment. I think this is an analytical and conceptual mistake that we should refrain from doing.

Senator Marc MacSharry: But you didn't have a problem making a hindsight judgment of a real-time action yourselves.

Mr. Marco Buti: We have to make, clearly, a judgment. At the time, it was ... it was, as I said, on the bail-in issue as well as on other issues, but when we come to the *ex post* reconstruction, I think we should have a degree of modesty and a sufficiently long memory to understand that ... At the time, you may recall that we had the *Financial Times* website counting the minutes till the euro would collapse. This was the kind of unprecedented life-threatening situation in which we were.

Senator Marc MacSharry: Okay. No, I-----

Mr. Marco Buti: We have stabilised the situation now, but we should not forget the kind of - let's say risks - that we were facing-----

Senator Marc MacSharry: Of course.

Mr. Marco Buti: -----and those circumstances.

Senator Marc MacSharry: So, given the risks - given the fact that Europe at that time didn't have a ... a lifeboat and the suite of decisions open to, say, the Irish Government at the time, do you feel that there was a possibility of an ECB-led initiative to tackle liquidity issues in Europe - if, for example, the decision that night was not a blanket guarantee but to say, "Okay, we're going to liquidate Anglo Irish Bank and Irish Nationwide and we're going to invest money into the others"?

Mr. Marco Buti: I think you are taking me into a - let's say territory - which I would ... I'm not comfortable with-----

Senator Marc MacSharry: No, no. Indeed, I would-----

Mr. Marco Buti: -----and I wouldn't want to, I mean-----

Chairman: You'll be back in again, Senator, one second.

Mr. Marco Buti: -----to have a ... to imagine a counterfactual and speculate on what the ECB could or could ... or could have not done at the time. So I'm ... that's what I can say.

Senator Marc MacSharry: I can understand that completely. The difficulty we have here is, on one hand, in welcoming your assessment that it added cost to the ... it added fiscal cost to the situation, we must also try and assess what other possible options there were, and so, while I can appreciate fully that it makes one uncomfortable to have to consider this, in considering our work here, we must try to see were there alternatives. And, I suppose, given your experience and the seniority with which your position comes, I am asking you to highlight if you feel that if the blanket guarantee was not opted for, what option was better for limiting the fiscal cost, either to Europe or the Irish people, and also in looking after the responsibilities which John Hurley, as Governor of the Central Bank and ECB central governing council member, felt that he had.

Mr. Marco Buti: I mean, what I can say on this is that the blanket guarantee was decided and it was based at the time - I mean, in understandably very difficult conditions - on a misdiagnosis of what the state of the banks were. I mean, the bank ... as I indicated before, you can have a blanket guarantee only if you think that the problem is one of liquidity, not of solvency. And it became clear quite quickly that there was a problem of solvency, not of liquidity. So that's where we stood at the time. I do not want to, let's say, venture into, let's say, counterfactual at this stage and, in particular, not on action that the ECB could have made. I am here representing the Commission, not the ECB.

Chairman: You are on the final question.

Senator Marc MacSharry: Yes, just a very final question. You said in your testimony, when - I think it was Deputy McGrath - that ... the lessons learned or what could have been done with the benefit of hindsight. You said we could have reduced the burden or effects on the least well-off. Isn't that correct? Can I, in just closing off, finally put it to you, Mr. Buti, to bring back to your colleagues in the Commission that there is still time to do that?

Mr. Marco Buti: During the whole implementation of the programme - and, I have to say, I pay tribute here to the Irish institutions, to the Irish stakeholders in general. We had many contacts with the social partners. We had contacts with the NGO - I think Social Justice Ireland - in particular. We listened very carefully to what we were ... we were told, and, I think, as much as possible at the time we tried to lessen the impact on the less well-off. If one looks at the ... at indicators of, let's say, inequality of distribution of income, of material deprivation, etc., you can see that the operation of the tax and benefits systems helped substantially to lessen the impact. This does ... I am not minimising at all the fact that it was harsh for everybody, but in terms of overall, let's say, fairness considerations, I think the programme was implemented adequately. We could have done, I think, even more to protect a certain-----

Senator Marc MacSharry: And perhaps we could-----

Mr. Marco Buti: -----certain part of the population.

Senator Marc MacSharry: Perhaps you might consider further concessions in that regard.

Chairman: Senator Barrett.

Mr. Marco Buti: When we come to the ... when we will come to the future, and in the context of the post-programme surveillance, we have the country-specific recommendations, we are in the process of, let's say, in general, co-ordination surveillance, I am pretty sure that the elements that you put forward will be duly considered.

Chairman: Thank you. Senator Barrett.

Senator Sean D. Barrett: Thank you, Chairman, and welcome to Mr. Buti and his colleagues back again. In the European Commission's *ex post* valuation of Ireland's bailout programme, it stated that the Irish banking sector has been relatively slow to return to profitability, and in the Commission's post-programme surveillance report of spring 2015, reference is made to the low amount of SME financing. In your assessment, has Ireland's banking sector become too risk averse, given complaints by SMEs and particular difficulties in accessing credit?

Mr. Marco Buti: I mean, the ... it is true. I mean, you are correct in stating that the return to profitability has been slow. It has been slow also because, I mean, we have ... I mean, the working out of very large non-performing loans, the reduction of the loss-making activities has taken time. So the banking sector has remained, I mean, loss-making 'til the first half of 2014. Now, does it mean that there is an excessive risk aversion? And, let's say, that there has not been sufficiently, you know, supply of funds to the SME - possibly but not necessarily. I mean, the ... on the issue of SMEs, the system in Ireland is such that there are also other sources of financing which are available and actually we are trying in the euro area, via the initiative on completing the capital market union, to increase the source of finances. I mean, the ... so there is an element here not only of supply side on the part of the banking system, but also on the demand side on the part of SMEs. So, overall, I think the judgment is ... has to be nuanced on this assess.

Senator Sean D. Barrett: When you said we would break the financial and sovereign loop, does that mean that it's the end of "too big to fail" banks or also that no bank should fail, that they would be on their own in the future?

Mr. Marco Buti: What we are doing definitely is to make sure that there is not "too big to fail" syndrome anymore.

Senator Sean D. Barrett: Okay.

Mr. Marco Buti: That ... and this is at the EU level with the implementation of the BRRD, which kicks off on 1 January 2016, but there is also decisions made more globally at the G20 level on the so-called TLAC, so that there is sufficient funds to make sure that these risks can be tackled without having a burden on the taxpayer which is unduly excessive, and the system that we have in Europe with the bank resolution and recovery directive, which requires 8% of the liabilities to be bailed in before public intervention is certainly a pretty tough conditions. The ... what we have now it is clearly a different legal and institutional setting that we had at the time. Certain choices that were made at the time would be made differently under the current conditions but the legal certainty and the much reduced risks of litigation is one of the advantages of the reforms that have been taken over the past years and, clearly, the reduction of the risks compared to the time wherein decisions were made in Ireland.

Senator Sean D. Barrett: Did the quality of risk-taking in banks decline when the model moved from depositor-saving finance to wholesale and then to emergency financing from the ECB and from central banks? Did you see a decline in the quality of lending and risk assessment by banks in that period?

Mr. Marco Buti: This is essentially related to the pre-crisis period when the mounting imbalances were, you know, below the radar screen actually accumulating and, certainly, the move to more wholesale financing for the banks, the concentration of risks essentially related to the housing market with the ... you know, the portfolio being essentially concentrated on that, clearly led to a deterioration of the situation, and Ireland and we all paid, you know, a heavy price for that.

Senator Sean D. Barrett: I think we had some banks that had 8% of their lending to industry and agriculture and 88% to property. Would the Commission monitor and seek to rebalance that kind of lending, were it to ... pattern ... were that pattern to recur in the future?

Mr. Marco Buti: No, I think what we ... I recalled when I had my first testimony here that we were under the curse of the great moderation at the time because, I mean ... and what we did, we had a very ... a pretty narrow view. We thought that the financial system ... I think this was not only the Commission was ... I think the main international organisations, we had the view that the financial system did not *per se* ... *per se* ... we create, create problems. So we know that that was not the case. Now clearly we are in a different situation. I think it is not so much for the Commission *per se* to monitor this but we have with banking union the SSM so the responsibility for financial supervision at the European level and I am pretty sure that in ... one of the advantages of the current system with the single supervisory mechanism is to break the sometimes cosy ... excessively cosy relations within the national setting making sure that problems of that sort will not accumulate in the future. I'm pretty sure the SSM will ring the bell should something of this ... let's say a portfolio imbalance of this sort emerge again.

Senator Sean D. Barrett: Yes. I welcome what you said because, while GDP is growing, the public perceives a massive transfer from them to the financial sector so they are actually still worse off even though GDP is welcome, it's increasing again, so measures to prevent those kind of transfers in the future from the Commission or national central banks, ECB, I think that's what the people want to come from an inquiry like this.

Mr. Marco Buti: I appreciate that. I think the, the key challenge for Ireland in the future is not only to grow ... to ... but also to grow steadily and to create wealth and create jobs. I mean, I appreciate also that there is a lag between the recovery coming forward now. Clearly, I mean, I quoted before the figure coming out ... that came out this morning. So now it is pretty vigorous. I think we can start to see the job creation and the unemployment coming down steadily - quite quickly - but there is a lag in perception. I think when we come to our responsibility here to

... of surveillance at the EU level, in particular the Commission, we are going certainly in the future to look more to the composition of growth. What is comforting from the latest figures for growth in Ireland is that if one looks at the composition, there is a strong component of investment, and investment helps not only in the short term but also, provided that is not misallocation of capital, it also improves the ... let's say, the situation looking forward, because it adds to potential growth. So I am overall consciously but definitely optimistic about the policy and the economic predicament for Ireland in the future.

Senator Sean D. Barrett: Do we need protection against asset price bubbles? That's my final question.

Mr. Marco Buti: All this multi-form assessment, which is ... takes place in terms of the financial system essentially by the new institution in the banking union, a single supervisory mechanism. And what we are doing at the European level, I'm confident that will allow to spot more, you know, in a more rapid fashion, in a more comprehensive way the imbalances coming, as one of the important innovation that we have in the new co-ordination system is the macroeconomic imbalances procedure. And the macroeconomic imbalances procedure should help precisely to tackle the issue that you, you highlight. Ireland is subject to macroeconomic imbalances procedure and as part of the surveillance we will look also at the ... let's say, avoid the first signs of possible accumulation of risks and a new bubble, knowing that memory is very short usually.

Senator Sean D. Barrett: Right.

Mr. Marco Buti: And, I think the Commission is here to try to insert in the policy game a longer-term perspective than those of elected politicians, including you all.

Senator Sean D. Barrett: Thank you very much. Thank you, Chair.

Chairman: Point taken and noted, Mr. Buti. If I can maybe just invite Deputy McGrath in to deal with his own wrap-up and then I have a couple of questions I wish to conclude with as well, Mr. Buti. Deputy McGrath.

Deputy Michael McGrath: Yeah, thanks Chair. Mr. Buti, the end of June 2012 summit agreement statement, which provided for breaking the vicious circle between the banks and the sovereigns, and it opened up the prospect of direct recapitalisation through the ESM - and that facility is now up and running, as I understand it - that was heralded in Ireland at the time as a major breakthrough and as the forum through which Ireland would get a deal on retroactive bank recapitalisation. Where stands that today?

Mr. Marco Buti: That is an instrument that is indeed available. We are again ... and I repeat and I hope that in the future things may change ... we are in an intergovernmental setting. So, it is ... this is not an instrument which is under the responsibility of the Commission. My hope is that in the future, we would integrate the ESM in the context of the Community setting, and we would streamline and make more efficient the decision-making on that, but this is not for now, it is for the future and the decision of the ESM is made by the member states, and there is unanimity rules on this, so everybody has to agree. The conditions for using the direct recapitalisation are made pretty stringent. So far, let's say, the prevailing view on the part of the member states has been that ... not to consider this as a suitable instrument. Now, if one takes the situation as it stands now, independently of the decisions that could have been made in the future, the question is "Is that necessary or wise now to have that?" I think the situation now has improved substantially and there is an upside in terms of the banks' situation. So should, I think, at this stage ... maybe it is wiser for the Government to benefit from the upside, rather than to leave it to the ESM.

Deputy Michael McGrath: Sure.

Mr. Marco Buti: So in the present situation I think the issue of the direct recaps, for different reasons, does not seem to be on the agenda, any time soon.

Deputy Michael McGrath: Okay and is it the case that there hasn't been any application from any member state yet under the direct-----

Mr. Marco Buti: No.

Deputy Michael McGrath: -----recapitalisation instrument?

Mr. Marco Buti: No.

Deputy Michael McGrath: There hasn't been. Finally, you had an exchange with Senator MacSharry there about the guarantee and the costs, and I just want to put it to you: on the one hand you're saying the guarantee was too generous and magnified the fiscal impact of the banking crisis, but on the other hand, you are defending the insistence of the ECB and the Commission that senior bondholders would not have any losses imposed on them. And I put it to you that there is a contradiction in both of those positions because the only way that the costs of the banking bailout in Ireland could have been lessened is if you either don't repay senior bondholders or depositors take a haircut. Junior bondholders suffered very large losses; equity holders were wiped out effectively, so how could you lessen the cost of the bank bailout without imposing losses on senior bondholders?

Mr. Marco Buti: The blanket guarantee went well beyond the senior unsecured bondholders. So, that is, one could have had, let's say, a more restrictive application of the guarantee still sparing the senior bank bondholders. So this is ... so there, basically the blanket guarantee covered everybody and that, with the benefit of hindsight, may have been excessive.

Deputy Michael McGrath: Well I think you're ... to bring it down to the net point, you're referring there to dated subordinated debt. Undated subordinated debt was not included. There was about €12 billion of dated subordinated debt included in a €375 billion guarantee, and about €1.4 billion of that dated subordinated debt fell due for repayment and was repaid during the guarantee. So, is that the only net point of difference?

Mr. Marco Buti: No, I think we're talking about the-----

Deputy Michael McGrath: What else are you talking about?

Mr. Marco Buti: We are talking about existing debt that we hold, so it's also new debt. I think the guarantee was indeed blanket, so it covered everything that exists in future.

Deputy Michael McGrath: Yeah but existing debt was senior debt as well, so I put it to you that there's a contradiction in what you're saying.

Mr. Marco Buti: No, the ... I'm not saying that the ... a possible alternative would have included senior debt ... and that, I don't think it would have been wise at the time but it could have been ... it could have been - and I said it in a very modest way considering the difficulty at the time - it could have been, let's say, less expensive considering other form of debt.

Deputy Michael McGrath: But in terms of the fiscal cost, very modestly less.

Mr. Marco Buti: Possibly, modest less, yes.

Deputy Michael McGrath: Or else present alternative evidence if you can, but-----

Mr. Marco Buti: No. I take your point. I think it's ... that's correct.

Deputy Michael McGrath: Thank you.

Chairman: Thank you, Deputy McGrath. I just want to deal with one aspect of that and then I've got some questions as well I wish to wrap up with. On the issue of burning bondholders, which has been expressed back and forth here this morning, and given that part of the exiting of a bailout programme requires the sovereign to acquire funding outside of the assistance programme, would the burning of bondholders and the matters that Deputy McGrath is referring to ... if that had happened, would the Irish sovereign been able to get access to independent funding outside of the structural programme earlier or later, or would it have had any impact whatsoever in your opinion Mr. Buti?

Mr. Marco Buti: I'm not sure I have grasped, let's say, the essence of your question. I don't think there is a relation really in terms of the timing between the two decisions. I've replied before to whether it would be ... it was too late or was too early. I think the decisions made at the time were ... I think it was due but maybe your question was more complex than this.

Chairman: No. The question is if the Irish Government hadn't honoured the debt it had taken on board by sovereignising the banks' debts, and had left it be burnt. The earlier discussions we had this morning with Mr. Chopra and others are very clear that there was both a banking crisis and a fiscal crisis in Ireland, and Ireland was going to enter a structural programme regardless. The nature of a structural programme is that you are now with a lender of last resort - that is, the only person that can give you money or is prepared to give you money. But as you exit the bailout programme, other lenders become available, as has been witnessed in Ireland where we returned to the bond markets and bonds got cheaper over a period of time.

Mr. Marco Buti: Yes.

Chairman: So, if Ireland had actually burnt that sovereign debt, that was originally banking debt, would it have had any impact whatsoever, in your opinion, with Ireland getting access to funds on the international market?

Mr. Marco Buti: I cannot tell, I cannot tell. What I can say only is what we have observed ... is that Ireland was able under the setting of the programme, to go back to markets already in July 2012, well before what, I mean, the schedule of the programme itself, which was, I think, an excellent result and largely unexpected at the time. This was based on the decision not to proceed with the bail-in of senior unsecured bond holders. Now, I do not ... I cannot tell you about the counter-factual - what I can tell you is that what happened was indeed a very positive element which, if anything, if one takes a prudent approach, would testify in favour of what was ... what the decision was on ... was at the time.

Chairman: Okay. And just coming back to Mr. Chopra as well this morning, in his engagement with the committee, he placed the IMF as a partner in the troika, but one could take an interpretation from that that the IMF was not the senior partner or maybe not an equal partner in that regard and I would like just to test that idea at the moment. So, in that regard, would you say that the IMF was equal to the European Central Bank and the Commission and was an equal partner in that structure and, subsequently, in the negotiations?

Mr. Marco Buti: In the troika we had three institutions and all decisions made, sometimes after very harsh discussions I have to admit, were made by the three institutions together and everybody, including on the matter of bail-in, would be comfortable with. Clearly, there was a bit of give and take in all this-----

Chairman: Okay.

Mr. Marco Buti: -----but the IMF was an equal partner as the other institutions. Mr. Chopra in the IMF has repeatedly indicated that is, you know, is the partner with longer ... the longest experience on this and I think we greatly benefitted from that experience and the ... we... I'm pretty sure also that the IMF would recognise that they have benefitted from our own knowledge on how the ... a country in the euro area faces challenges which are not purely national and domestic but having broader relevance for the function of the currency union.

Chairman: Okay. And in that regard, with the IMF's long experience in dealing with programmes and the relative, if little or no, experience that the European Union had as ... in the wider entity, there is a position articulated that the IMF were of the view through their long experience that the position being articulated by the European Central Bank and maybe the European Commission was too severe in its austerity approach. Would that be accurate?

Mr. Marco Buti: I would not subscribe to that statement. I think what we had at the time was already the implementation of the Stability and Growth Pact and the excessive deficit procedure in a pretty lenient manner. Initially, we had given four years instead of one for the correction of the excess deficit. We had the ... from 2013 to 2014 before ... already before the programme was actually agreed ... and, in the context of the programme, 2015 so as the deadline. All this was discussed within the troika. The IMF may have had a preference for a slight less ... slightly lower adjustment, but it was really a marginal one. The issue ... there was not really a difference in terms of the overall correction of the deficit - 2015 was agreed by everybody. I think us, considering the size of the public debt ... the size of the deficit ... the fact that Ireland is a very small, very open economy so fiscal adjustment in a sense it has in macro-economic terms lower costs than the more closed economy. We thought that in order to regain credibility we would be ... there should be an up-front correction that is ambitious whilst being realistic and reasonable. That's what we applied, and if one looks at what has happened since then in the implementation of the Stability and Growth Pact, I think this position here can be largely supported.

Chairman: All right, Mr. Buti, just two final questions I want to deal with. The last one I will take as ... I will allow you a bit of time to maybe just give your final remarks to the committee, but one is a specific item in relation to NAMA. And when developer Mr. Michael O'Flynn in evidence before this inquiry ... when he was here what he said was that, "NAMA was intended to save the Irish banking sector, but in fact hastened its demise and along the way added to the burden on the Irish taxpayer". Amongst the reasons cited was an inability on the part of NAMA, according to Mr. O'Flynn, to recognise the cyclical nature of the economic downturn and make a longer term view of asset realisation and maximisation of proceeds. What is your assessment of that statement by Mr. O'Flynn and were there any credible alternatives to the NAMA model by your reckoning?

Mr. Marco Buti: No, I don't want to go into the details of that, but I think-----

Chairman: Of the person, yes, but in general.

Mr. Marco Buti: -----no, that statement ... I think that statement overall ... I would not support that statement overall. I think we ... the sales of loans to NAMA in 2009 ... at 2009 values effectively insulated the banks of further decline in the property market. I think loans were sold at their long-term economic value. I think what our ... so, our experience in general with NAMA, even though it was not part of the adjustment programme-----

Chairman: Okay.

Mr. Marco Buti: -----so one has to be aware also that we were in touch as part of the overall discussions but we did not influence NAMA and we did not have privileged access, is that ... our experience is that the NAMA has worked very well. High professional people who definitely helped in supporting bank liquidity and favouring the access to the ... eventual access to the euro system. So, I would say that comment was in my personal view too harsh.

Chairman: Okay. Finally, and you can add any further comments you wish to this in terms of looking ... going into the future or in terms of recommendations, Mr. Buti, but in the European Commission's *ex-post* evaluation of Ireland's bailout programme, it is stated that while the burden of fiscal adjustment was shared quite widely, overall it was the younger generations who were hit harder by the crisis. And I think there has been some noting in there that while people may not have become unemployed they would have maybe lost their jobs or they would have less income ... not in terms of losing the job, but would have had less incomes and more outgoings to meet. Could I maybe ask you to please elaborate on this evaluation with particular reference to those in receipt of social welfare income versus those on earned income, however?

Mr. Marco Buti: The fact that the young adults have seen let's say the sharpest decrease in their living standard I think is a fact. I mean in a ... in this ... I mean is in a context of high youth unemployment and increasing university fees, reduction in unemployment benefits which had to be implemented at the time. I think others let's say suffered less. We assess and try to implement the programme in a way that would reduce the burden on those individuals also. As I indicated before, one could have possibly done things in a more targeted manner. What-----

Chairman: The proposition there, Mr. Buti, that I am saying is that there's no question that people saw significant drops in their incomes and so forth. Your proposition is that they were the ones that seemed to have picked the ... or been impacted upon the hardest. But in contrast to people who were not working whatsoever, who had lost their jobs, 24% of the Irish economy was in construction. Thousands upon thousands of those people lost their jobs and had to go on social welfare. Would you say that it was those that remained - and by your proposition it would imply - that those who remained in employment were the ones that were actually impacted most in that age category as opposed to people who actually were reliant upon social welfare?

Mr. Marco Buti: Look, this, okay, this is the assessment of the *ex-post* evaluation ... by the way is an independent ... even though we think the Commission is an independent *ex-post* evaluation I think that statement is largely ... that assessment is largely correct. I think that statement is largely ... that assessment is largely correct. It is ... we ... I mean the system and the Irish economy had to undergo a dramatic change in model of development and the shedding ... the very large shedding of labour in the construction sector led to that type of impact and those ... that ... so young adults, males maybe in particular, suffered more than other parts of the population. I think that's a fair ... it's a fair assessment. With the hope is also now that with growth coming back that there will be also within the labour force those who will benefit more from the revival of growth in the present circumstances and in the future.

Chairman: Thank you very much, Mr. Buti. I'm going to bring matters to a conclusion. Is there anything you would just like to mention by means of closing remark or comment?

Mr. Marco Buti: I ... only to say that I would like to thank you institutionally but also personally for the invitation. I think we have as European Commission accepted very gladly your invitation to come here. I have been ... I've tried to be as ... let's say, as open and transparent as possible for what I know. I've told you everything I know following your questions. I think ... I hope this is appreciated also institutionally by the committee. I think this ... you're doing an important job.

I think my final word is the perspective should be if one looks at the experience with this programme, what could have been done better. Possibly that is the perspective but in the acknowledgement that the programme was by all standards a success. And I take the example of other Community programmes within the euro area and with the EU and I take the standard also of other IMF-only programmes outside Europe. So from that viewpoint, I think the programme is a success. Then one can look at the data and here and there certain things could have been done but I think we have learned a lot from this experience of this programme but overall, I think we are confident that should the economic policy of Ireland continue to be anchored to stability, reforms, growth, fiscal prudence, that the future of Ireland is bright.

Chairman: Thank you, Mr. Buti. And in wrapping up this session, I would like to thank you for your participation here today and for your engagement with the inquiry and to also formally acknowledge the ECB's assistance and co-operation with the inquiry ... sorry ... yes I wish, I wish ... the Commission's co-operation and assistance with the inquiry right from the outset in its various stages. So with that said, the witness is formally excused and I propose we break for one hour to return at 4 p.m. Is that agreed? Agreed.

Sitting suspended at 3.03 p.m. and resumed at 4.10 p.m.