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Joint Committee of Inquiry into the Banking Crisis

Witness Statement of

Mary Coughlan

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¹ See s.37 of the Houses of the Oireachtas (Inquiries, Privileges and Procedures) Act 2013

Joint Committee of Inquiry into the Banking Crisis

Statement in writing by Ms. Mary Coughlan pursuant to a direction under Section 67(1) of the Houses of the Oireachtas (Inquiries, Privileges and Procedures) Act 2013

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I am directed to make a statement in writing to the Joint Committee of Inquiry into the Banking Crisis (the “Joint Committee”) on the list of questions provided to me (and now repeated below) relating to those lines of inquiry relative to my role as Tánaiste. Given the particular questions asked, in making this written statement I have necessarily also had to draw on my roles prior to my nomination as the member of the Government to be the Tánaiste.

By way of background, I was first elected as a Teachta Dála for Donegal South West in February 1987 and was returned as a member of Dáil Éireann at each subsequent election until February 2011. From February 2001 to March 2011, I served in the following successive roles in Government:

- Minister of State at the Department of Arts, Heritage, Gaeltacht and the Islands (with special responsibility for the Gaeltacht and the Islands);
- Minister for Social and Family Affairs;
- Minister for Agriculture and Food;
- Minister for Agriculture, Fisheries and Food;
- Tánaiste and Minister for Enterprise, Trade and Employment;
- Tánaiste and Minister for Education and Skills; and
- Tánaiste, Minister for Education and Skills and Minister for Health and Children.

I welcome the opportunity to make a statement in writing to the Joint Committee. At the outset, I would like to put on record my regret at the difficult consequences felt by so many families across Ireland arising from the banking crisis. Its unforeseen and dramatic impact resulted in hardship in many homes and placed immediate hopes and aspirations out of reach in many others. It was a hugely difficult period post-September 2008.

As the Joint Committee may appreciate, it was an extremely challenging time to serve as a member of the Government. Taking the action we believed necessary to address the crisis, stabilise the public finances and place Ireland on a sustainable path to recovery involved a

series of difficult, unpalatable and, in many cases, unprecedented decisions. With Government comes that responsibility however and I know that I and my colleagues, together with so many very dedicated public servants, worked tirelessly during that period to do everything we could to address the crisis in good faith and in what we believed to be long-term best interests of the Irish people.

To what extent did we get everything correct? Only the passage of time will tell. As with certain domestic decisions pre-2008 which contributed to the extent of the crisis, Government policy and decisions are taken at a particular moment in time with the best advice then available to Government – it can be many years later before we come to learn of and understand their full effect. While the nascent economic recovery presently underway would indicate that the path we set out upon in 2008 – albeit a difficult path – was the correct one, it is my hope that in the decades ahead that we can look back and see that this was so.

In addressing the questions asked by the Joint Committee, I set out below my response in the order set down in the direction received. Note that in preparing this statement, I did not review or have access to the papers, files or other materials held by any Department in which I served as Minister and the answers given are based on my best recollection from the period concerned.

1. R1b *In your opinion is the current supervisory regime robust enough to prevent another crisis?*

e.g. i) in the event of a rapid rise of market interest rates, and its impact on household and commercial debt

e.g. ii) in the case of a Euro-related crisis, such as Greece leaving the Euro

It became evident in the analysis that followed the decision of the Government in September 2008 to provide financial support in the form of a guarantee to certain credit institutions in order to maintain the stability of the State's financial system and the subsequent enactment by the Oireachtas of the *Credit Institutions (Financial Support) Act 2008*, that the State's then supervisory regime had failed to prevent what we now know to have been grossly excessive and irresponsible lending to the property sector in the State and had failed to properly judge the level of exposure and risk that had accumulated in the State's credit institutions.

The supervisory architecture and approach then in place emphasised compliance with governance processes over analysis of credit institution lending decisions and exposure. This, together with the division of responsibility for macro and micro prudential supervision – split as it was between the Central Bank and Financial Services Authority of Ireland (the “Central Bank”) and its constituent part, the Irish Financial Services Regulatory Authority – had resulted in a situation where the overarching objective of the stability of the financial system was failing to directly inform the supervision of individual credit institutions.

To address this failing in the supervisory regime, in addition to the appointment of new personnel to lead the supervisory institutions, we took a decision to fundamentally reform the supervisory architecture and significantly strengthen the supervisory regime. My recollection is that this significant and complex legislative task was to require three pieces of legislation. The first was to provide for a revised unified corporate structure within which the Governor of the Central Bank and the Chief Executive Officer of the Irish Financial Services Regulatory Authority could operate with enhanced powers. The second was to enhance further the powers and functions of the unified, restructured and re-named Central Bank of Ireland regarding the prudential supervision of individual financial institutions, the conduct of business, including the protection of consumer interest, and the overall stability of the financial system. The third was to consolidate statutory arrangements for the Central Bank of Ireland and financial regulation in the State.

The first of these pieces of legislation was enacted by the Oireachtas in 2010 as the *Central Bank Reform Act 2010*. It provided for the establishment of a single fully-integrated Central Bank of Ireland (by re-integrating the Irish Financial Services Regulatory Authority into the Central Bank) with a more complete remit over prudential regulation and financial stability issues. It provided the new entity with additional powers to prevent potential serious damage to the financial system in the State, to support the stability of that system and to protect users of financial services. It also provided for oversight on the performance of the Central Bank of Ireland by a committee of the Oireachtas.

While the 30th Dáil Éireann was dissolved on 1 February 2011, the *Central Bank and Credit Institutions (Resolution) Bill 2011* was presented to Seanad Éireann on behalf of the then Minister for Finance on 28 February 2011.

While not being directly engaged on developments in the supervisory regime since the appointment of the current Government on 9 March 2011, I welcome and am broadly supportive of the actions of the current Government in seeing through the work we commenced to reform the supervisory regime. In that regard, I note, in particular, the subsequent passage of the *Central Bank and Credit Institutions (Resolution) Act 2011*, which provides the necessary mechanisms to enable the Central Bank of Ireland to intervene where a credit institution gets into serious difficulty and is in danger of becoming destabilised or otherwise failing, and the *Central Bank (Supervision and Enforcement) Act 2013*, which further strengthens the ability of the Central Bank of Ireland to impose or supervise compliance with regulatory requirements and to undertake timely regulatory interventions.

In my opinion, the reformed supervisory architecture and strengthened supervisory regime established by the *Central Bank Reform Act 2010* and further enhanced by subsequent legislation has equipped the Central Bank of Ireland with the mandate and tools necessary to ensure robust regulation of the credit institutions within its remit. Properly resourced, diligent exercise of these tools, the performance of such exercise being informed by the lessons learned since 2008 and now the subject of oversight by the appropriate committee of the Oireachtas, should ensure that Ireland's financial system is never again jeopardised by such reckless business decisions on the part of Irish credit institutions.

2. **R1b** *From your time at Cabinet, can you outline whether any concerns or reservations were expressed about the strength or quality or regulation of the financial sector in Ireland?*

It is my recollection that, prior to September 2008, during my time as a member of the Government no concerns were expressed within Government regarding the strength or quality of regulation of the financial sector in Ireland. While

there was considerable debate from 1999 to 2002 following publication of the *Report of the Implementation Advisory Group on the Establishment of a Single Regulatory Authority for the Financial Services Sector*, it is my recollection that, while debate focused on the need to rationalise and improve significantly the protection of consumers of financial services and the structure by which the new single regulatory entity would be accountable to the Oireachtas and the judiciary, there was never a concern that the then current day-to-day regulation of Irish banks was not robust enough.

As outlined in my response to question 1 above, it became evident post September 2008 that the revised architecture for regulation, introduced in 2002 and placed on a statutory footing in 2003, in practice operated in a way that, ultimately, proved not fit for purpose. Considerable time and energy was expended within Government in the period post-2008 to fundamentally reform the supervisory architecture and significantly strengthen the supervisory regime culminating in the actions taken as outlined in my response to question 1 above.

3. **R2b** *During his Hearing in the Context Phase of this Banking Inquiry, Prof. Fitzgerald said (Volume 1, No 7, page 333): “There was a cultural change in the Department of Finance in the last decade. It became more concentrated about the politics of things and less interested in the technical detail. I would have had less interaction.” Would you like to give us your own view on these comments?*

While I note the perspective of Professor FitzGerald, whom I respect, I can only give a view from my perspective in dealing with the Department of Finance as a line Minister. Throughout my career in Government, routine interactions occurred with the Department of Finance regarding annual budgets, spending analysis, output statements and on the detail of new or revised schemes/initiatives. These were, in my experience, always very robust encounters, in particular where there was an impact on spending. It is my opinion that no obvious change in approach occurred at my level of interaction with the Department of Finance that would warrant concluding that there was a “cultural change” of the type articulated by Professor FitzGerald.

4. **R2b** *What discussions can you recall about the likelihood or otherwise of a “soft landing” in the property market in the period up to 2008? Bearing in mind that there was an increased level of warnings in the public domain.*

While my recollection is that the Irish economy continued to receive favourable assessments from most domestic and international commentators, including from the International Monetary Fund and the Organisation for Economic Co-operation and Development, from 2007 reports and commentary in the public domain began anticipating a softening in growth momentum, a reduction in consumer demand and a decline in activity in the construction sector. It is my recollection that, taken together, the varying views on the Irish and international economies fused to form a “soft landing” consensus for Ireland (including in relation to the property market), being the view articulated by both the then Central Bank and the Economic and Social Research Institute. My recollection of discussions at a political level in this regard is that they would have focussed on what measures were necessary to address the impact of the forecasted slow-down rather than on questioning the underlying premise of the expert analysis and advice being received by Government.

5. **R2b** *In your view was there discussion at Cabinet about the level of increase in bank lending in the years up to 2008 and the risk to the Irish economy that this might cause?*

The members of the Joint Committee will be aware that I am constrained in terms of detailing discussions held at Cabinet.

In general terms, I would comment that lending by credit institutions in Ireland in the period up to 2008 underwent rapid change in the context of strong demand, new entrants in the banking sector and increased banking competition. It would have been the consensus view that increased competition in the Irish market was welcome from a policy perspective, but the Government would have relied on the Irish Financial Services Regulatory Authority in terms of the appropriate regulation of lending by credit institutions given its independent

statutory role in that regard. My recollection is that no material concerns were articulated to Government prior to 2008.

In terms of risks to the stability of the financial system, again, the Central Bank had the independent statutory role in that regard and my recollection is that no material concerns were articulated to Government prior to 2008.

6. **R3b** *What is your view as to how the regulatory/supervisory bodies dealt with the financial services institutions they were charged with overseeing? Do you believe that their engagement with the financial institutions was sufficiently robust?*

It is clear today that the State's then regulatory/supervisory bodies exercised an inadequate form of regulatory control over the credit institutions that they were charged with overseeing. With the benefit of hindsight, the principles based approach was clearly not robust enough and a more intrusive form of regulation and oversight is required. It is my hope that the reformed supervisory architecture and strengthened supervisory regime established by the *Central Bank Reform Act 2010* and further enhanced by subsequent legislation has equipped the Central Bank of Ireland with the mandate and tools necessary to ensure robust regulation of the credit institutions within its remit in the future.

7. **R4c** *One of the statutory objectives of the CB is 'the promotion of the financial services industry in Ireland'. In your view was there a conflict between this objective and the Financial Regulator's responsibility for prudential supervision?*

Section 5A(1)(b) of the *Central Bank Act 1942*, as then standing amended by the Section 5 of the *Central Bank and Financial Services Authority of Ireland Act 2003*, included among the general functions and powers of the Central Bank "to promote the development within the State of the financial services industry (but in such a way as not to affect the objective of the Bank in contributing to the stability of the State's financial system)".

The complete text of this particular function established by the Oireachtas for the then Central Bank gave a very clear direction as to the nature of such promotion. My own view, principally informed from my work on the promotion of the Irish financial services sector while serving as Minister for Enterprise, Trade and Employment from 2008, is that robust and sensible regulation is a selling point in attracting the right type of financial services sector investment. Investors jurisdiction-shopping in search of a less than robust regulatory environment are to be avoided.

While it is for others to articulate if, in carrying out their duties in the then Central Bank, they felt a conflict did arise between its various functions, the combination of regulation and promotion in any statutory body has – particularly in times of difficulty – the potential to give rise to the perception of a conflict. In that regard, in introducing the *Central Bank Reform Act 2010*, I consider that we made the right decision to remove this function and to put in place an unambiguous regulatory focus for the restructured Central Bank of Ireland.

8. ***R4c*** ***What level of contrarian or independent expert advice is sought by Oireachtas and its Committees when examining key issues? Is such advice sought regularly or only on an exceptional basis?***

During my time as a Teachta Dála prior to my appointment as a Minister of State, I served on, or was in regular attendance at, a number of committees of the Oireachtas, including the Joint Committee on the Irish Language, where I held the position of Chairperson, and the Joint Committee on Tourism, Sport and Recreation, where I held the position of Vice-Chairperson. From 2001 to 2011, as a Minister, I regularly appeared before relevant committees of the Oireachtas to inform, to debate and to account for key budgetary and policy initiatives of the Government and my Department.

Both as a back-bench Teachta Dála and as a Minister, it was my experience that committees were appropriately resourced to obtain such expert advice as any such committee deemed necessary to assist it with its enquiries. Oireachtas committees had very significant powers, including to: send for persons, papers

and records; take oral and written evidence; invite written submissions and oral presentations from interested persons or bodies; draft recommendations for legislative change and for new legislation; require principal office-holders in State agencies or bodies to attend a meeting to discuss their official responsibilities; engage specialist or technical knowledge; print and publish reports and related documents; appoint sub-committees and request a plenary debates, among others.

While the dynamics of each committee differed depending on its membership, in my experience, committees provided a particularly important platform for opposition members of the Oireachtas. Opposition members generally led the charge in questioning and holding a Minister or relevant official to account, including through marshalling the resources and powers available to the committee and inviting the views of contrarian opinion or seeking independent external advice.

9. R5a *Did the government consult the Oireachtas and its Committees through a pre-legislative consultative process prior to any of the major policy decisions taken in the years running up to the crisis and during the financial crisis? Has it done so since September 2008?*

During my time as a Teachta Dála, there was an evolution in the role of committees of the Houses of the Oireachtas, from their being no formal system of committees following my first election in 1987, to their establishment in the early 1990s and, post-2002, providing significant detail of their formal role in the revised Standing Orders of Dáil Éireann. I understand that this role has been added to with the introduction of a formal concept of pre-legislative scrutiny involving committees of the Oireachtas introduced to the Standing Orders of Dáil Éireann having full effect from January 2014. It is a further evolution of the legislative process and role of Oireachtas committees that I welcome.

I would not distinguish between pre and post 2008 in terms of my time as a member of the Government in this regard, but would comment generally that it was my experience that before a bill was initiated in the Oireachtas, the

proposal would have already been through a number of stages of scrutiny within Government (including being the subject of a regulatory impact assessment) and, in some instances, externally, such as being the subject of white paper or the subject of another process of consultation with members of the public or a number of stakeholders. In many instances the subject matter of a bill would also have been extensively debated in public and have been the subject of discussion by a relevant committee of the Oireachtas. Committees, of course, set their own agenda as to what matters they wished to address or propose initiatives on to the Government of the day.

Clearly, in the case of urgent exceptional circumstances, the level of consultation that a Minister may wish to engage in prior to the publication of legislation is necessarily truncated, as would have been the case in the emergency situation which arose in September 2008. I understand such a carve-out has also been included in the new pre-legislation scrutiny process formalised with effect from January 2014 in the Standing Orders of Dáil Éireann.

10. R5b *What is your view of the quality of advice provided by the Department of Finance to the Government and in particular the analysis on which that advice is based?*

Department of Finance advice would have been provided to the Minister for Finance in the first instance and the Minister would have considered that advice in bringing to Government his views and proposals. As a Minister outside of that Department, it is not possible to give a fair appraisal on the quality of advice provided on a day-to-day basis.

In terms of advice provided directly to Government prior to 2008, the Department of Finance would have made submissions on a regular basis to Government on economic and financial policy issues and on Departmental proposals as and when they arose. Principal among its submissions each year was the annual June memorandum to Government outlining the economic outlook and the budgetary framework within which the annual budget was to be delivered. I had no reason to assume at any time that the advice given was

based on anything other than sound analysis of the various metrics, inputs and economic views available to the Department of Finance. While, as a Minister in another Department, I would have had at times a different perspective on priorities and on the best approach to take within my sector, that discussion formed part of the annual engagement with the Department of Finance during the budgetary process.

From mid-2008, the advice provided to Government focussed on dealing with the developing economic and banking situation. The Department of Finance exhibited commendable dedication to public service at a very difficult time in developing and implementing solutions to assist the Government in its determination to close the gap between income and expenditure – starting with the budgetary adjustment announced in early July 2008 – and to stabilise the State’s banking and financial system.

- 11. R5b** *On occasions, advice was received from Department of Finance containing warnings and the Government chose not to follow this advice from the Department of Finance, would this have been a matter for discussion?*

It was my experience that Department of Finance advice was always taken into consideration in the development of budgetary proposals. In addition to that advice informing the overall budgetary framework, the advice and position of the Department of Finance was central to the detailed annual engagement and discussions between Departments during the budgetary process.

- 12. R5c** *Was there a point, in your recollection, prior to September 2008 when the sustainability of the Budget was thought to be in material difficulty.*

It was clear by summer 2008 that the sustainability of the budget was in question, with the Exchequer returns for June 2008 showing tax revenue some 7% behind profile. As a result, the Government proceeded immediately to take corrective action by way, initially, of the public spending adjustment announced on 8 July 2008. This was followed, post September 2008, with the October emergency budget and publication of the framework for sustainable economic

renewal titled, “Building Ireland’s Smart Economy”, work on which had commenced in the summer months.

13. R5c *Programmes for Government and Social Partnership Agreements were key drivers on the Expenditure side. In your view how appropriate were these plans in light of the volume and sources of available income to fund these policies.*

In the period to 2008, Programmes for Government and Social Partnership Agreements were both drivers and enablers of Government policy. Drivers of tax and expenditure policy, yes, but also enablers of significant public sector and economic reform.

Programmes for Government, including to this day, set out the basis for a five-year programme of work between coalition partners in forming a Government based on the respective strengths of the parties involved and their commitments to the public in the context of a General Election. It is my view that, in a democracy where no single party Government had been formed in over 25 years, they are an appropriate mechanism by which a newly formed Government can set out its agreed policies so that it may be held to account, in particular in its initial years in office immediately following a General Election. The content of any given Programme for Government is necessarily dictated by the economic circumstances in existence and foreseen at the time it is negotiated.

The same principle applied to the negotiation of Social Partnership Agreements – the economic circumstances in existence and foreseen at the time such agreements were entered into dictated the terms of the final agreement. While social partnership has played an important and effective role in delivering industrial peace and facilitating economic development since 1987, it did, over time, grow to encompass areas of policy well outside its original remit. While this expansion of its remit drove additional focus on public expenditure, my perspective is that – rather than available resources being the issue (this was a matter of fact during any given period) – the consequence of such dilution of its mission was a diminished focus both on the delivery of public sector reform,

modernisation and flexibility, and on ensuring competitiveness across the economy generally.

14. R5d *Would you support the view that the dominance of Oireachtas by Government in terms of setting the agenda affected Oireachtas' capacity to perform its oversight and accountability roles with respect to the stability of the financial system?*

It is for each House of the Oireachtas to set its own agenda. In our form of parliamentary democracy, the election of the Taoiseach and subsequent appointment of a Government necessitates commanding a majority in Dáil Éireann. While that majority may subsequently exercise effective control over the agenda of that House, it is important to remember that only up to fifteen members of that majority are in fact members of the Government. The balance of members may have a mandate from their respective constituencies to support that Government, but that does not mean that they cannot and do not exercise an independent mind in influencing the agenda of the Oireachtas and this would have been my own experience.

While the influence of members supporting the Government was generally very effectively exercised in the parliamentary party room, in the public arena, it was the opposition members who took the lead role in holding a Government of the day to account. This oversight and accountability role was most effectively achieved, in my opinion and experience, in the detailed work carried out within committees of the Oireachtas where opposition members led the agenda. As highlighted in my answer to question 8 above, Oireachtas committees had very significant powers to assist them in undertaking that task.

Therefore, while conscious of the particular challenges for opposition and potential dangers in terms of accountability and oversight where a Government commands the support of an overwhelming majority of members in Dáil Éireann, I do not subscribe to the simplistic view that a Government automatically dominates the setting of the agenda of the Oireachtas or that it can ultimately curtail the opportunity of and obligation on all members of the Oireachtas to carry out their oversight and accountability roles to the best of

their ability.

In that regard, I am hopeful that the additional oversight role entrusted to a committee of the Oireachtas by the *Central Bank Reform Act 2010* on the performance of the Central Bank of Ireland will in time prove itself an effective additional layer of scrutiny and accountability over the guardians of our banking and financial system.

15. R5d *Can you outline your experience on how the relationship between the government and the banking and property sectors operated during your period in Cabinet?*

The relationship between Government, the banking sector and property sector was appropriate and professional at all times. In terms of my own engagement with the sectors, it would have been relevant to my respective Ministerial function at the time. My recollection is that, in both cases, that engagement would have been primarily in the context of my role as Minister for Enterprise, Trade and Employment – by way of example, engaging with the banking sector on the availability of credit for business to sustain and create jobs post September 2008, engaging with the property sector in devising innovative solutions to the apprenticeship situation following the collapse of the domestic construction sector and promoting the Irish financial and construction sectors overseas in the context of Enterprise Ireland led trade missions.

MARY COUGHLAN

7 August 2015