TUARASCÁIL ón gComhchoiste Fiosrúcháin i dtaobh na Géarchéime Baincéireachta

An tAcht um Thithe an Oireachtais
(Fiosrúcháin, Pribhléidí agus Nósanna Imeachta), 2013

REPORT of the Joint Committee of Inquiry into the Banking Crisis

Houses of the Oireachtas
(Inquiries, Privileges and Procedures) Act, 2013

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Volume 2: Inquiry Framework
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EBS: Core Book 36

January 2016

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THEME: B1

Effectiveness of banks' board governance, client relationships and business models

LINE OF INQUIRY: B1a

Composition, skills and experience of the board and board subcommittees

EBS Building Society

Minutes of Nominations Committee Meeting held at 16:00 on Thursday 29 January 2004

Present:	Yvonne Scannell (chair), Brian Joyce, Ted McGovern, Mark Moran
In Attendance:	Joe Ryan (secretary)
Apologies:	Michael Moroney, Ethna Tinney As the only items on the agenda were consideration of recommendations to the Board on the re-election of Michael Moroney and Ethna Tinney, respectively, it was arranged that they would absent themselves from this meeting.
Re-election of Michael Moroney:	Brian Joyce, chairman of the Board, reported on the outcome of his discussion with Michael Moroney following receipt of the individual director evaluation (based on the evaluation forms completed by the other 10 directors and collated by Jim Bruce). Having considered this, the Committee decided to recommend to the Board that it supports the re-election of Michael Moroney.
Re-election of Ethna Tinney:	Brian Joyce, chairman of the Board, reported on the outcome of his discussion with Ethna Tinney following receipt of the individual director evaluation (based on the evaluation forms completed by the other 10 directors and collated by Jim Bruce). Having considered this, the Committee decided to recommend to the Board that it supports the re-election of Ethna Tinney.

Signed: Dr Yvonne Scannell

Date: 13/03/04

EBS Building Society

Minutes of Nominations Committee Meeting held on Wednesday 24 January 2007

Present:	Yvonne Scannell (Chair), Ted McGovern, Mark Moran, Michael Moroney, Emer Finnan (Secretary).
Minutes:	The Minutes for the meeting held on 21 December 2006 were agreed and signed.
Non-Executive Directors Recruitment:	The Committee discussed the proposal to nominate Jim Ruane as a director. All three referees contacted spoke very well of Jim Ruane and in view of these recommendations and the unanimous opinion of the Committee on Jim, it was agreed to nominate him as a director at the next Board meeting. A proposed contract of appointment for new directors sourced from the Institute of Chartered Secretaries and the Prospectus book on corporate governance, was also discussed. Minor amendments are necessary and members are to respond to the Secretary with these. All new directors will be asked to sign this contract which must first be approved by the Board. The selection of other new directors was discussed. There are currently four promising candidates, on whom informal feedback is good. It was agreed how to progress the further evaluation of each of the candidates.
Process for re-election of directors:	Procedures for the renomination of existing directors were also discussed. The Chair reminded members of the recommendations of the Combined Code with respect to the re-election of directors. The Nominations Committee considered these recommendations and if it could recommend to the Board whether it should support Ethna Tinney's re-election. The following were considered: ♦ Ethna's performance as a Director has been formally independently adjudged to be well below average in the two formal board evaluations to date; ♦ Ethna's performance since the last formal evaluation is still not considered to be of the standard required; and ♦ There is a lack of fit between Ethna's skills and what the Nominations Committee deem to be the required skills for the Board, in the context of the need to progressively refresh and strengthen the Board. The view was that the Nominations committee could not support the recommendation to the Board for a third term of office and that the interests of the Society would not be best served by supporting Ethna for re-election for the third time. However, in light of the seriousness of this and in order to provide Ethna with an opportunity to make representations to the Committee, it was decided to defer making a final decision on the Nominations committee's recommendation to the Board with regard to the re-election until the meeting on 8th February 2007.
Next meeting:	8th February 2007.

Signed: Dr Yvonne Scannell

Date: 22 March 2007

EBS Building Society

Minutes of Nominations Committee Meeting held on Thursday 8 February 2007

Present:	Yvonne Scannell (Chair), Ted McGovern, Mark Moran, Michael Moroney, Emer Finnan (Secretary).
Minutes:	Some changes were proposed to the minutes (of the previous meeting held on 24 January 2007) which will be put through and the minutes will be considered at the next meeting.
Matters Arising:	None.
Non-Executive Directors Recruitment:	• Mark Moran provided an update on [redacted] who will not be going forward due to time commitments. • Mark Moran has called [redacted] • Ted Mc Govern has spoken to [redacted] and he would be interested. He has been away for a couple of weeks and a meeting will then be set up. • Yvonne Scannell has tried to contact [redacted] [redacted] to progress. These candidates will continue to be progressed. If one of them is not interested contact will be made with [redacted] and [redacted] Yvonne Scannell also mentioned [redacted] and [redacted] At some appropriate time in the future we need to close off on all candidates previously spoken to.
Director's Contract:	The Secretary tabled the revised contract and some minor amendments were noted which will be incorporated and the contract will be sent to Arthur Cox for their review.
Re-election of director:	Mark Moran updated the Committee on his meeting with Ethna Tinney on 6th February in Limerick at which he apprised her of the Committee's deliberations. He also reported that Ethna confirmed she did not wish to make representations to the Nominations Committee. Following a discussion the Nominations Committee decided to recommend to the Board that the Board should not support Ethna Tinney's re-election as a Director at the upcoming AGM, after considering the points raised at the last meeting: • Ethna's performance as a Director has been formally independently adjudged to be well below average in the two formal board evaluations to date; • Ethna's performance since the last formal evaluation is still not considered to be of the standard required; and • There is a lack of fit between Ethna's skills and what the Nominations Committee deem to be the required skills for the Board, in the context of the need to progressively refresh and strengthen the Board.

To: **Board of Directors**
EBS Building Society

From: [redacted]

Date: **30th March 2006 Board Meeting**

Re: **Corporate Governance Standards**

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1. Introduction

As a non-executive director with experience of corporate governance in varied business environments the experience in EBS over the last twelve to fifteen months has been difficult. The environment for me, as a non-Executive Director changed once I began to challenge the executive handling of key business agendas starting with Project Nova, followed by the emergence of the 5m Special Pension Contribution to the Managers and Senior Managers Pension Fund and finally with the handling of Executive Remuneration, pension and retirement benefits in the Remuneration Committee.

It is my first experience of being corporately "bullied" as a Director because of positions I have articulated. However, it has reinforced in me an understanding of and commitment to the need to implement the Corporate Governance Standards set out in the Combined Code in EBS Building Society.

The EBS Building Society is slowly and painfully emerging from a legacy Building Society governance culture. Many key decisions were vested in the CEO/Chairman axis and non-Executive Directors and many Sub-Committees were either administrative or little more than rubber-stamping.

If EBS Building Society is to preserve its mutual status with the special protection expected in the new legislation, then this governance culture will have to change fundamentally, if we are to serve members responsibly and act with their ownership interests in mind.

In EBS, I don't yet see an appreciation of how much the corporate governance environment has changed in recent years and the Society is losing momentum, when in fact, given it's trustee type status, it should be leading the field in standards of Corporate Governance.

The recent appointment of the new CFO and Head of Strategic Development has made a hugely significant contribution to improved financial and general management standards. This is most welcome, however these advances must be augmented within a transformed corporate governance framework.

I suggest that EBS engage Professor Niamh Brennan, Director of the Institute of Directors Centre for Corporate Governance in UCD to conduct a Corporate Governance Audit and to help develop a blueprint for the society that we might also take to the members for adoption. The paper on Corporate Governance Datacheck, presented by [redacted] at the BSA Conference in 2004 merits revisiting in this respect.

I appreciate the support from the Senior Independent Director and Vice Chairman, who is a member with me on the Remuneration Committee, on these issues.

2. Corporate Governance and the Adoption of Combined Code Standards by EBS

"Anyone taking up a senior appointment at a mutual must recognise the unique status of such an institution and the need for correspondingly greater, rather than lesser, standards of accountability and governance".

Steve Huxham Investors Association

An active, well informed, and independent Board is necessary to ensure the highest standards of corporate governance. The Combined Code on Corporate Governance sets out standards in relation to these issues.

All directors, executive and non executive, have overall and equal responsibility for the leadership of the Company. The Companies Act does not distinguish between the two.

A director must act as a reasonably diligent person who has both the general knowledge, skill, and experience that may reasonably be expected of a person carrying out the same function as that director and the actual general knowledge skill and experience of that director. Accordingly, the experience and expertise of the Director will determine the standard of care expected from such a Director.

Non-executive director should:

- Ensure the company provides them with sufficient information
- Seek clarification or independent advise when they are in doubt, and
- Raise matters of concern for board consideration.

In terms of the standards required of all directors, in the 'Equitable Life' - judgement it emphasises:

- Their collective and individual duty
- Delegation does not absolve the directors concerned.
- Each case will be fact specific

The Combined Code provides that as part of their role as members of unitary board, non-executive directors should constructively challenge and help develop proposals on strategy. Non-executive directors should scrutinise the performance of management in meeting agreed goals and objectives and monitor the reporting of performances. They should satisfy themselves on the integrity of financial information and that financial controls and systems of risk management are robust and defensible. They are responsible for determining appropriate levels of remuneration of executive directors and have a prime role in appointments and where necessary removing executive directors and in succession planning.

3. Chairman & Chief Executive Officer

The Combined Code states that there should be a clear division of responsibilities at the head of the company between the running of the board and the executive responsibility for the running of the company's business. No one individual should have unfettered powers of decision. The roles of chairman and chief executive should not be exercised by the same individual. On appointment, the chairman should meet the independence criteria set out in the Combined Code but in practice he is not considered independent thereafter.
In law, the chairman has no greater power that any other director apart from chairing both the board meetings and the company's AGM. In contrast, the chief executive officer (CEO) or managing director will usually have express or implied authority to perform certain duties for the company.

EBS Comments on the Higgs Report were as follows:

The roles are separated. The responsibilities of the CEO are set out in writing (in his employment contract) but the division of responsibilities between the Chairman and Chief Executive has not been committed to writing.

The Division of responsibilities between the Chairman and Chief Executive needs to be committed to writing.

As a non-executive director this area presents difficulty to me and has in the past vis a vis governance of the Nova Transaction, Remuneration Committee and General Board Governance. It is something I have raised with the Chairman.

4. Duties of non-Executive Directors

The duties owed by a non-executive director are, in substance, no different from those owed by an executive director. The statutory provisions that apply to directors make no distinction between executives and non-executives. Non-executive directors also have the same rights of access to information about the company as executive directors. They are expected to satisfy themselves that proposed actions are in the best interests of the company by calling for appropriate information.

Non-executive directors are expected to carry out their functions with skill and care and owe their company the full range of fiduciary or trustee-type duties. As a non- –executive director is likely to be expected to carry out a narrower range of functions that an executive director, in practice his exposure is therefore likely to be correspondingly reduced. **However, a non-executive** director cannot rely only on the fact that a course of action is recommended by the executive members of the board. In a judgement in the Equitable Life case in October 2003, Mr. Justice Langley stressed that:

- It is no longer the case that directors may place unquestioning reliance upon others to do their job; and
- The extent to which a non-executive director may reasonably rely on the executive directors and other professionals to perform their duties is plainly 'fact sensitive' – i.e. it will depend on the particular circumstances.
- Mr. Justice Langley added that it was 'plainly arguable…. that a company may reasonably at least look to non-executive directors for independence of judgement and supervision of the executive management'.

5. Liability for breach of fiduciary duty

If a director acts in breach of his fiduciary or trustee-type duties and the company suffers loss as a result, that director will be personally liable at common law to compensate the company for the loss.

The Companies Act contains the following protection regarding any proceedings for negligence, default, breach of duty or breach of trust against a director. If it appears to the court hearing the case that director is, or may be, liable but has acted honestly and reasonably, and that having regard to all the circumstances he ought fairly to be excused, and court may relieve him, either wholly or partly, from his liability on such terms as it thinks fit. However, in the Equitable Life judgement mentioned above, Mr. Justice Langley commented that, while the Companies Act contemplates the possibility of a court concluding that it should relieve an officer without a full trial, it would require a quite exceptional case for a court to grant relief without such a full trial.

6. Sub Committees

In accordance with Board Manual version 1.7, 18th January 2005 the definition of Matter Reserved for the Board include the Terms of Reference and membership of Committees and Boards.

The Remuneration Committee Terms of Reference state that "the Board shall periodically review the membership of the Committee"

To my knowledge, no board review of the membership of this committee took place in advance of the Chairman's decision to appoint two additional non-executive Directors to the committee and subsequently ask an existing member to step down.

7. **Remuneration Committee**

The committee should consist of at least three (or, in the case of smaller companies, two) members, who should all be independent non-executive directors. The remuneration committee should make available its terms of reference, explaining its role and the authority delegated to it by the board. The committee should have delegated responsibility for setting remuneration for all executive directors and the chairman, including pension rights and any compensation payments. The committee should also recommend and monitor the level and structure of remuneration for senior management. Under the Combined code, the Chairperson of the Board is not eligible to chair the Remuneration Committee, because in practice, he is not considered independent.

8. **Nomination Committee**

A majority of the members of the committee should be independent non-executive directors - the Chairman of the Committee should be either the Chairman of the Board or an independent non-executive director.
Higgs also recommended that no one director should sit on all three board committees, audit, nominations and remuneration simultaneously.

9. **Independence**

My understanding of the issue is based on the Higgs Review of 2003 circulated to me by EBS and the commentary circulated by Company Secretary [redacted] He also circulated the EBS detailed reply to the Central Bank of Ireland Controls Report on the application of Combined Code within the Society.

In the EBS Annual Report and Accounts 2004, we designated five non-executive directors as Independent. At our "off site" Board meeting on $17^{th}/18^{th}$ June 2004, a paper on "Governance" was presented by the Company Secretary focussed on ways to improve board effectiveness.

It referenced the Non-Executive Directors meeting of 12th February 2004 at which it was noted that a number of directors are not independent per Higgs. On Page 10, the following was presented to the Board

10. Board Independence "at least half the board, excluding the Chairman, should ….. be independent"

Brian Joyce (Chair)

(Ind.)	
Ron Bolger	John Cullen
Cathal Magee	Ted McGovern
Barbara Patten	Mark Moran
Yvonne Scannell	Michael Moroney
Ethna Tinney	Joe Ryan

Higgs recommends that the Board should identify in its annual report the non-executive directors in determines to be independent. The Board should state its reasons if a director is considered to be independent, notwithstanding the existence of relationships or circumstances, which appear relevant to its determination. (Higgs defines these circumstances/relationships in his report).

In our Annual Report & Accounts 2005, I note that, it is stated that

"The Board is fully satisfied that all non-executive directors are independent".

I don't recall the Board considering this issue since June 2004. It does appear that the statement in 2005 marks a departure from Board policy on the Combined Code Standards. The question then arises, what standards do we benchmark ourselves against in terms of Corporate Governance of the Society.

I think it is important to clarify that there is no implication that a Non-Executive Director, who is not designated as 'Independent', for whatever reason, under the Combined Code has any shortcomings in terms of being an effective non-executive Director. It simply means that by virtue of that designation, under the Combined Code, there are compliance protocols to be observed in terms of overall Board membership and in particular the membership of the Remuneration and Nomination Sub Committees. If a Board is in compliance with the Code in this respect the issue of 'independence' does not further arise. Given our policy, in any review of membership of the Board or Sub Committees, Compliance with the Standards of Combined Code should be the starting point.

When Directors fees were reviewed by Remco in February 2003, the fee increase, which was higher than usual, was expressly justified on the more onerous responsibilities for Directors arising out of Higgs and the Combined Code.

10 EBS AGM

The EBS AGM was scheduled to take place on 24th April 2006.

The [redacted] rang Directors suggesting a change of date from the 24th to 18th April. I indicated that because of vacation plans made with family, the proposed new date would not work for me as I would be in USA. I received a further email from [redacted] on 15th February '06 stating that

> "Yes it is unfortunate. Everyone else can make it and due to the legislation Brian and Ted felt that it was better to move it."

It is noted that neither the Chairman or CEO discussed with me before deciding to change the scheduled AGM date.

In the update note on Legislation to the Board on 28th February 2006 it was stated

> "the intention will be to publish a bill around the end of April/first week in May with the legislation being enacted before summer recess, end of July."
> "It was also stated that end of April is probably the earliest that it could be published."

At the Board meeting on 28th February 2006, the Chairman advised that [redacted] would remain on the Board until the 2007 AGM. [redacted] had earlier in 2005 stated to the Board that this was his last year as Director and that he was stepping down. It is worth noting, in this context, that with the EBS AGM scheduled to take place on 24th April 2006, [redacted] would not have been eligible to remain as a Director of EBS having reached the age of 70 on [redacted] 2006. This is the day after our rescheduled EBS AGM on the [redacted] 2006 which means it becomes possible for [redacted] to remain on the Board until next AGM.

11 Appointment of Non-Executive Director

The EBS placed large public advertisements in the national media seeking to recruit new non-Executive Directors to the EBS Board arising out of a vacancy emerging with [redacted]. An Executive search and selection consultancy was also retained to drive the process.

Seven months later, no proposals for an appointment have emerged from the Nominations Committee. I am not aware of how many candidates were shortlisted and interviewed for the role in first and secondary phases of the recruitment process.

In the buoyant Executive market of today with high calibre individuals with significant interest in non-Executive roles, I am astonished that no suitable candidates are emerging for consideration for appointment now.

EBS has made a virtue of its approach to open recruitment of non-executive Director roles, but it reflects poorly on the governance of the society if having initiated a process, attracted significant interest, having the resources available to search the market as well over six months, that the process has failed to bring forward a suitable candidate.

12 Remuneration Committee

There have been a number of governance issues that have presented difficulties within this committee. I will identify in headline terms only the major items:

- The Early Retirement Package for Executive Director, [redacted] which did not come before the Remuneration Committee for approval.

- The Term Sheet Offer/Remuneration Package for new CFO, which had wider pay policy considerations, was agreed with him directly before reference for consideration and approval by Remuneration Committee.

- A Towers Perrin Review on Senior Management Remuneration including CEO, was commissioned by the Remuneration Committee in February/March 2004, to report by the 30th April 2004. The Remuneration Committee did not receive this Report until it's Remco meeting of 24th May 2005. This was after the new remuneration package for new CFO had been executed. During the previous 12 months a number of papers on market positioning and on the structure of the reward package had been prepared and presented by Towers Perrin to EBS but none of these papers were brought forward to Remco for consideration

- The minutes of the Remuneration Committee have been particularly problematic.
  The Chairman has been critical to me of my approach to minutes of the Remuneration Committee.

13 General

Higgs recommends that where a non-executive director has concern about the way in which a company is being run or about a course of action proposed by the Board, these should be raised with the Chairman and fellow directors and non-executive directors should ensure their concern are recorded in the minutes of the board meetings if they cannot be resolved.

14 Way Forward

In the circumstances of the dynamic that has developed around these issues, I am proposing to the Board that we engage the services of Professor Brennan to conduct an audit and report to the Board with recommendations within a couple of weeks. The existing governance structure would remain in place without change in the meantime.

Memorandum

To: [redacted]

From: Ron Bolger, Senior Independent Director

Subject: Corporate Governance and other concerns

I have reflected carefully and at length on the Board meeting of 30 March 2006, especially the last segment of it, and the events leading up to it. In particular I have reviewed my papers from Board, RemCo and BACC meetings over the last 18 months.

For the last 18 months the Corporate Governance environment in EBS Building Society, at Board and Committee, has seriously deteriorated. Individually and collectively as a Board of Directors we all bear responsibility. As [redacted] I feel a particular burden of responsibility. Despite my efforts to provide professional guidance and advice and to support the best interests of the Society I now find myself being personally discredited when I speak out.

I would like to outline a number of areas where deficiencies have brought us to this current unacceptable state:

- Serious breakdown in communications and trust between the [redacted] and three of the independent directors, [redacted]
- Breaches of the sanctity of the confidentiality of discussions between the [redacted] and [redacted] in particular between the [redacted] and myself as [redacted]
- The overwhelming lack of independence at Board level where three of the non-executive directors have served for terms of [redacted] and one NED has a significant cross directorship. The three Executive Directors can never be considered independent. The Combined Code dictates that at least half the Board, excluding the Chairman, are independent. The consequences for the few truly independent directors are to make it more difficult for them to properly exercise their responsibilities,.
- The effect of this lack of independence on crucial committees can be seen as follows:
  - Remuneration Committees should comprise only independent directors in accordance with the Combined Code. Up to 2005, two of the three members were independent but struggled and failed to exercise adequate control over a number of crucial issues; the independence of the committee is then hugely undermined by the addition of two members who are not independent. The stated objective of the Chairman is to get 'balance' on the Committee.
  - The Combined Code states that Nominations Committees should have a majority of members who are independent directors, whereas only 1 out of the 6 members on the EBS Nominations Committee is independent.
  - The lack of movement and refreshing of non-executive directors on the Board and Committees which to date has only occurred when a director reaches 70 years of age, gets ill, or dies.
  - The manner of the handling of new director recruitment/selection which is totally driven by the current [redacted] with minimal involvement from the Nominations Committee.
  - The presumption of the [redacted] when, in calling for a vote of confidence in himself on [redacted] 2006, he indicated that he "has the votes in his pocket anyway". Additionally stating to me, post the AGM, that he will be reappointed as [redacted] at today's Board meeting and, if I allow my name to go forward for appointment as [redacted], that I will be defeated.
  - The handling of the €5m cash injection into the Manager and Senior Managers' pension schemes, occurring at a time when the [redacted] was negotiating a special deal with [redacted] to exit his role as [redacted]
  - The subsequent reporting by the [redacted] of his investigation into the €5m payment to the 16 March 2005 Board meeting which contrasted with the eventual report of 5 December 2005 by the [redacted] on the same matter.
  - The same [redacted] report indicating "when asked by Ted and subsequently Brian …" when, in fact, it was to be the [redacted] on behalf of the RemCo who was to be in control of that investigation.
  - The resistance by the [redacted] to the distribution of the [redacted] report to all members of the Remuneration Committee and his subsequent circulation to the entire Board but without formal discussion or any time for consideration of the issues. The existence of the Report is not minuted in the meetings of the relevant RemCo or Board.

- The commissioning by the Remuneration Committee of a report from Towers Perrin to be completed in May 2004 and eventually received for the meeting of 24 May 2005 and the lack of follow through of a key aspect of that report, namely the LTIP which would form the basis for the Senior Executive bonus arrangements going forward. (The effect being that half way through the LTIP performance period, no objectives or measurement systems have been put in place yet.)
- The escalating cost of (particularly) the Senior Managers' Pension Fund has been of great concern to the RemCo. In accepting the considerable salary increases recommended in the TP report, the RemCo sought to obtain a higher contribution from senior executives to more fairly distribute the cost of their pensions. An executive contribution of 10%, up from 5%, was agreed on 23 June 2005. However within a week this was put on ice following a memo from the CEO and despite the [redacted] believing that 10% was being contributed, the position remains at the lower level.
- Despite the assessment of the [redacted] by the Remuneration Committee granting him a 32% bonus (i.e. 80% ranking of a 40% pool), this being recorded in the minutes as 35% (almost a 1/10th hike which is then applied to a package of many hundreds of thousands of euros in value) and the attachment of a subsequent paper – for the first time – seeking to provide workings for the 35% figure.
- The emails from the independent directors of the Remuneration Committee to the Chairman regarding the Minutes of RemCo meetings and the failure to accurately reflect decisions taken.

These points are in addition, and at a high level, to the detail contained in the Memorandum dated 30 March 2006 from [redacted] to the Board wherein he refers to being corporately "bullied" with regard to a number of issues. As [redacted] I personally told the Chairman that he should review his own performance in the context of the Corporate Governance issues raised and in particular I would not support his attempt to force the removal of [redacted] from membership of the Remuneration Committee, which was the Chairman's intent for the Board meeting of 28 February 2006.

The Board meeting of 21 October 2005 indicated that the [redacted] were investigating an alternative approach to Board evaluation to be carried out in the first 6 months of 2006. We are now more than half way through that period and there has been no further reporting or action. It is totally inappropriate that the [redacted] should be involved in the establishment of a Board evaluation procedure. This is a job for the Chairman, assisted by the Company Secretary, and a job that cannot be delegated.

Such an evaluation can add great value to the workings of a Board. I believe that properly conducted by a credible authority the issues which are the subject of this Note and the Memorandum of 30 March 2006 by [redacted] can be investigated, brought openly onto the table and resolved in a depersonalised and business way. A Corporate Governance audit by an independent authority would add great weight to the workings of the Board of EBS Building Society and its sub committees.

I strongly recommend that no decisions on leadership of the Board should be taken pending the results of such an investigation/audit/evaluation.

Unless the Board of EBS Building Society takes the appropriate immediate action to deal with these governance failures, then the onus is on me, as [redacted], to hand these issues on to someone else who will force changes upon us, the Financial Regulator.

The unacceptable standards of governance bring in to disrepute what is portrayed as the "Most Trusted Brand" and of which best corporate governance is not optional.

Finally, I set out on the attached page some relevant extracts from the Higgs Review to assist the Board's consideration of these matters.

[redacted]

20 April 2006

EBS Building Society

Minutes of Board Meeting held on 12 June 2006 at The Radisson Hotel.

Present:	Brian Joyce, Ron Bolger, Ted McGovern, Alan Merriman, Michael Moroney, Tony Moroney, Barbara Patton, Cathal Magee, Yvonne Scannell, Ethna Tinney, Emer Finnan (Secretary).
By Conference Call:	Mark Moran.

Special Board meeting to consider corporate governance issues:

Barbara Patton introduced the topic saying that this meeting was called as a special meeting to deal with corporate governance issues that were tabled recently by some of the directors. As already agreed David Duffy from Prospectus has been asked to prepare a report based on the pre-reading circulated to all Directors, however, for scheduling reasons this has not been produced as yet. It will be produced over the next couple of weeks and brought to the Board. In the meantime Emer Finnan has prepared a desk research paper on the corporate governance issues raised and how we compare to our peers.

There is general agreement that the issues currently preoccupying us go beyond corporate governance, however, they are also around relationships and trust and these issues also need to be addressed.

Emer then presented the paper which covered the following:

1. The Combined Code
2. Building Societies application of the Combined Code
3. Top Irish plcs application of the Combined Code
4. Independence
5. Board Committee Membership
6. Board Evaluations
7. Appointment of Directors
8. Role of Chairman and CEO

The conclusion was that EBS performs very well in comparison to our building society peers in the UK and the top 11 ISEQ companies. On the topic of independence for example all the 11 companies have directors with tenure over 9 years or with cross directorships who are considered to be independent.

[redacted] then tabled a paper which addressed the points raised in [redacted] paper which was tabled on 30th March 2006 and [redacted] paper which was tabled on 20th April 2006.

[redacted] then tabled a paper which addressed the points raised in [redacted] paper which was tabled on 30th March 2006 and [redacted] paper which was tabled on 20th April 2006.

A discussion then took place where all directors contributed and gave their point of view. [redacted] tabled a paper which he circulated. The overwhelming view was that these issues had dragged on too long, were undoubtedly damaging the Society and need to be brought to a conclusion. /.........

Special Board meeting to consider corporate governance issues (cont'd):	At the end of the conversation the chairman asked each director, given where we had arrived in our discussions, whether they believed that board relations were repairable. A sizable majority of the Board said that they were not while one director reserved his position. The chairman then closed the meeting and asked the directors to consider what had been discussed. He said he would arrange to meet with both [redacted] and [redacted] separately in advance of the next scheduled Board meeting.

Signed: B. Joyce

Date: 29/6/06

record in the minutes that [redacted] departure package had not been approved by [redacted] This hardly constituted an example of leaving legacy issues behind us. At the end of that meeting I concluded that I would have to recommend to the Board that [redacted] should no longer be a member of [redacted]. I went to [redacted] to inform him of this. I explained to him what I wanted to do and I had hoped he would resign from the Committee at my request as any reasonable director might do. The reason for wanting to remove him from the Committee was due to the fact that the nature of his contributions were constantly undermining the effectiveness of the Committee. Non-executive directors are expected to **constructively** challenge the issues? But the nature of [redacted] contributions were couched in negativity, intransigence and recrimination.

There is not and never has been any effort on my part to prevent or hinder any Board member from expressing a point of view sincerely held. This is a fundamental principle on which we operate. It is, however, unacceptable to engage in ill-considered, repetitive, intemperate outbursts with colourful language that manages to cause offence to the audience and results in polarisation. The essence of a good non-executive director is to have the ability to express an unpopular concept with a sensible degree of diplomacy and regard for his/her audience. Additionally, he/she needs to know when to stop gnawing on an over-chewed bone and move on. There is a need on the part of a non-executive director to have a collegiate and collaborative approach as opposed to an aggressive confrontational one. The latter can and does bring out the worst in people. When the Chairman is engaging in push-back of bad behaviour or the Executive rebuts assertions made or challenges judgements which they believe to be incorrect they are doing no more than their job and it does not amount to corporate bullying in any shape or form. [I think in truth that one could argue that [redacted] has more to answer to as a bully than anyone else around this table]

[redacted] lack of collegiality is exacerbated by his lack of time for EBS. He is a poor attendee sometimes arriving late and departing early; frequently consulting his Blackberry during meetings and invariably on his mobile at breaks. He rarely seems to engage in any kind of dialogue with his colleagues on the Board. I would believe that all of this is a contributory factor to his 'disconnect' with the main body of the Board. This situation has now been compounded by his taking on another non-executive directorship which he did not consult me about beforehand. It is fundamental that a non-executive director has an adequate amount of time to give to the Society to add some value and in [redacted] case this is not evident. Had he consulted me about his new [redacted] I would certainly have voiced these concerns to him at the time.

SUMMARY

The issues raised in the two papers are <u>not the substantive issues at all</u>. In my view the <u>substantive</u> issues are:

(a) It was clearly time for a change at the Head of our Finance Function and we parted company successfully with the incumbent.

(b) In his place we recruited a top class Finance Director who is clearly adding value.

(c) We made a €5m contribution to the Pension Fund and have since agreed to follow it up with a further contribution to bring it to the Minimum Funding Standard. We are in no way unique in this regard. The Society has obligations in relation to funding our Scheme's obligations and there are compelling arguments why this has been the correct approach to take.

(d) There were lessons to be learnt from the manner in which the €5m contribution was made. These lessons were taken on board swiftly and a number of changes to due process put through as a result.

(e) The Chief Executive got the correct bonus based on his performance rating using the same formula as used in previous years. This has been explained repeatedly.

(f) The REMCO was dysfunctional and was being used as a stalking horse for self-serving agendas. It has made real progress since it was strengthened.

(g) [redacted] are Independent within the meaning of the Combined Code and the change in our interpretation of Independence was arrived at in an open and transparent fashion. Our approach to Independence is in line with the Top Ten ISEQ companies and our change in interpretation progressed transparently through Nominations Committee, BACC and Board

(h) The Nominations Committee is taking care to recruit a worthy candidate or candidates who will enhance and enrich the composition of the Board and ideally expand the choice of directors from which the next Chair will be chosen.

(i) There is little doubt that we have a far better compliance level with the Combined Code that many of those who are obliged to adopt it.

(j) The Chairman had an obligation to bring forward the injudicious behaviour of [redacted] in making calculatingly divisive remarks about the Chief Executive to his subordinates.

Corporate Governance has been used as a Trojan Horse to magnify complaints that have neither merit nor substance. They are cobbled together to make it look as if there are serious breaches of governance when in fact they are nothing of the kind. The disappointment of the [redacted] in not being seen as a [redacted] by his colleagues on the Board is understandable but understanding does not stretch to overlooking his conduct since or his retrospectively making common cause with [redacted] who seems unable to take off his [redacted] hat when he comes to meetings. The interests of the Society are not served by this behaviour and the dissidents need to explain to the rest of us their real motivation. Nothing they have written in their March and April submissions identify any <u>substantive</u> issue at all.

[redacted]

12th June 2006.

TO:	**BOARD MEMBERS**
FROM:	[redacted]
DATE:	**12th June 2006.**

re:	**Corporate Governance and Related Issues**

1. INTRODUCTION

I've been a [redacted] for [redacted] years and before that headed up several very large departments within both the [redacted] and the Dublin branch of [redacted]. I've been very fortunate in the colleagues I've worked with, the variety of business experiences I have been exposed to and the bosses who over the years have challenged and counselled me, but most importantly developed me.

In that time I've acquired a very strong set of personal and business values and a business philosophy which is totally focused on doing the right thing and aspiring to be the best in all that you do. This philosophy recognises the centrality of developing, nurturing and engaging your people as the best means of delivering meaningful levels of customer satisfaction, retention and depth of relationships which translates into a long-term quality earnings stream and in turn a strong business franchise.

I understand the importance of corporate culture and the fact that 'soft drives out hard'. Get the soft stuff right and over time the hard business results will follow. And culture starts at the top. For EBS that means it starts in this room. We all need to be very conscious of our responsibilities in this regard.

On a few occasions along the way in my career I've inherited a blame culture. I always seek to eradicate this swiftly replacing it with a culture of clear accountability and learning. I try to do this by example. People get the message and they thrive as a result. In a blame culture people are scared and they conceal things. This takes you into a downward spiral of fear, distrust and recrimination with predictable results. Mistakes happen in every organisation. The acid test is the way you react when it happens to you. But I've never actually experienced a blame culture myself. Until now. Over the past eighteen months or so the atmosphere in this Board has changed dramatically for the worse. There has been blame about Nova, blame about Towers Perrin, blame about the €5m contribution, blame about pensions, blame about the disengagement process, and then the appointment process for the new Finance Director. The list goes on. It seems to get added to every day.

I'm not going to go back into all the detail. I think the [redacted] Paper deals very comprehensively with that. For my executive colleagues and myself it has been a process of continuous, disproportionate nitpicking, often retrospective, and increasingly accompanied by personal innuendo.

The irony is that we have a new team in place – and yes, it is a new team, granted one which is still evolving – which has the multiple challenges of managing the business, charting a future course for the business in the post-legislation environment and becoming an effective, cohesive leadership unit. At the same time we are being deflected from the really important things by repetitive recitations of historical legacy issues which are for the most part firmly rooted in the past and have little or no relevance to the way we are routinely going about our jobs today.

This team signed up to build something great here at EBS, something distinctive and special, a task which was always going to be challenging given our relative lack of scale, the constraints inherent within our unique corporate form and some of the established cultural norms which need changing. But they signed up willingly, with a mixture of apprehension and excitement because they saw great potential. In doing so they walked away from secure positions in large organisations with real prospects for personal advancement and reward. But they signed up, as I did, enthused and engaged by the challenge of the EBS cause, which is more than a mere job – the potential to create something and leave a legacy.

I sold that vision to people. It wasn't particularly difficult. If you believe it yourself the selfbelief can be infectious. And EBS itself is a great draw. But I now feel let down by this Board – of which I readily acknowledge I am a part – for permitting self-destructive myopia cause so much damage to that dream, for making both the recruits and the longer serving members of our leadership team, who had also signed up for a new challenge, question themselves on what they have done and tellingly question the ability of this Board to be able to wake up and smell the coffee, to focus on the right things and get behind our efforts to create something special here.

Let me also leave you in no doubt, the dysfunctional behaviour in this room has leaked into the rest of our organisation. Nobody should be surprised by that and it shouldn't take a genius to appreciate the detrimental impact this is having and how worried we should all be about this. Apart from being a major distraction, focusing us away from the really important stuff of being externally focused on market developments and inspiring and aligning our people around changing the status quo, this is the kind of unhealthy atmosphere which can paralyse decision-making, sap organisational self-confidence and encourage a culture of safety-first, second guessing.

I'm growing personally impatient with turning the other cheek and attempting to appease people who are being persistently unreasonable and who when questioned have little constructive to offer as to how matters might be resolved for the common good and who seem determined to approach this on a destructive, self-serving win-lose basis. That's neanderthal leadership and management thinking. It's now time to call a halt in the interests of EBS.

As I said, I believe the [redacted] Paper comprehensively addressed the issues raised in the two Papers from [redacted] and [redacted] and I do not want to go back over that ground yet again. However there are a number of points made relating to myself and my executive colleagues where I believe I have no choice. I need to deal with them here.

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2. [redacted] PAPER

Taking [redacted] Paper first. At the time I said it was a good, considered contribution in many ways on the subject of Corporate Governance generally. However, I also said that, as I heard it, it was a very subjective and selective account of the individual case histories he chose to highlight.

For example,

- He says that the environment for him changed "once he began to challenge the Executive handling of key business agendas". I think everyone will agree that that was the tipping point for all of us. But there are two points to be made on this. Firstly his challenges were not just directed at the Executive. As made very clear in [redacted] Paper the [redacted] was also being challenged because he was fully involved from the outset in the majority of the issues which became contentious. Secondly and crucially, the key point here is not that [redacted] was expressing an unpopular contrarian point of view. The thing which changed the atmosphere in [redacted] and the boardroom was the manner of his communication and his inability to move on once the debate is over. As he has reminded us in his Paper "the Combined Code provides that as part of their role as members of a unitary board, non-executive directors should **constructively** challenge ....".

  [redacted] communication style around this time could not be characterised as constructive both in terms of the type of language used by him in his own contributions, by turns colourful, emotional and regularly personal, and also his impatience, distraction and body language generally while other people were contributing. For my part I have said to him directly in an attempt to fix this that I usually have absolutely no difficulty with the substantive points he is trying to make but find myself having a big problem with the manner of his communication.

  I have no sense whatsoever from [redacted] that he accepts that perhaps his communication style might be a contributor to the situation we find ourselves in today.

- [redacted] speaks about the need to implement the Corporate Governance standards set out in the Combined Code in EBS. He further says that in this regard the Society is losing momentum when in fact .... it should be leading the field in standards of Corporate Governance. Who exactly is he comparing us to?

  I don't accept his assertion for a minute and I don't believe the objective data backs him up either. And there is a lot of data, whether it's benchmarking ourselves versus the ISEQ Top Ten or the BSA's customised Combined Code questionnaire for mutuals. We have nothing to be ashamed of. Nor are we being complacent. We know there are some areas where we can improve – but they are not the ones at the heart of [redacted] Paper. [redacted] has chosen Governance as a flag of convenience and has seriously oversized it. Director after director at our discussion on these matters in March and April said that this is not about Governance. I have immersed myself in this topic in the last few months and with each passing day, as my colleagues and I research the topic more, I find myself disagreeing more strongly with his contention.

- [redacted] also speaks of the [redacted] axis as something which presents difficulty to him. I've thought long and hard about this because he doesn't produce much by way of specifics. I've re-examined the relationship I've had with other [redacted] is my fourth) and I initiated a conversation with [redacted] where the two of us took our working relationship apart to critically examine whether there is indeed anything improper in it or disrespectful to other directors. I was really surprised at this point when it appeared in [redacted] Paper. Of course, I have a close working relationship with the [redacted] – but it's no different to ones I've had in the past. And we've had to work at it. It hasn't all been plain sailing. The notion that we approach Board or subcommittee decisions as if they are just rubberstamping exercises is far from the truth. We try to do our homework to anticipate problems and concerns which may arise in the minds of directors and we always try to spend quality time (unfortunately not always possible) with the [redacted] on important topics in advance of a Board. Pushback from the [redacted] and differences of opinion or emphasis are not unusual. But we try to work out our differences if at all possible before bringing it forward.

Is that not the way it is meant to happen?

If not, then [redacted] and I, and I suspect others around this table, have been getting it wrong all our working lives. Consider the alternative, your [redacted] regularly disagreeing at the Board on key issues of importance to the business. Hardly a model most of us would want to adopt, I suspect.

In this regard I would commend to you a publication entitled "The Art of Chairing a Board" published by The Change Partnership Ireland in May 2005. I believe [redacted] would have circulated copies of the book to the Nominations Committee, and perhaps others, when it was first published. There is a lot of very good and relevant wisdom in it because it reflects the views of practitioners. It is not high theory.

Please bear with me as I take you through a couple of extracts.

In Chapter 4 devoted to "Developing long term Vision and Strategy" one of the roles of the Chair in relation to strategy is:-

⇨ ***To challenge the CEO in relation to Strategic Plans and Act as his/her Mentor:-***

It goes on:- "The effective Chair will have the ability to challenge, test, embellish and question strategy and its resourcing. The Chair will also discuss on an ongoing basis and challenge long-term strategy plans with the CEO. ***Such challenges should however, take place outside the board meeting with the CEO, so that at the meeting itself there is an agreed position on what needs to be discussed and decided by the Board"***

⇨ A further insight on this topic states:-
"Once the Chair has agreed strategy, the task is to succeed in getting the CEO through the decision – making process at the board".

[redacted] clearly meets these criteria. He is experienced, wise and generous with his time. He challenges and provokes and once the debate is over he supports. I have to say, so did my other chairmen. In my view this is the way it should happen.

In Chapter 5 devoted to "Effective Management of Board's Business" it states in relation to 'Setting the Agenda'

- *The majority of participants agreed that the Chair should be both actively involved in setting the agenda and in the preparation of Board papers with the CEO.* ***One of the reasons suggested for this was:-***
  - ***to ensure that no items appeared on the agenda that the Chair was not prepared to support***

- In relation to 'Reaching a Decision' it was suggested *"that the responsibility of the Chair is to get a clear consensus on issues, arrive at a decisive summary on what has been decided and what needs to be done."* It goes on … ***"Decisions based on consensus are desirable. But if there is no consensus, will the courageous chair make a decision? That is what the Chair is paid for, after all"***

Again I believe Oir-P meets the criteria and I think there is an important point for us in here. Nobody likes to lose an argument but I sense it presents a particular problem for Oir-P. If his view does not prevail, if he does not get his way, he is not prepared to note the difference, let go and move on. You have to do that in life. You have to do it in an effective Board. It's not constructive to keep fighting the same old battle again and again. That's not the way to move forward. That's not the way to be constructive.

3. [redacted] PAPER

Turning to [redacted] Paper:

- It is noteworthy that when [redacted] presented his Paper to the April Board meeting the overwhelming view was that it was not collaborative in tone. It isn't. It also has a number of factual errors and several very unpleasant suggestions which I want to ask him about today.

- I'm going to take these points in the order they appear in the original Paper

- First of all [redacted] seems to think there is some sort of two tier categorisation of independence - the truly independent like himself and the compromised. It doesn't work like that. It is primarily about independence of mind and objectivity. The biggest and most admired companies in Ireland take that view as has been demonstrated. To take just one, CRH, they have two directors of 14 years and 17 years tenure respectively. One was the SID and upon his retirement will be replaced by the other as the SID. We've discussed it at REMCO, Noms Comm and at Board and we've made a decision. [redacted] finds himself in the minority but he won't let go because no fewer than thirteen subpoints in his note hang off his particular interpretation of Independence which is at odds with the Board view which in turn is captured in the 2005 audited accounts, **which he has signed as** [redacted].

- Secondly, What exactly is [redacted] suggesting when he links "the handling of the €5m cash injection into the Manager and Senior Manager's Pension Schemes occurring at a time when the Chairman was negotiating the special deal with [redacted] to exit his role as [redacted]"? Why is he connecting these two entirely separate events? Is he asserting that something dishonest lies at the heart of this? More innuendo. [redacted], please speak plainly and clarify.

- [redacted] have been reminded repeatedly that the Towers Perrin Report extended over such a long period of time because their work in the period April '04 to May '05 coincided with a period of considerable organisational and strategic uncertainty against the backdrop of the "Off/On/Off Again" Project Nova. I'm sure we can all remember the twists and turns with Nova before it ended in November 2004 after a period of preparing for and conducting two-way Due Diligence. This was then followed by several departures and arrivals at Senior Management level. What would have been the point concluding a report like TP in a period of such organisational turbulence? It was absolutely the correct thing to do to wait until things had stabilised. There is nothing sinister here. There is no misgovernance here. It is worth noting that TP recommended increases for the Management Board. And let's ask ourselves the question - Who lost out by the fact that this Report was delayed by a year? Senior Management is the answer.

- [redacted] then makes assertions about a new LTIP Scheme which we are supposed to be half way through but with no objectives or measurement systems having been put in place - the implication being no doubt that we will put them in place **after** the fact. He is wrong.

The new LTIP Scheme has not in fact been implemented. We are concluding the old MTI Scheme which still has one year of its three year cycle to run. The LTIP is scheduled to be introduced next year. REMCO was given a full status report on the TP recommendations at its meeting on 2 May 2006. This charge should now be taken off the table.

- The [redacted] has already dealt with the issue relating to executives being asked to increase their pension contributions from 5% to 10%. But I want to put it on record that I consider the way [redacted] summarises this issue in his Paper to be a gross misrepresentation of what actually happened. The proposal to move to 10% was hasty and ill-considered. It had not been fully thought through. Subsequent events have demonstrated that it was correct to defer - as REMCO eventually agreed - until the full pensions review had been completed. This review advised against implementation and this has now been approved by REMCO.

- On the question of my 2005 Annual Bonus, again the [redacted] has dealt with this in detail. The basis used was consistent with prior years to which [redacted] was a party. It is another example of [redacted] being wrong and being shown to be wrong yet we have him repeating the falsehood and using it to shore up other arguments. What exactly is he suggesting? That the [redacted] and I connived to dishonestly increase my bonus? For the avoidance of doubt if that is his view let him say it or withdraw it. I have all the papers from prior years and can very easily demonstrate the consistency of 2005's bonus calculation with 2004's and 2003's.

- On the question of the development of a new Board evaluation procedure, [redacted] states it is totally inappropriate that the [redacted] should be involved in its establishment. Who says so? On what basis? [redacted] has been working with the Chairman on this and good progress has been made. She asked me to sit in with her on one meeting with a prospective supplier which I was happy to do. Where is the problem with that? If the allegation is that this was delegated by the Chairman to the Chief Executive, this is made-up nonsense. It wasn't. It is absolutely risible and preposterous that something as insubstantial and unsubstantiated as this should find its way into a paper alleging Governance failures. This strikes me as another instance of revisionism on [redacted] part. He made no issue about this in October 2005, the Board meeting he cites, or to my knowledge since.

  Then on the question of timing of the new evaluation procedure's introduction, how could you do a constructive Board evaluation exercise in the current war zone? We have bigger and more fundamental issues which need to be tackled now before we 'normalise' with a new Board evaluation process. This rationale has been discussed and agreed at the Nominations Committee.

- Finally, [redacted] has written his Paper as [redacted] I believe this is completely inappropriate. I went down to see him at his office in the run up to our 30 March Board meeting. I asked him in his capacity as [redacted] to join with me in rising above the fray and to use our respective influences to bridge the divide between the [redacted] and [redacted] and to try to defuse things constructively. I had some suggestions in that regard. I was very disappointed and disheartened with the response. He told me that the [redacted] role in his opinion is a non-role. I disagreed with him saying that as [redacted] I felt strongly that he should have an important part to play in helping us to find a solution which would avoid us damaging the business further. As I pointed out to him at the time he was wearing a number of different hats in this affair [redacted] and also a partisan player with an agenda in the difficulties between [redacted] and the [redacted] I believe these last two hats seriously compromised his objectivity - both then and now - and he needed to move into a middle space in the interests of the Society. In the end I did not get a positive response, I did not get any suggestions as to how we might move things forward other than a mantra repeated at regular intervals then and since that '[redacted] must go'.

That is [redacted] agenda and sadly it is influencing everything he says in his Paper. In my view his own objectivity is seriously in doubt.

My experience of [redacted] is that he is looking for opportunities to undermine [redacted] at every turn. Every subject, every decision is an opportunity for pointscoring. He says in his Paper that the [redacted] has serious questions to answer. In my view it is he who has serious questions to answer;

⇨ as our former [redacted] who sees it as a non role,

⇨ as the current [redacted] who clearly does not enjoy the support of the majority of the NEDs on this Board, and

⇨ as a Director who will not abide by the decisions of the Board when he does not agree with them and who clearly has an oft-articulated very low opinion of the capability and objectivity of most of the people around this table.

His behaviour is divisive. It is not collegiate. It is not faithful to the spirit of a unitary board. It is undermining the effectiveness of this Board.

4. CONCLUSION

- To conclude I want to make one very important point on behalf of myself and my executive colleagues. It relates to the number of occasions when we are asked for explanations about matters and are met with disbelief, sometimes quite aggressive disbelief. Up to now it has been our practice to reiterate, to elaborate, to provide further details or documented proof that what we are saying is in fact the case. Even this doesn't work and the false charges or conspiracy theories persist. Explanations are not accepted. Proof is not accepted. Our word is not accepted. Our integrity is being called into question to an unacceptable degree. There are many examples referred to within this Paper and in [redacted] but I will cite just one, the change in the date of the AGM. [redacted] has explained what happened here on numerous occasions. Yet it continues to be portrayed as a sinister plot to keep [redacted] on the Board for another year. This is an example of where the conduct of some people in this room is eating away at the confidence and effectiveness of the Executive. Is this what you want? [redacted] deserves better. She is new to this internecine hostility. She is a consummate professional and it is totally unacceptable that she should be repeatedly publicly doubted in this way. I'd like to think that the people concerned would find it within themselves to do the decent, manly thing and now say they accept what she says. That would be a start.

- I've kept my counsel for a long time. I left the issue of Board relationships to the [redacted] and non-executives to resolve for many months. I did not think it possible that it would spiral out of control in the way that it has.

  This is not about Governance. It never was.

  - It's about broken relationships and bad communications, individually and collectively.
  - It's about the erosion of trust
  - It's about blame at the expense of learning
  - It's about ego, competitiveness and ambition
  - It's about lack of proportionality
  - It's about form over substance
  - It's about empathy with EBS and our business.... or not
  - It's about being forward looking .... or not
  - It's about fairness to new people, who've joined EBS to turn it into something we can all be proud of and who just want to be allowed get on with the job
  - It's about supporting each other and giving each other the benefit of the doubt
  - It's about striving for unity rather than fostering divisiveness
  - It's about collegiality.

- I tried to intervene in the runup to our meeting in March to pull us back from the precipice. As I've said, unfortunately that was not successful. The period since then has been disheartening. Very strong positions have been taken. Harsh things have been said. I say this with a heavy heart but I'm reluctantly coming to the view that I do not think we are going to be able to put this all back together again.

- The Executive team is more determined than ever to see this through. We have the self belief that we can chart a course for this business in the post-legislation environment. It won't be easy but we can do it. At the moment this Board is getting in the way. In the interests of this business, the people we employ and the members we serve, the prevailing difficulties must be put behind us. They must come to an end. There is no alternative.

Oireachtas-P

12th June 2006.

EBS Board Meeting 12th June 2006

I am personally very disappointed and saddened that we have ended up in the situation that we find ourselves in today.

As directors, we have a collective responsibility for the success of EBS and a duty of care to both the society and its members. Our members expect and demand from us good leadership, strategic direction and robust governance.

Yet we find ourselves paralysed by infighting and are running a very real risk of leaving as our legacy, a society that is weakened, defocused and vulnerable. Our members as owners would rightly ask "how could their board allow this to happen?"

What is clear is that relationships have broken down and that rather than deal with this, we are cloaking the reality in a debate about governance. Accusations and counter-accusations have been flying around this boardroom for months and it would appear, for much longer at certain sub-committees.

However it goes beyond this – the personal integrity of the executive management, the secretary, the [redacted] and indeed many non-executives has been needlessly called into question – often times repeatedly so.

Furthermore, flippant and convenient stereotyping has been used to cast dispersions on and indeed undermine many around this table. Yet we want to hide behind governance?

In terms of governance, we all agreed that [redacted] should lead a process to address the perceived issues of governance. Notwithstanding this, we continue to frustrate her efforts and not allow her make sufficient progress. For me, it has been quite revealing.

I personally have every confidence in [redacted] ability and leadership to progress and provide benchmarked insights in the whole area of governance and in so doing, enable us to more effectively govern the society.

The real issue within this Board however is not governance; it is the Boards psychological disposition.

- Our mindset is not one of leadership.
- Our culture is not inclusive, supportive or trusting.
- And our mood is obstructive and argumentative.

Is this what our members really expect from their board?

Of course, individually and collectively we have not got everything right and like every other organisation we can learn and improve. By the same token, we have had many successes and have made much progress in a difficult and competitive market, despite ongoing board disharmony.

Equally, I recognise that not all expectations have been met all of the time and that this has led to negative feelings and high emotions. This is clearly very evident, yet we have not taken the time out, or for that matter shown a willingness to agree how governance could work more effectively in EBS.

Nor have we grasped that governance is not a passive function. Essentially it is about leadership. Do we honestly believe that we are providing leadership through this Board?

Whether we like it or not, our actions and inactions have a profound impact on this organisation.... But do we really have an appreciation of the impact that we have?

I can tell you first hand that we are creating negative consequences for EBS and while many may well be unintended, they are nonetheless quite real and absolutely detrimental to the society's long term success and survival.

Our business is complex enough without this. Our core market is changing all around us. The mortgage market on which we are so dependent will ultimately slow. We are also facing tougher competition from major international banks on a daily basis.

In recognition of these facts, the society is trying to diversify and reduce its dependence on interest income and only two weeks ago tied to Irish Life to develop a Bancassurance business.

We also recognise the need to examine our traditional business model, our infrastructure, our distribution footprint and our cost base. And of course, we also know that we have constraints around capital.... as does every other lender in Ireland.

But is this where our Board is spending its time to add value? And if its not, lets ask ourselves - "who is doing it for us?" Let's also ask ourselves if we believe that personal positions, pride and egos are more important than the society and its members? I personally doubt it.

The reality is, that this organisation needs more so than ever, a strong and unified Board that has the courage to take the type of decisions that we collectively deferred in the pursuit of Nova and mortgage market growth.

In this regard, I am more than amused that there is a view in certain quarters within this boardroom that strategy is a spectator sport and that when convenient one can detach themselves from any involvement and or responsibility for the various strategies that have been pursued over the years. It certainly is not my experience of other organisations.

As you know, I joined EBS almost three years ago and have served on this Board for the last year. Before joining EBS, I was an executive with Bank of Ireland and a Director of its subsidiary, ICS Building Society.

ICS was a hugely positive experience. As a strong and unified Board, we had the clarity of intent, confidence and conviction to take over the Banks mortgage business and become the market leader in Ireland. The Bank has [redacted] to thank for this.

However, it would not have been possible if the ICS Boards psychological disposition had been anything other than inclusive, supportive and trusting of each other.

In joining EBS, I took personal risks but saw the potential to create a real alternative to plc banks on the back of a superb brand. Admittedly, the society's plan at that stage was to accelerate its ambition as part of Rabo Bank which would have seen EBS, ACC and possibly Friends First all under the one roof. Project Nova was a bold transformational play.

However, Nova never came to be, whereas my commitment to this organisation has never been anything other than total.

Despite our many challenges, I still see huge potential for our organisation. Sure we need to evolve and hopefully the promised legislation will remove many of the shackles that exist today.

But let's face reality; legislation will be of no benefit unless we change our behaviour around this table. This is our real Achilles' heel.

I am proud to be part of EBS and deeply want this organisation to be successful. Notwithstanding this, I fear that there has not been, nor is there a willingness to resolve our differences and move on.

As things stand, our future is destined to be less than our potential and ultimately this Board is running a risk that EBS may not exist at all.

We need to draw a line in the sand now. This organisation needs to and has a responsibility to move forward.

I have listened, read and re-read the various submissions and more importantly observed the mindset and disposition that is tearing this board apart – this is not about governance.

We can not allow this fractious behaviour to continue to undermine and indeed threaten the very essence of this organisation.

Finally, for the record I believe that we have in [redacted] a good and effective [redacted] – I have worked with many.

I am more than happy to serve this organisation under [redacted] leadership and stewardship.

[redacted]

12th June 2006

Minutes of Board Meeting on 1 March 2007 (Cont'd.)

Activity Reports/ Business Updates (Contd.):

<u>Commercial</u>

An update was provided on the Commercial Business year to date. It was noted that there has been a slow start to the year and it is likely that the 1st quarter will be below budget. Against the backdrop of the current market uncertainties it was agreed that it would be unwise to put undue pressure on our Commercial business at this early stage.

<u>Treasury</u>

It was noted that the French Commercial Paper programme has commenced well.

The new liquidity framework is in parallel run at present.

<u>Financial Regulator</u>

An update was given to the Board on stress testing. It is very apparent that there are anomalies in the market and the Regulator has agreed that they would review the guidelines in consultation with the industry. We are awaiting the outcome of this review.

The recent onsite review was discussed. In relation to credit, there was a concern raised regarding the extent of credit policy changes made recently. Our affordability model was also discussed.

Separately minutes and board workings were reviewed by the Regulator. Their position is that they would prefer if all policies were reviewed at board level rather than BRC and also would prefer an independent Risk function i.e. concern that Alan Merriman is responsible for both the Commercial business and the Risk function. A concern was also raised that not enough time is being spent at Board on credit. We are reviewing the issues raised and a letter from the Regulator is expected shortly which can be discussed in more detail at that time.

Since the last Board meeting the Chairman had met Pat Neary and Con Horan. The purpose was to introduce himself. The Chairman articulated what we were trying to achieve as the last mutual and that we wanted to be able to compete with the banks e.g. covered bonds. Overall a positive message was received that the Financial Regulator wanted to support us.

An update was provided on asset covered securities legislation. Based on legal advice the DCI option is not available to EBS. The industry agreed a workable solution but the Regulator did not approve of this approach. The Department of Finance have said they will look at amending the Building Societies Act to provide a solution.

The Regulator has not approved the Tier 1 transaction as yet and, therefore, the timelines are likely to be later than originally envisaged.

[redacted]

Tithe an Oireachtais
Houses of the Oireachtas

Joint Committee of Inquiry into the Banking Crisis

Witness Statement of

Alan Merriman

Session 53a (a.m.)

29 July 2015

Strictly Private & Confidential

As indicated on its cover page, the document(s) contained within are confidential unless and until the Joint Committee decides otherwise including where the Joint Committee publishes such document(s). For the avoidance of doubt, "documents" include witness statements in this context. Further to section 37 of the Houses of the Oireachtas (Inquiries, Privileges and Procedures) Act 2013 ("the Act"), while the documents remain confidential, you must not disclose the document(s) or divulge in any way that you have been given the document(s), other than:

> "(a) with the prior consent in writing of the committee,
>
> (b) to the extent necessary for the purposes of an application to the Court, or in any proceedings of the Part 2 inquiry, or
>
> (c) to his or her legal practitioner."[1]

Serious sanctions apply for breach of this section. In particular, your attention is drawn to section 41(4) of the Act, which makes breach of section 37(1) a criminal offence.

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

ALAN MERRIMAN - WITNESS STATEMENT

1. INTRODUCTION

I refer to the direction to attend and make a statement in writing pursuant to Section 67(1) of the House of the Oirechtas (Inquiries, Priveleges and Procedures) Act 2013 as received by me on 1 July 2015 (the "direction").

2. BACKGROUND

I joined EBS Building Society in July 2005. I was 37 at the time of my appointment. Prior to this I had been with Pricewaterhousecoopers for the previous 17 plus years, where I was the partner leading the Irish banking and insurance audit & advisory practices. As a partner in PwC I had the opportunity of working for many of the Irish banks – both audit work and on the advisory side. My clients included Bank of Ireland Group, First Active, Permanent TSB, EBS, ACC Bank, Anglo Irish, the Central Bank and many of the international banks based in the IFSC.

Joining EBS was a great opportunity to test myself in industry and to work somewhere with common good where I might perhaps make a meaningful difference. I joined as Finance Director, with a wide brief, mainly to help the Society advance its ongoing professionalisation across its platform and with the strategic challenges that it was then grappling with. I viewed mutual status as a big positive. The Chinese curse of beware of what you wish for comes to mind.

3. EBS CONTEXT

Explaining the EBS context is perhaps the most valuable contribution I can make. EBS was different. I think its important to acknowledge this. A member owned non profit organisation. The last remaing true building society in Ireland. It was established by teachers, was popular amongst civil servants, teachers, guards and nurses amongst others and its people, whether at branch level or at head office – root and branch had a DNA and culture of being community based and Member focussed. It was not focussed on profit. Rather it was trying to serve Members better through superior service, real trust and competive pricing compared to the banks and to be relevant. It was a very democratic organisation with a diverse board and true member representation. It thought of itself as the alternative to the commercially driven banks. It had a great culture and spirit.

Neither was it perfect. By 2005 member value was not very tangible, trust and Member satisfaction were declining and external stakeholders were increasingly sceptical about the Society's future as an independent organisation. With the likes of Danske Bank aggressively pricing for the high credit quality refinance mortgages and the likes of Bank of Scotland, PTSB, Ulster and Bank of Ireland aggressively targetting EBS's traditional heartland – the first time buyer market – EBS was being squeezed. Irish Nationwide the other "mutual" clearly had different values but was held up by many as the more 'commercial' organisation with a lower cost base and a focus for development deals that was "showing up" the management in EBS. This pressure to ensure the Society continued to be relevant and for Management and the Society to perform at a new more dynamic level was evident from my very first Board meeting at which the 2005 long term strategic plan was approved.

Whilst the perception from the outside would be otherwise, let me say that managing a mutual was hard. Judging Member value is ambiguous. What the Members' want can differ very starkly amongst themselves and sometimes the clarity of being profit driven seemed much simplier to me than working to a Board of very diverse talents and views as to what would be best for EBS as a mutual. Savers looking for better rates, borrowers looking for cheaper and bigger loans, everyone wanting better service, but lower costs – all drawing from the same small shared pot. Paradoxically too for EBS, the tiger economy weakened its positioning and brought very different challenges for the Society. For instance, new foreign competitors attracted by high growth changed the mortage market, the trade unions and National Partnership agreements brought very high annual wage increases and so for EBS – it was challenged to make all ends meet. Savers were not getting much value as interest rates declined and borrowers, who tended to be more favoured – and for whom we could say were achieving some pricing benefits with EBS - this was falling and was marginal at best. And it was clear that the bigger players – which effectively meant everyone else - were able to tap cheaper funding, get greater economies of scale, ride the tiger economy in other very profitable ways outside of mortgages and cross subsidise their mortgage business from other products such as consumer or SME lending. They the banks had ready access to capital or international parents willing to invest in the high growth Ireland – and they were winning, or at least EBS was losing as evidenced by EBS's natural market share steadily eroding bit by bit.

The Board believed in Mutuality and wanted to preserve it. The Members – based on surveys and feedback said they wanted to preserve it - and whilst the concept was very appealling and most everyone could sign up to it, at least aspirationally, the reality of delivering on it – was very different. The truth, whether it was well understood or not, EBS was fighting for survival – not only in 2009 or 2010 but also back in 2005 and even before this. This I believe was understood relatively well in Department of Finance and at the Central Bank/Financial Regulator. And change for EBS was seen as necessary, a least from without if not fully within.

I share this perspective with you – so that you can consider that what EBS did (and did not do) in terms of strategy and how this evolved was very much motivated to help it survive and be relevant to its Members. Retaining a mutual in Ireland. The Board took this very seriously. Had it not competed in the market – EBS would end up extinguished. By definition as a home lender this meant being able to offer attractive mortgages to our Members – both in pricing and in credit terms – had it not done so – it would have lost substantial new business and Members and this in turn would have meant a downward spiral of less value for existing members, reduced income and lower profits, necessitating deeper headcount cuts and loss of talent, cost restructuring, branch neglect and closures, and further weakening of the EBS offering, etc.

You do not need to be a banker or politican to understand this. Faced with choices – the vast majority of businesses and the very essence of human nature itself is that you will do, within moral and commercial reason, what is needed to survive and keep the dream alive. EBS was no different. EBS had effectively little choice but to compete and fight.

4 CHALLENGES AHEAD – KNOWN & UNKNOWN

I knew pretty much immediately after joining in July 2005 that EBS was more challenged than I had understood. But having such concerns and bringing about much needed change to address these concerns was a different matter. For instance, in 2006 management tried to convince the Board that considering a partner –whether a mutual or otherwise may be necessary and changes to legislation to enable this would be sensible and ought to be pursued by the Society. The Board disagreed. In January 2007 – I advocated strongly to the Chairman and CEO that we should accept an offer we had received from AIB to 'merge' with EBS – I was in a minority of one and the Board did not engage on it with any seriousness. Throughout this time in advocating these positions, I was principally concerned about longer term capital and funding challenges and what I referred to as a death of a 1,000 cuts, or the downward spiral. Being part of a team but with a strong contrary view to the 'group think' is very tricky. In summer 2008 the Board after much heated debate finally agreed that preserving mutually as unlikely but even then they felt management was too negative on our outlook and the challenges ahead. Clearly matters only got worse.

As negative as I was, I did not anticipate the extent of the cliff which the global economy, and Ireland and EBS with it, went over. Property prices falling by 60% back to levels below those of nearly a decade earlier and unemployment extending to over 15%. Such a scenario and dramatic collapse I viewed as highly unlikely back in 2005 and 2006. For me, my experience of 2005 was of PwC having to scout around the world to try and recruit staff; Foreign Direct Investment still strong; and low interest rates and strong demographics to boot – so the immediate outlook seemed quite constructive and whilst it inevitably had to slow down - I was in the soft landing camp and yes I saw life getting tougher especially for EBS, but certainly no where close to what actually transpired.

Even in early 2009 before I left EBS and as bad as it was then, I did not anticipate that it was going to be as shocking as it got. I sat in many meetings with the Central Bank and the Regulator during 2008 and 2009 and at the highest of levels and can assure you – they assured us – that these issues would pass and we just had to put our heads down and get through it. And to be fair to the Central Bank and the Regulator, whom like EBS had limited resources – the U.S. Fed with all its intelligence and hundreds of economists did not see this great recession crisis coming either. Neither did others such as OECD, World Bank, etc. The fact is the tail risk came and the Irish banking model as it had evolved over a substantial period of time and EBS along with it could not withstand it.

5. LINES OF ENQUIRY

B1- Integrity of Financial Reporting

We always endeavoured to report faithfully. I enjoyed a good loyal and bright team who worked incredibly hard during all this time to professionalise further EBS internal workings, systems and controls. There was a lot of transformational change going on in EBS over this time, ranging from the introduction of IFRS, Basel II, organisational change, special projects, capital and funding transactions and cost restructuring work which would have drawn heavily on the already busy and stretched Finance Function.

Accounts for financial institutions are complex, it is far from bean counting. In summary, I can attest that EBS had a strong framework for oversight and approving the accounts – this extended, inter alia, to extensive planning work, careful analysis, detailed papers on judgement issues for the Audit Committee, and private meetings between the Audit Committee and E&Y to openly discuss any key concerns. Dargan Fitzgerald the E&Y partner has already confirmed his positive view on the workings within EBS in this regard.

The only time – as Finance Director – I ever came under any real pressure or challenge on the accounts was in 2009 when reporting on the 2008 results. The impairment provisions especially on the development finance book were disturbing to say the least and we had to keep moving the loan loss number up as we learned more and as the economy detiorated further. We changed our views with the fast moving facts. This unnerved some of the Board who were very uncomfortable with not only the absolute level of provisions that we were reporting but also why our provisions seemed relatively so much higher than the banks were making publicly known. Understandly this led some of the Board to question whether we were being naïve or worse still was EBS lending actually worse than the other banks. Our view was that we did not know but perhaps because we had a smaller book and had stopped commercial lending in April 2008 due to earlier concerns we had a much better understanding of our stressed book than perhaps the banks had. However being ahead of others in understanding the damage that was unfolding was also undermining confidence at board level as to what was the right number. E&Y had no difference of opinion with our provisioning. The Central Bank and the Regulator did though – in that they were concerned that our provisioning might cause wider difficulties for the other banks and we were cautioned at the highest of levels to be very sure that what we provided was really needed. Needless to say this feedback to the Board only served to reinforce some views about our possible naivety or lack of commericiality. Nevertheless management held to our views, stayed true to the integrity of our reporting and provided what we believed was warranted at the time and that could be justified under IFRS, and the Board approved the accounts on this basis. The rest you know – the provisions – whilst appropriate from a historical accounting perspective – where far too light compared to what was ultimately needed. So yes in my view the intergity of the accounts in EBS was robust during these times and there was no manipulation by Management or the Board of reporting earnings.

B2a - Appropriateness of Property-Related Lending Strategies and Risk Appetite

EBS was a home lender. This was its core business. Mortgage lending always dominated and was followed by commmerical lending (which started in 2001 and was stepped up further in 2005). There was very little else.

By definition then EBS was consequently effectively very reliant on the health of property market and the employment market as it had been for many decades. The fact that the country and its fiscal budgeting as a whole was too – was maybe less well appreciated. Building Society legislation restrained what EBS could actually do and diversifying into new business lines was challenging. Mortgages for our members. Commerial lending to non members - with the idea of earning higher margins that could then help reduce pricing on mortgages to Members. And driving up ancilliary income is what EBS had to work with. It was not an asset manager, did not have life assurance products of its own, did not do SME lending or corporate finance. It was a home lender, funded only in part by retail members and the rest coming from the Markets in one way or the other.

So in terms of what we did do, credit terms were of course a key value proposition for our Members and EBS positioned itself in particular to assist First Time Buyers. Helping those Members get on the housing ladder was a key raison d'etre for EBS – not to do so was against the grain as to what EBS was about. So the EBS risk appetite has to be judged in this context. We lent to our Members to help them get on the ladder. We lent as much as we felt they could reasonably afford in line with the Market and that they too were willing to borrow to invest in their new home and family's future It was not for profit, it was to support community and family.

Credit terms and risk appetite were within those offered generally by the market and the competitor analysis we did supported this. Yes we competed by stretching a little here and there from time to time but in a measured way and with full board oversight. The Society as a financial safeguard also paid for insurance to help mitigate credit risk, and all mortgage credit changes also came under the scrutiny of Genworth and this too acted as a further third party check and balance.

B2b - Appropriateness of Credit Policies, Delegated Authorities and Exception Management.

EBS had a separate risk function and Head of Risk to bring independence and rigour to credit policies and support the Board in this critical area. All polices necessitated Board approval and there was a clear exception management process in place. Key credit changes such as the step up in development lending and the move to 100% mortgages were well debated at all levels of the organisation and up to and including the full Board. Risk as well as the business always has a strong and independent voice.

Overall - policies, sectoral limits, exception to policy reporting, stress testing including against specified Central Bank and Financial Regulator set parameters were all applied. History has now shown failings but at the time – they were considered robust and provided comfort as to capital adequacy and loss absorption capacity. All material commercial and development loans over certain thresholds were individually approved by a special Board Credit Approval Committee which included a majority of non executives . Risk oversight in EBS was the responsibility of many, not any one individual – but especially the Executive team and ultimately the Board itself collectively. It was certainly not embodied in any one individual.

E&Y have already provided independent expert testimony to the Committee that in their opinion EBS governance and controls was strong and indeed compared well to what one might expect for an organisation of our size. Certainly the EBS risk function and control environment generally evolved considerably during the period 2005 to 2009 with substantial catch up and investment in people, systems and processes in a multiude of different areas.

The regulator, Fitch and Moodys were all briefed and understood our limits relating to residential mortgages, commerical and development finance and no concerns were expressed about these non residential mortgage strategies. All understood the necessity for EBS to expand its business and improve profitability. I would go as far to say we were encouraged to expand and become more commerical.

Risk management is a continuous process with improvements and better ways of doing things always emerging. My EBS experience was no different in this regard. It did lots of things very well, but also had lapses and was learning continuously.

B2c -Analysis of Risk Concentrations, Adverse Economic Scenarios and the Impact on Capital Structure.

EBS had a similar risk governance framework to the banks and was subject to continous supervision from the regulator and probing from the Rating agencies on our polciies and risk management framework. We took risk management very seriously and invested heavily in people, processes and the likes of Basel II. During my time with EBS, until the crisis hit, our external credit ratings actually improved.

EBS as a domestic home lender, was concentrated in mortgages in Ireland. Realistically even with the benefit of hindsight no matter how this might have been managed or better mitigated – the great recession and its consequential impact on banking models as they had evolved would regardless have had a mortal impact on EBS. Whilst its Development Finance lending book is often highlighted as what brought EBS down, view this as exaggerated or at best overly simplistic. It is undoubtedly the weight that sank us. But even without it, I believe the same outcome would have been inevitable in that other exposures or business model vulnerabilities would have caught up with EBS one way or the other too.

Like a fraud or the cockroach – when one is discovered and the post mortum rigourously done – the underlying weakness or cause was not just the one but rather a multitude of collective weaknesses or vunerabilities or cockroaches. So if it was not the development finance book – it would have been the buy to let mortgages, or the pure commercial lending book, or the high LTV first time buyer book, or the downward spiral hitting bottom as new business and income eventually collapsed. Or liquidity and/or funding knock-outs. Or as I say a combination of all these.

Let me deal with the Development Finance book though. It was circa €500m and policy was to contain it to no more than 3% of the entire book. Yes just 3%. Whilst this level seemed reasonable – by contrast when a great recession brings a 60% to 80% correction in land prices and little or no transactions and you are simultaneously effectively forced to sell –

the severity of losses even from such a small book are lethal. So whilst business being written at 65% or 70% LTV ratios at the time in a growing economy seemed very reasonable – the impact this business would subsequently have on incurred losses in due course was very damaging. Whilst this type of possible loss impact was I think generally understood – no one within EBS was antipicating such severe moves. And if we had – then our adjusted credit policies would have meant we were simply out of the market in its entirety as we would have got absolutely no business. A decision we did come to in early 2008, albeit too late, even whilst others kept going . As many other witnesses have commented – the reality is that the stress testing conducted did not envisage anything like the losses that actually transpired – and in part this reflects that the magnitude of adjustments was effectively unprecedented globally.

In January 2009 mangement undertook a very detailed post mortem review of the development finance business for the Board. This covered the rationale for stepping this business up further in 2005 and addressed questions around strategy, risk concentrations, governance, execution, reporting lines and integrity of reporting. The analysis pulled no punches – of course mistakes were made and to quote "these together with a sharp property price correction and wider global dislocation events have left the Society overly exposed to this hard landing".

B3b - Analysis of Liquidity Risks under Adverse Scenarios.

EBS took liquidity risk very seriously. We operated under a variety of safeguards including legislative requirements; regulatory requirements and our own internal assessments. Liquidity management was the responsibility of the Head of Treasury and also overseen by the Head of Risk. Management at various levels, the Board and the Risk committees reviewed liquidity risk and policies frequently. Enhancements were continuously being made. Residential mortgages generally were viewed as a good source of collaterial to tap funding and deal with liquidity emergencies if necessary. Numerous initiatives were invested in and executed throughout this time to protect liquidity, widen funding and in so doing improve the Society's capacity to deal with liquidity stresses.

B3e - Capital Structure and Loss Absorption Capacity

EBS as a mutual did not have the same access to capital that other financial institutions such as the banks enjoyed. In this sense it was very reliant on retained earning and continuing annual profitability to support risk weighted asset growth. This for me was the key to understanding the quality of earnings or in a mutuality context the sustainability challenge facing EBS.

We did raise Permanent Interest Bearing Shares which added to loss absorption and helped sustain balance sheet growth for a while. And these were well oversubscribed at the time – showing strong (albeit misguided) international belief in the status of and future wellbeing of the Irish housing market and EBS. We also found other ways to optimise our capital ratios and funding such as securitisation and covered bonds (again with lots of international interest). Our total capital ratios were well above regulatory minimums and supported A ratings from both Fitch and Moodys.

The survival challenge as I saw it was circular in that we needed to issue new mortgages to stay relevant in the market place and bring in fee income as margins eroded and costs escalated in the tiger economy. The weaker earnings from lower margin business in turn hurt core capital and whilst we could find relief measures I grew increasingly concerned about the long terms consequences of this. This ultimatetly led to Managment collectively expressing such concerns to a specially convened Board in 2006 and advocating a needed change in thinking and legislation to allow for strategic flexibiilty. The Board as I explained earlier were not convinced that the degree of risk was as high as Management believed and the Executive were directed to continue to focus on preserving mutuality and driving performance to ensure this. I subsequently sought advice from Arthur Cox and based on their advice raised the matter again at the following Board Risk Committee – expressing my grave concerns about the Board's decision and the challenges ahead. However again I was unable to persaude others on this.

Subequently, in early 2007, AIB made an approach to acquire EBS. The terms offered were in my view very attractive and included for example EBS brand being retained and an independent subsidiary and network. The offer from memory was €700m. Unfortunately it would mean the loss of mutuality but by then as I have explained I thought this inevitable anyhow. My rationale was simple, as much as I wanted to see mutuality work, I felt strongly that it was not realistically viable – our capital challenges, thinning margins, funding model and lack of flexibility and over-reliance on property products as we competed in a very aggressive market would eventually catch up with us.

Again I share these insights – so that you can understand that capital and loss absorption were key agenda matters and the Finance, Treasury, Risk and Strategy teams within EBS and the Executive Management as a whole did foresee dangers. This led to very robust exchanges at Management and Board level – however ultimately the Board as a whole were more optimistic than Management and I would reiterate that as pessimistic as I was – neither I nor anyone else in EBS foresaw the extent of the great collapse that did eventually occur.

B6a - Effectiveness of Internal Audit Oversight and Communication of Issues

EBS similar to all financial institutions had its own internal audit function. The department was staffed by competent professionally qualified auditors, and broadly speaking divided its work into branch inspections and Head Office related work. The department had a direct reporting line to the Chairman of the Audit Committee and its plan and reports were routinely reviewed and discussed at Committee level including in private. The scope of all work was independently set of management. This work was valuable and the work and status of internal audit within EBS was well regarded. During my time at EBS quite a number of audits led to material findings that gave rise to full discussion at Audit Committee and Board and changes to better ensure controls to support risk appetite.

B6b - Effectiveness of the Oversight of the Prevailing Risk Culture

Similar to every other area, the independent risk area and the prevailing risk culture throughout the organisation were under the scope of the Internal Audit Function. What they choose to focus on – was subject to their own views on risk assessment and rotational emphasis. In addition to unit reviews, Internal Audit would also undertake thematic reviews as part of their annual programme. Internal Audit also would have been party to reviewing various corporate governance reviews such as Turnberry. As E&Y already attested too, and I agree, EBS had strong governance in place and this extended to the workings of internal audit and their supporting effective risk management. Internal audit through all their work would have had a strong sense of the prevailing risk culture and reported on this to the Audit Committee continously. Whether risk management was effective or not is another matter but I am satisfied that any failings were not as a result of internal audit deficiencies in identifying these or indeed lack of oversight of the prevailing risk culture. Ultimately accountability rests with management and the Board not the internal auditors.

B7a - Impact of prevailing Accounting Standards in Recognising Risks

As extensively covered already by the Committee in earlier sessions – I would simply note that IAS 39 was unhelpful. The reality is that accounting is a rear mirror view and not as well placed as one might like to assist in predicting future outcomes and/or highlighting and helping users understand all risks. However I would also note that voluntary disclosure theoretically could have mitigated some of the weaknesses in financial accounting standards and/or the regulatory system could have required more capital as a buffer to be held regardless of the accounting convention.

B7b - Effectiveness of the External Audit Processes to Identify and Report to the Board and Management any Concerns Related to

Significant Risk exposures including Property, Funding and Liquidity.

Prior to the crisis I do not recall any of the external audits ever raising any key concerns about significant risk exposures to areas such as property, funding and liquidity. They will also tell you that this is outside their statutory remit. Having said that, if they had had any such material concern – I would have expected them to raise it, at least informally with myself and/or the Chief Executive or in private with the Audit Committee. Auditors whilst not bankers do have the benefit of having access to many financial institutions – domestically and internationally and in so doing and as global businesses themselves - understanding international best practices and risk warning indicators. They are also trained and disciplined in prudence and risk management. My belief is that E&Y prior to the crisis had no such material concerns relating to EBS exposures including property, funding and liquidity.

R3b- Nature and appropriateness of the relationship between the Central Bank (including the Financial Regulator), Department of Finance and the Banking Institutions

I have no particular insight to bring to bear here. From what I saw first hand the Central Bank and the Financial Regulator worked relatively closely together during the crisis. There was continuous dialogue with all authorities including the Department of Finance. The only thing I would add is that just like in EBS – any failings I would attribute to each authority as a collective and not to any one individual. For a bank or building society to be reliant on one individual is very poor goverance, for a supervisory authority even more so. So I would be more critical of collective failure than individuals.

6 CONCLUDING REMARKS

EBS as a whole and its Members were casualties of this crisis. They were not the making of it.

I believe with strong conviction - given the circumstances and what EBS had to work with – that regardless of what strategy evolution EBS adopted during this time – other than perhaps a trade sale to a large overseas financial institution (which was not the preference of the Board nor the Members) the Society and its values would have been lost one way or the other. This would have necessitated legislative change.

Like with a tsunami, EBS was essentially in the wrong place at the wrong time. Hamstrung by legislation, its concentrated lending business, its reliance on wholesale funding and trying to compete with much larger and commerically short term driven organisations both domestic and international who were stretching credit standards and aggressively pricing mortgages – meant that the continuation of the market as it then was - never mind the crisis - was life threatening for the Society. The business model was stretched.

EBS did what the Board collectively thought best to survive and to then hopefully allow it prosper in due course. In so doing it was trying to be true to its Founders and Members and all stakeholders by preserving the optionality of a Mutual continuing in Ireland and remaining relevant in the market place. It ultimately did not succeed, which is I think a real loss to the country as harder times bring an appreciation back to community support and family. The EBS brand being retained by AIB – is testmony to the goodwill that the Society had amongst its Members and more generally.

I think banking generally will change radically for the better in the decades ahead – the move to mobile and new technology will I think disrupt the incumbants and empower the consumer. I think we are in the early innings of some transformational changes. Whether the Lendingclub.coms or Starbucks become the new modern day substitutes for EBS and take on the baton of offering a better alternative to the banks - time will tell.

I hope these personal insights help the Joint Committee in its deliberations.

Alan Merriman
8 July 2015

B1a – Composition, skills and experience of the board and board subcommittees

Information Summary (Section33AK)

Note: All references are aggregated

Document Category	Time Period
Internal memos	
Correspondence	Q2 2007
External consultants reports	

Q2 2007 the Financial Regulator wrote to An Institution listing a number of issues, findings and recommendations following an inspection and review of Residential Mortgage Lending, lending policies practices and procedures.

The review highlighted 5 High Priority findings, 23 Medium Priority findings, 1 Low Priority Finding and 2 Observations.

An Institution was invited to consider these matters at its next board meeting and to respond to the Financial Regulator with details of how and when the findings were to be addressed by An Institution.

High Priority Findings

1. Stress Testing of Loan Repayments.

   Mortgage repayment capacity, as defined by Net Disposable Income (NDI) was not calculated on the basis of stress tested mortgage repayments. This is a requirement and must be reflected in the Credit Policy. Stress testing must be carried out at SVR + 2% as guided by the Regulator. Policy must also state that interest only facilities should be stress tested on a capital and interest repayment basis.

2. Repayment Capacity

   Financial Regulator required that Credit Policy be amended to clearly state which of NDI or Affordability Test methods for calculating repayment capacity is a policy requirement and which is guidance only.

   All monthly financial commitments should be included in calculating NDI.

3. Corporate Governance - Strategy

   The Financial Regulator questioned An Institution’s strategy direction in the context of its stated intention to develop a “non-member” business and recommended that the strategy should be clarified, documented and should be driven and approved by the Board.

   The Financial Regulator required An Institution to forward a copy of the strategy document to it.

4. Role of the Board in Assessing Risk

   Financial Regulator recommended that all material risk policies should be approved by the Board, rather than a sub-committee of the Board. This would ensure that all non-executive Directors agree with the material risk policies and that they would comply with the Financial Regulator requirements.

   Board reports on risk management must be more comprehensive and must include more information on residential and commercial lending so as to ensure that the Board is fully aware of all relevant risks.

5. Risk Management

   Financial Regulator did not approve of the fact that the Chief Risk Officer also held the post of Finance Director and had responsibility for Commercial Lending. This had the potential to create significant conflicts of interest and to compromise the independence of the risk function. The Financial Regulator was also concerned about succession planning in view of the multiple senior roles held by one individual.

   The Financial Regulator required the Board to confirm that an independent risk management system was in operation and that they were satisfied with the succession planning process.

<u>Medium Priority Findings</u>

The 23 medium priority findings can be categorised as follows;

- Functioning and review of Board performance (6 Findings)
- Credit policy and procedures (9)
- Review of Loan files (6)
- Other matters (2)

Functioning and Review of Board performance

The Financial Regulator commented on the need to update board manuals to reflect current reporting structures; to ensure that the minutes of the board and board committees clearly reflected the discussions held; to ensure that the board reviewed its own effectiveness on an annual basis; to ensure that the committee structure of the board was in line with best practice; address issues raised by non-executive directors concerning need of more clarity on the roles of the board and board sub-committees as well as addressing concerns over the quality of reporting.

Credit Policy and Procedures

The Financial Regulator noted that the Credit Policy document had not been updated since 2002 and recommended that this should be done annually. Content in respect of certain aspects of policy also needed to be clarified.

The Board should consider if, in light of the level of exceptions to policy being reported, the Credit Policy is appropriate to the nature of the business being conducted.

The underwriting management system needed to be improved in order to eliminate the need to handle the increasing number of more complex transactions using spreadsheets. This would also improve the quality of data-capture. Certain underwriting procedures also need to be clarified.

The Financial Regulator noted that the credit scoring and risk ranking techniques already in use should be incorporated into the decision "engine". Also, the monthly sample review of underwriting conducted by the business should also be reported to the Credit Risk Committee.

MI systems should capture all relevant information in relation to facilities.

The Financial Regulator questioned the accuracy of information on accounts which appeared to have substantial arrears of between 81 and 915 months. They questioned if the level of provisioning was adequate.

The Financial Regulator identified issues/queries on 23 of 33 loan files reviewed. These included queries on details of income used to calculate repayment capacity, the need to back-test assumptions made on room rentals as part of the original loan approval, and the inclusion of rental value for the property in the valuation report. Other issues identified were; recommendation to verify accuracy of employer confirmations of income; consider monitoring employer concentrations and obtaining valuations for all top-up facilities.

Other Matters

The Financial Regulator identified an overpayment to bondholders in the Emerald securitisation programmes. It queried the reasons why this happened and what measures had been put in place to prevent a recurrence.

Low Priority Findings and Observations

The Financial Regulator required Internal Audit to review the methodologies for determining provision levels in order to confirm their effectiveness.

The Financial regulator noted that certain documents requested in the course of the previous inspection in Q4 2005 had not yet been provided.

An Institution should provide details of any proposal to outsource elements of its IT requirements to India and consider if any such move could require approval under the Building Society Act.

Tithe an Oireachtais
Houses of the Oireachtas

Joint Committee of Inquiry into the Banking Crisis

Witness Statement of

Fergus Murphy

Session 49b (a.m.)

22 July 2015

Strictly Private & Confidential

As indicated on its cover page, the document(s) contained within are confidential unless and until the Joint Committee decides otherwise including where the Joint Committee publishes such document(s). For the avoidance of doubt, "documents" include witness statements in this context. Further to section 37 of the Houses of the Oireachtas (Inquiries, Privileges and Procedures) Act 2013 ("the Act"), while the documents remain confidential, you must not disclose the document(s) or divulge in any way that you have been given the document(s), other than:

> "(a) with the prior consent in writing of the committee,
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Serious sanctions apply for breach of this section. In particular, your attention is drawn to section 41(4) of the Act, which makes breach of section 37(1) a criminal offence.

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

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Joint Committee of Inquiry into the Banking Crisis
Submission Paper
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Opening Statement / Introduction

In my invitation to appear before the Joint Committee of Inquiry I was asked to give evidence relating to a number of lines of inquiry in the context of my role as CEO of EBS. I took over responsibilities as CEO of EBS on 14 January 2008, less than 8 months before the commencement of the Government guarantee. I joined the EBS Board on 1 February 2008. In July 2011, EBS was acquired by AIB and in December 2011, I was appointed Director of Transformation at AIB. I continued in the role of CEO of EBS until July 2012.

On my appointment as CEO I was specifically mandated to renew EBS at a very difficult time for the institution and to make changes that would help remedy the mistakes of the past. This was an enormously challenging period. As a consequence of my international experience I had formed the view that a correction in the Irish property market was likely. Upon joining EBS I soon realised the extent of the problems that existed in the institution, particularly in relation to its property lending. However, I did not predict that the down turn would be as severe as it has been and I thought that EBS was fundamentally sound and would survive.

By way of brief summary, my career progressed through a number of international banking institutions prior to joining EBS. I joined Rabobank in 1994 and held a range of senior positions at the bank including Global Treasurer Rabobank International and then Managing Director of Rabobank Ireland plc before becoming CEO Rabobank Asia. I had previously worked in Banque Nationale de Paris (BNP) and Kredietbank in a variety of treasury and capital markets roles. During my time with Rabobank and BNP I developed strong international banking expertise covering capital market, institutional business, and retail. On my return to Ireland in 2007 I was approached to join EBS as CEO.

My appointment to EBS resulted from a comprehensive selection process and my understanding is that, among other aspects, my experience in capital markets was considered a key asset by the interviewing panel as it was seen as a way of broadening the knowledge and skill set at executive level, particularly in light of the challenges facing EBS. My familiarity with international best practice in governance, prudential banking practices and risk management, gained in my years at Rabobank, was also an important factor in my selection. I also had the advantage of knowing EBS as I had tried, on behalf of Rabobank, to acquire EBS in 2002/2003 prior to my departure to Asia. This was prior to EBS moving into Land & Development lending in 2005.

EBS had, in the period before my tenure, built a significant loan exposure in Commercial Property and Land & Development lending. This exposure had been funded primarily from short term wholesale markets. The legacy impact of these two factors, in particular, contributed to a significant weakening of the institution as losses crystallised through the transfer of assets to NAMA, as the underlying weakness of the economy increased the level of non-performing loans, and as the institution deleveraged to a more sustainable funding profile. Ultimately, the cost of this legacy, despite advanced talks with third party capital providers, was borne predominately by the Irish taxpayer.

During my tenure at EBS, I sought at all times to minimise the potential capital impact of these legacy issues through a range of strategies including, in summary:

- Changed the profile of EBS from an institution with a high risk appetite to one that was much more risk averse. In particular, I led the adoption by EBS Board of a Risk Appetite Statement;
- Initiated a withdrawal from Land & Development lending within four months of taking office and a withdrawal from Commercial Property lending within six months;
- Continuously tightened new residential mortgage lending criteria thereby reducing credit risk;
- The net effect of the above steps reduced annual growth of the total loan book from circa 20% per annum on average in the years (2002-2007) preceding my appointment to an average per annum growth rate of circa 1% from 2008 onwards. The annual growth of the residential mortgage lending book reduced from 17% on average in 2002-2007 to circa 2% from 2008 onwards;
- Implemented a cost cutting programme that achieved a 20% reduction in the EBS cost base in two and half years;
- Strengthened corporate governance practices and internal controls, while building a culture of responsibility and accountability;
- Strengthened EBS' funding management by shifting the focus from short-term wholesale funding to retail deposits, representing 1.7 times the volume of net residential mortgage lending during the period 2008-2011;
- Established a covered bond bank in 2008 which generated stable long-term funding of €1bn in November 2009;
- Implemented a bilateral repo programme which helped to reduce reliance on Central Bank funding;
- Put in place a robust contingency liquidity infrastructure; and
- Relentlessly pursued all opportunities to improve the capital strength of EBS and reduce the need for State support, including debt buy-backs at a discount and leading discussions with numerous counterparties to effect a sale/merger of EBS that would secure its future.

I would like now to specifically address the lines of enquiry asked of me in the invitation document.

TOPIC 1: B1 Effectiveness of banks' board governance, client relationship and business model

- *Composition and experience of board and board subcommittee (b1a)*
- *Quality of the business model setting process (b1c)*
- *Adequacy of board oversight over internal controls to ensure risk is properly managed and monitored (b1d)*

There were a number of critical factors relevant to the effectiveness of EBS' governance leading up to and upon my arrival in January 2008 and which had a bearing on the subsequent steps undertaken to improve that governance:

- EBS' status as a mutual organisation, with an ownership base made up of customers or "members", had a bearing in particular on Board composition. The appointment of Board directors from the membership base was a throw-back to former times and was unwieldy;
- There were a number of Board and senior manager and executive resignations preceding and immediately subsequent to my arrival, resulting in significant organisational changes and realignment of the key management team;
- There was transformational change in the regulatory environment from a principles-based prudential risk approach to a more "assertive" and micro risk based approach which led to a significant increase in the level of CBI regulatory oversight of all banks including in the area of governance.

During my tenure as CEO, significant changes were made to the EBS governance structure to meet new regulatory standards and to align with best international practice, while building a new, professional senior management team to implement these requirements and practices.

Some key steps undertaken during my tenure to enhance the quality of Board Governance include:

- I undertook to improve EBS' Risk Appetite Framework. The Risk Appetite Statement was proactively developed in 2009 before being approved by the Board Risk Committee and the Board in July 2010;
- As a core objective, I immediately sought to significantly increase the level of governance at EBS in line with international best practice with a strong emphasis on board oversight and its engagement in the risk management function;
- The effectiveness of the Board and Board Risk Committee was strengthened and oversight of risk management improved. For example,
    - Appointment of Chief Risk Officer ("CRO") with a reporting line to the Chair of the Board Risk Committee
    - Enhanced risk management capacity by improving training for the Board e.g. a Risk Management Manual was compiled for Board induction and for ongoing monitoring and evaluation
    - External assessments of the Board's effectiveness were conducted. Material Board subcommittees also undertook annual reviews of their effectiveness
    - Increased information and risk reporting to the Board and subcommittees
    - Increased the number of meetings held by the Board Risk Committee

The Board of Directors and/or the Board's Risk Committee constantly reviewed and "health-checked" adherence to new guidance on corporate governance. I also promoted the adoption of a risk control framework based on the "three lines of defense" model which is considered best practice, with actions including:

- Removing responsibility for the commercial property lending from the Finance Director/CRO role;
- Separating the CRO and Finance Director roles and creating a new CRO role reporting directly to the CEO. The CRO was also given a dotted reporting line to the Chair of the Board Risk Committee;
- Appointing a full-time Head of Compliance;
- Moving the Compliance reporting line to the CRO;
- Filled a regulatory relationship manager position to ensure that there was an appropriate CBI engagement policy in place.

In addition to improvements to EBS' governance structures and processes I took steps to change the business model to one that was more risk averse than in the years preceding my arrival through changing lending and funding strategies. These steps are discussed in more detail on **pages 6-9**.

TOPIC 2: B2 Effectiveness of banks' credit strategies and risk management

- *Appropriateness of property related lending strategies and risk appetite (b2a)*
- *Appropriateness of credit policies, delegated authorities and exception management (b2b)*
- *Analysis of risk concentration in the base, the adverse economic scenarios and the impact on capital structure (b2c)*

On joining EBS in January 2008, I identified a number of concerns with respect to risk appetite and property lending strategies. As context, the EBS total loan book had grown from €5.7bn in 2001 to €15.9bn by the end of 2007. There was a large increase in residential mortgage lending at the Building Society in the previous 6 years, and the residential mortgage book had grown from circa €5bn in 2001 to €14.2bn by 2007. The institution had entered Commercial Property lending in 2001/2002, a departure from its core business, and critically, EBS also had entered Land & Development lending over the period 2005-2007. Those two books had grown to a combined €1.7bn exposure by the end of 2007.

I set about pursuing a significantly more conservative credit and risk appetite than over the years preceding my arrival:

- **Ceased Land & Development lending**: In April 2008, after reviewing the condition of the balance sheet, I immediately initiated a cessation of Land & Development lending, due to its high risk characteristics, the overheated nature of the domestic property market and recognition that it was non-core exposure for EBS core strategy;
- **Ceased Commercial Property lending:** In June 2008, I initiated a cessation of all other Commercial Property lending;
- **Pursued strategy of managing down commercial book**: To aid this process, I employed a number of commercial property lending professionals, closed regional lending offices and improved controls by consolidating operations into a more centralised operation. Staff were internally reassigned to wind down the book and processes and procedures were embedded to ensure the portfolio was managed in an effective manner;
- **Tightened residential mortgage credit standards:** With the above changes, residential mortgage lending then became the core lending function in EBS. I also tightened credit underwriting standards and shifted the focus to more sustainable, lower risk products by reducing the share of new business related to Buy-to-Let, switcher and equity release products;
- **Strengthened focus on "at risk" and non performing customers**: In late 2008, EBS set up task forces to manage residential and commercial customers that were non-performing or "at risk". EBS also actively worked with external bodies to evaluate potential forbearance measures including commissioning an external review of Potential Solutions for Mortgage Debt Management in Ireland and presenting its findings to the Joint Committee on Social & Family Affairs. I believe EBS was to the forefront of developing approaches to managing such borrowers given these initiatives preceded the requirements of the Mortgage Arrears Resolution Strategies and the October 2011 Keane Report; and
- **Improved risk management:** As discussed earlier, I also took steps to improve EBS risk management such as separating the roles and/or reporting lines around Finance Director, CRO and Head of Commercial Property Lending.

The effect of these changes was to dramatically reduce the growth in the EBS loan book, which grew by circa 1% per annum in the years 2008-2011 compared to the annual growth rate of 16% in the period 2005-2007. The tightening of residential lending standards to those based on a more sustainable and cash flow based criteria significantly improved the quality of new loans originated from 2008 onwards. However, even after the cessation of Land & Development and Commercial Property lending activities in 2008, the legacy of those exposures was to heavily impact the institution's capital base in the years to come.

TOPIC 3: B3 Effectiveness of banks funding liquidity strategies and risk management

- *Appropriateness of funding sources, the mix, maturity profile and cost (B3a)*

EBS had traditionally pursued a conservative funding strategy. For example, in the late 1990s retail deposits were the primary source of funding for EBS. However, by the start of 2008, EBS' funding profile consisted of 26% retail deposits and 74% from various wholesale sources and corporate deposits, with a clear overreliance on wholesale funding (36%). By the time I joined EBS, the contraction of the global funding markets that began in mid-2007 was significantly impeding EBS' access to the wholesale and corporate funds.

I sought to immediately shift management and Board focus to improving liability management in order to mitigate funding difficulties by:

- **Increasing retail deposits:** I sought to fund net growth in the residential mortgage book with retail deposits. EBS achieved a growth in retail deposits of €2.0bn over the period January 2008 to December 2011 versus net residential mortgage lending of €1.2bn in the same period;
- **Maximising long term debt issuance & implementing secured funding platforms**: in November 2008, EBS Mortgage Finance was established as a covered bond bank and to facilitate securitisations;
- **Ensuring that robust contingency liquidity mechanisms were in place:** I also established a platform to increase the amount of collateral available for contingency liquidity purposes; and
- **Asset & Liability Committee (ALCO):** I immediately set about strengthening the ALCO process. For example, I expanded the scope of the meetings to include a focus on retail deposits. In addition, significant time was devoted to the Internal Capital Adequacy Assessment Process **(ICAAP**) at ALCO and other fora**.**

Given the macro environment, and the particular difficulties faced by the Irish banking sector, these measures were not sufficient to prevent EBS from having to utilise emergency funding mechanisms such as the Credit Institutions (Financial Support) Scheme and the Credit Institutions (Eligible Liabilities Guarantee) Scheme. In addition, reliance on Central Bank funding fluctuated through the crisis and peaked in 2010 at 26% of total funding as a range of international shocks impeded access to alternative sources of finance. However, I believe were it not for the various funding and liquidity initiatives outlined above the reliance by EBS on emergency funding mechanisms would have been greater.

Capital structure and loss absorption capacity (B3e)

At the end of 2007, EBS had circa €1bn of total regulatory capital comprising €811m of Tier 1, including €245m of hybrid capital instruments, and €265m of Tier 2 capital which was predominantly comprised of subordinated debt. This equated to a Tier 1 Capital ratio of 9% and a Total Capital Ratio of 11.9%. However, as a mutual Building Society, EBS had limited ability to raise external capital as it could not raise equity capital from its members. Therefore under my leadership EBS implemented a number of initiatives to strengthen its capital through other means including:

- **Capital Forum**: I established a management committee that was charged with formulating, implementing and monitoring capital management;
- **ICAAP**: under the Basel II requirements adopted by Ireland in 2007 and 2008, credit institutions were obliged to submit ICAAP reports to CBI. Under my leadership, the ICAAP

was substantially developed and integrated within the risk management framework. I believe the enhanced ICAAP improved the risk and capital management processes of EBS;

- **Operating earnings:** costs were reduced and margins improved by introducing Risk Adjusted Return on Capital ("RAROC") discipline;
- **Subordinate buybacks**: In 2010 and 2011 EBS bought back/redeemed its outstanding subordinated debt and hybrid capital instruments at market prices resulting in a total net gain of €319m which contributed to EBS' capital;
- **Improvement in loan book quality**: through the cessation of Land & Development and Commercial Property lending and improvements in credit underwriting standards for residential mortgages I believe capital was preserved through less provisioning than would otherwise have been required;
- **Third party capital discussions:** From 2008 onwards, EBS entered discussions with a range of financial institutions (foreign and domestic) and private equity investors with the goal of agreeing an alliance or take-over of the Building Society. This culminated in the appointment of a preferred bidder for the institution in February 2011; and
- **Retail deposits:** As discussed, because of my refocussing EBS' funding strategy to retail deposits, EBS achieved a growth in retail deposits of €2.0bn over the period January 2008 to December 2011. While deposits are not treated as regulatory capital, as discussed further below in **Topic 5 pages 11 - 12**, there is a critical link between the capital strength of a bank and the strength of its funding. Therefore I believe the additional retail deposits raised during my tenure assisted in reducing the instability of EBS during an extremely volatile time.

While the level of additional required capital identified by PCAR I and II was considerable and subsequently led to the requirement of State support, I believe the above initiatives taken together lessened the need for State support as we continually sought to reduce the damage of the legacy loan exposure at the bank. The increase in retail deposits during my tenure significantly lessened the need for central bank and emergency State support, while we pursued all options available to raise external capital for the institution.

<u>TOPIC 4: B5 Adequacy of the Incentive and Remuneration arrangements to promote sound Risk Governance</u>

- *Adequacy of the incentive and remuneration arrangements to promote sound risk governance (b5a)*

EBS remuneration policy was set by the Remuneration Committee which was responsible for approving all material remuneration decisions. I cannot comment on the adequacy of the role of incentive and remuneration in promoting good risk governance at EBS prior to my arrival but I can say that from 2008 onwards no executive or manager bonuses were paid.

TOPIC 5: C2 Role and effectiveness of policy appraisal regime before and during the crisis

- *The liquidity versus the solvency debate (C 2c)*

From my experience, there is a critical link between the capital strength of a bank and the strength of its liability structure. Weakness in the liability side of a bank's balance sheet and overreliance on shorter term or temporary funding sources undermines the stability of a bank in times of extremity or shocks to the banking system. The remedy requires a significant increase in stable funding lines or decrease in the asset side of the balance sheet i.e. deleveraging the bank. Equally, worries over the capital base of a bank, in providing the protection to absorb future losses, affect the ability to attract stable funding sources.

This circular relationship is a negative force in times of banking market stress. Add in over exposure to a high risk asset class depreciating in value (i.e. falling property values) and the uncertainty over capital strength ultimately can undermine attempts to solve funding problems.

The Irish banking system's reliance on wholesale funding, a dependency shared across the European banking system, proved to be a critical weakness when the US sub-prime destabilisation of August 2007 ultimately lead to the weakening and then closing of access to market funding lines in 2008.

Whilst EBS' customer funding profile at year-end 2007 compared favourably to peers, for an institution of its size and mono-line nature with greater sensitivity to the cost of funds there was an over-reliance on short-term funding. Similar to other institutions, prior to my arrival at the bank in 2008, EBS had availed of the keen pricing and ready access to wholesale funds (particularly shorter-dated funds) which facilitated significant balance sheet growth up until 2007. The complete dislocation of the wholesale funding markets in the latter half of 2007 prevented EBS from securing any long term funding. Furthermore, EBS faced significant refinancing requirements in the first half of 2008. By the time I joined EBS, the damage had been done and could not be corrected in the short term. Nevertheless, as outlined on **pages 8-9**, a comprehensive program to strengthen the stability of EBS' funding was instigated in early 2008 which significantly reduced the potential for loss already embedded in the structure of EBS' liabilities.

Our concentration on solving the funding problem at EBS drove a growth retail deposits of €2bn over the period January 2008 to December 2011. EBS was also the most successful of the covered institutions in retaining customer deposit funding, losing just 4% of its total deposits in 2010. The institution actually increased retail deposits by €531m in 2010, despite the Greece debt crisis in May 2010, which fundamentally destabilised the global markets in the lead into the expiry of the guarantee scheme.

The program to seek new capital partners for the bank in 2010, to decrease the potential cost to the taxpayer, could not ultimately alleviate the damage that was done by the excessive property lending which had taken place pre 2008. When in 2010 €836m of property loans, originated in just two years between 2005 and 2007, were transferred to NAMA at an average discount of circa 60% the resulting capital loss on those loans was very damaging.

My view is that, in isolation, the capital impact of the loss generated from property lending pre 2008 proved to be the dominant reason why the institution required external capital support in 2010 and 2011. EBS, during the period from 2009 to 2011, sought to reduce that bill through continual talks with third party investors, to the stage of agreeing a preferred bidder in February 2011. However, it was the combination of the nature of the funding difficulties that the society faced by early 2008, accompanied by the sharp downturn in the Irish economy and the collapse of the property market, that created a follow on impact on capital, which undermined EBS's autonomy in funding and capital plans.

<u>TOPIC 6: C3 Appropriateness and effectiveness of DOF actions during the crisis</u>

- *Appropriateness of the Bank Guarantee decision (C3b)*

As CEO of EBS, I was not party to any discussions with the Irish State in the period before 29 September 2008 about the guarantee scheme which was agreed that night, or any proposals to put in place a guarantee scheme for the Irish banking system.

EBS was the largest building society in the Irish State, but despite the underlying structural weakness of its funding profile and the build out of property lending pre-2008, the liquidity worries which dominated in the summer of 2008 did not extend to EBS in the way that it did to INBS and Anglo Irish Bank. EBS was not under pressure from a significant flight of deposits in the lead up to the guarantee, although weakness in the wholesale funding markets were challenging to the Society.

My first knowledge of the guarantee scheme announcement was through a short call with my Chairman early on the morning of the 30 September. He had been contacted by the CBI. This was followed by confirmation that EBS would have to apply to be covered under the guarantee scheme. At EBS, we had spent the months since my arrival in January 2008 reviewing all alternatives for stabilising the funding profile of the society but a guarantee of any kind would not have been factored into our plans. When a guarantee was formally announced, EBS was named as one of the covered institutions and we had no input into its construct or make up.

It is clear, in hindsight, the conditions which precipitated the decision to put in place a guarantee scheme were fully in existence before I took over leadership at EBS in January 2008. The property exposure that had been built into the Irish system over the previous 5 years to 2007 and the increased dependency on wholesale funding to predominately fund that exposure proved a critical weak point for the banking sector. As wholesale interest rates increased significantly from August 2007, this weakness was to prove deeply damaging as wholesale markets shut in 2008.

The reality that the crisis was already in play by 2008 is a point well captured by Professor Patrick Honohan in his 2010 report ("The Irish Banking Crisis - Regulatory and Financial Stability Policy 2003-2008"). In discussing his report with the Houses of the Oireachtas Joint Committee on Finance and Public Service on 15 June 2010, Professor Honohan noted:

> *"…We know clearly enough the real bubble from the banking point of view and the excessive lending started somewhere in 2003. The period 2003 to 2007 is the real bubble period."*

Professor Honohan wrote in his report that:

> "*..above all, the lending decisions that generated this huge cost were made long before the point was reached of the guarantee. The damage had already been done*."[1]

In hindsight, given the weakness of the Irish banking system in the lead into 2008 and the acceleration of negative international events (such as Lehman's collapse) by September 2008, the options available were limited by the night of 29 September 2008.

[1] P. Honohan, "The Irish Banking Crisis - Regulatory and Financial Stability Policy 2003-2008", 2010, page 15

TOPIC 7: C4 Appropriateness and effectiveness of domestic policy responses

- *Decision to recapitalise AIB Anglo, Bank of Ireland, EBS, PTSB, and the alternatives available and or considered (C4c)*
- *Effectiveness of the actions to merge AIB and EBS, Anglo and INBS, and deposit transfers, CISA (C4d)*

As a prelude to examining the path to recapitalisation at EBS in 2010 and 2011, I want to put the period in context. EBS had Core Tier 1 capital at the end of 2009 amounting to €455m, which was used to absorb impairment provisions on the residential and commercial book in 2010, offset by gains on the buyback of capital instruments and operating profits for the year.

Following the PCAR I exercise in 2010 the CBI determined that EBS required €875m of capital. This was to cover: 1) the expected losses on the sale of assets to NAMA and the impairment provisioning on that loan book; and 2) to bring the Core Tier 1 ratio from 4% to 8%.

As stated EBS's status as a mutual Building Society limited its ability to raise external capital. Under my leadership EBS implemented a number of initiatives to strengthen the Society's capital and lessen the need for State support (as set out on **pages 8-9**). When Irish banks and EBS were denied access to the capital markets, I attempted to find a partner that would solve EBS' capital problems. I also actively pursued private equity investors. Following the 2010 PCAR, I established the Capital Forum, a management committee that was charged with formulating, implementing and monitoring capital management.

As the requirement for a sale / merger with a third party seemed likely from September 2008 onwards, this was included as a potential capital source in EBS' capital planning. EBS also outlined in its EU Restructuring Plan submitted in May 2010 the plan for a sale and was instructed to commence the sale process by the Department of Finance / NTMA in May 2010. EBS attracted a number of interested parties and a preferred bidder was confirmed by the NTMA in February 2011. The discussions with the Consortium were ended by the NTMA on 30 March 2011 prior to the announcement that EBS was to be merged with AIB on 31 March 2011.

In 2011, before the merger announcement with AIB, the CBI conducted a Prudential Liquidity Assessment Review (PLAR) and a second PCAR exercise that determined EBS required additional capital of €1.5bn to cover forecast impairment of the commercial and residential property loan books and expected deleveraging losses. This total additional requirement also included a buffer of €300m at the discretion of the CBI.

As a mono-line bank, the future of EBS as a standalone was always dependent on government strategy and on the type of banking sector which could be agreed with the Troika. The decision to merge AIB with EBS was taken on the basis that a stronger combined bank would emerge to lend to and support the Irish economy as a "Pillar Bank" alongside Bank of Ireland.

I think that the past three years have shown the success of that merger. Since the merger, AIB, in combination with EBS, has recovered significantly. In its role as a principal lender in the Irish economy, the AIB committed €6bn in new lending in 2014 and as growth takes hold, in line with the recovery of the economy, the bank has a role to continue to support it. AIB recorded profits over €1.1bn in 2014, the highest level in 7 years. EBS produced profits of €128m during that period. AIB's Core Equity Tier 1 ratio reached 16.4%, from 15% in 2013. With a loan to deposit ratio of 99%, AIB has significant potential to grow its balance sheet in a sustainable way, underpinned by both the opportunities here and abroad. The group outlined a strategic plan three years ago to bring the bank from restructuring to stabilisation to positioning for growth and profitability. We have met and exceeded the targets we set ourselves and in 2014.

AIB's EU Restructuring plan has been approved and we have comfortably passed the Comprehensive Assessment. We hold leading market shares in core Irish target markets and we are targeting €7bn-€10bn in lending per annum across these markets. Our lending to corporate and business customers (ex UK) grew by over 50% in 2014 to circa €2.5bn. I believe the bank is very well positioned to return capital to its shareholder, at the State's discretion.

TOPIC 8: R3 Clarity and effectiveness of the nexus of institutional roles and relationships

- *Nature and appropriateness of the relationship between the CBI (including the Financial Regulator), the DoF and the banking institutions (r3b)*

I had little exposure to the CBI or Department of Finance prior to joining EBS in January 2008. I therefore cannot comment on the relationships EBS had with the institutions before that point.

As I joined EBS, I immediately set about establishing a strong framework for risk governance and made a number of strategic decisions aimed at containing potential losses at the society (such as the decision to close the commercial property unit) and to ease the funding challenges at the Society. I ensured that all these decisions were communicated to CBI on an ongoing basis. CBI itself would periodically request information and recommendation actions as the nature of regulatory oversight shifted from 2008, and the reporting requirement on Irish institutions increased.

My interaction with the Department of Finance was initially limited but intensified as EBS developed the plan for recapitalisation, and I worked closely with that team as we sought to find a viable capital partner for the institution up to February 2011.

As CEO of EBS I was engaged with CBI during the two stress tests, the PCAR of 2010 and PCAR/PLAR of 2011.

In my opinion during the period from January 2008 and March 2011, the engagement between EBS, the CBI and the Department of Finance was transparent, consistent, constructive and positive given the background environment in the Irish Banking sector. Today, the relationship between AIB and the Minister for Finance is governed primarily by the March 2012 Relationship Framework and is a very constructive one.

Tithe an Oireachtais
Houses of the Oireachtas

Joint Committee of Inquiry into the Banking Crisis

Witness Statement of

Fidelma Clarke

Session 52a

24 July 2015 (a.m.)

Strictly Private & Confidential

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> "(a) with the prior consent in writing of the committee,
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> (b) to the extent necessary for the purposes of an application to the Court, or in any proceedings of the Part 2 inquiry, or
>
> (c) to his or her legal practitioner."[1]

Serious sanctions apply for breach of this section. In particular, your attention is drawn to section 41(4) of the Act, which makes breach of section 37(1) a criminal offence.

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

Statement to the Joint Committee on Enquiry into the Banking Crisis

Fidelma Clarke

I have been asked to give evidence on six lines of enquiry relating to my role as Chief Risk Officer / Credit Officer / Company Secretary of EBS Building Society.

I was appointed Chief Risk Officer of EBS and became a member of the executive management team on 1 January 2009. I had been appointed Company Secretary in July 2008, and resigned from that position in June 2009 to concentrate on the demands of the Chief Risk Officer role. EBS appointed an Acting Chief Credit Officer with a separate reporting line from mine from 2010 to 2011 - a role that was independent of, but worked closely with, the Risk function.

Following the second Prudential Capital Assessment Review in Q1 2011, EBS was merged with Allied Irish Banks plc and became EBS Limited, a wholly owned subsidiary of AIB, in July 2011. In December 2011 I joined AIB as a Joint Interim Acting Chief Risk Officer in advance of a permanent Chief Risk Officer's appointment commencing. I subsequently was appointed Head of Governance and Assurance in AIB, Head of Enterprise Risk Management and am currently Head of Risk Analytics, reporting to the Group Chief Risk Officer.

In June 2012 I resigned as Chief Risk Officer of EBS as the position was no longer required. In 2012 I was appointed, and remain, a non-executive director of EBS Limited. I have also been an executive director from 2008 and a non-executive director since 2012 of its covered bond bank subsidiary, EBS Mortgage Finance.

Prior to being appointed as Chief Risk Officer I worked in the risk function as Head of Credit Policy, Credit Review and Enterprise Risk and subsequently Head of Risk, reporting consecutively to two executive directors who were the Chief Risk Officers of EBS amongst other responsibilities.

In addition to providing my witness statement for the period mid 2008 (when I became Company Secretary) to July 2011 (when EBS was merged with AIB), I have included additional contextual information for the period preceding 2009 where I felt it might be of help to the Committee.

With regard to two lines of Inquiry, namely, the appropriateness of the bank guarantee decision (C.3.b) and the decision to recapitalise Anglo, AIB, BOI, EBS, PTSB and alternatives available / considered (C.4.b), as I was not a member of the executive management team until January 2009 and had no involvement in any discussions with the Government in the lead up to the Guarantee or the decision to recapitalise EBS, I am not in a position to be of assistance in these areas.

My statement is based on my best recollection of events and a review of a limited number of historical documents. I hope the information provided will be of some benefit to the Inquiry.

Effectiveness of banks' credit strategies and risk management

- **Appropriateness of property lending strategies and risk appetite (B.2.a)**

In its Restructuring Plan submission to the EU Commission in May 2010 EBS set out the key reasons why it ran into financial difficulty which was exacerbated by the sharp economic downturn and a global credit crunch. These were

1. A decision to step up lending to the land and development sector at the height of the Irish Property boom in response to sustained pressure on net interest margins and a desire to achieve income diversification and insufficient internal controls to manage and monitor this lending.
2. Strong growth in EBS's residential loan book in a time of compressed lending margins.
3. EBS was a moderately capitalised business – albeit within regulatory requirements.
4. An over-reliance on (cheaper) wholesale funding between 1998 and 2007.

Specific controls which had been put in place to mitigate the risks of lending to the land and development (L&D) sector proved to be incapable of protecting the Society in the face of the scale of the financial crisis which ensued. These included

- An overall cap of 3% on the proportion of the balance sheet exposed to the Land and Development sector.
- A cap of 15% on the overall exposure to the commercial property sector including land and development.
- A requirement to recruit lenders with expertise in L&D lending.
- Experienced EBS commercial lending personnel to meet with customers and visit the site of all proposed developments as part of the credit assessment process.
- All sites / property taken as security to be independently valued by experienced chartered surveyors from an EBS appointed panel.

In relation to residential mortgage lending, the increase in demand for and supply of mortgage credit over the course of the 2000s has already been extensively reported on. EBS's policy changes were made on the back of the strong economic climate, improved demographics, higher income levels and improved affordability; they were also influenced by competitor practices. As mortgage lending was its core business, EBS had long-established risk mitigation controls in place, including

- A centralised underwriting unit.
- Underwriters were not incentivised / remunerated on the basis of whether they approved or declined loan applications.
- Stress tests for increases in interest rates from the early 2000s for mortgage and for commercial property loans.
- A bespoke loan affordability model (externally reviewed) incorporated an assessment on a case by case basis of how much money the loan applicants would need to live on after debt repayments.
- Mortgage Indemnity Insurance in place for higher LTV loans which ultimately reduced the losses incurred by the Society.
- Independent property valuations required in all cases.

Significant investments were made in underwriting systems, data quality, credit risk models, provision models, capital models and management information capabilities 2003 - 2007.

Clearly and very regretfully, the level of risk undertaken by the Society increased in parallel with the boom period and the control structure in place to mitigate risk transpired to be insufficient in the face of the economic and property market collapse and external market destabilisation.

Property Lending Strategies from 2008 - Risk Management of Legacy Book

The Society's risk appetite reduced substantially from the height of the boom as a result of the swift deterioration in asset quality on the back of eight ECB interest rate increases from 2005 and the knock on impact on loan affordability.

Economic forecasts at the start of 2008 pointed to a more challenging environment in the coming two years, although it transpired to be significantly more challenging than these forecasts.

The primary focus of property lending strategies and risk appetite from this time on was risk containment, servicing EBS customers in difficulty and credit loss mitigation. Key actions to mitigate risks over the period included;

Commercial Property Book

- From July 2007 EBS had significantly reduced the level of new lending to the Land and Development sector. Under the direction of a new CEO EBS ceased all lending to this sector in April 2008 and ceased lending to the commercial property sector in June 2008.
- In August 2008 EBS established task force teams to manage 'at risk' and non performing residential and commercial loan exposures. These developed into Special Asset Management teams in 2009.
- From Q1 2009 circa 70% of the Society's commercial loan asset exposures were reviewed on a case by case basis each quarter for loan loss provisioning purposes. They were subsequently reviewed by the Chief Risk Officer, Head of Commercial Credit Risk and Head of Finance before being recommended to the executive management team and the Board for approval.
- Recognising that the credit teams were not experienced in distressed credit risk management, EBS brought in credit professionals with experience of downturns to provide an independent view on the quality of the loans, potential losses and guidance on how to manage credit exposures.
- In October 2009 two external experienced credit professionals were retained to review of the provisions status and forecast in the then three year plan, the results of which were shared with the Board. Based on a (high level) review, the findings were that the provision forecasts appeared reasonable but that they could be required earlier than the plan indicated. Recommendations sought and provided for enhanced credit management were implemented over the following months.
- After an extensive search an interim Chief Credit Officer was appointed on secondment from an external firm from August 2010 to November 2011, reporting to the CEO and working closely with the Risk function.

- A project team was established in 2010 to manage the transfer of assets to the National Asset Management Agency (NAMA) and to create a capability to manage the assets post transfer on a third party services arrangement.

Residential Mortgages

- In relation to residential mortgages in the second half of 2009 EBS commissioned an external review of Potential Solutions for Mortgage Debt Management in Ireland, the findings of which were presented by the CEO and me to the Joint Committee on Social and Family Affairs in December 2009. One of the recommendations was the imposition of maximum loan to value exposures – a recent, welcome development.
- EBS subsequently worked closely with the industry bodies and the Expert Working Group in 2010 to identify and agree forbearance measures for customers in difficulty and to review how best to implement them from an operational, accounting and tax perspective.
- To address the lack of arrears management and credit counselling skills experience, training programmes were developed and rolled out.
- EBS insourced the Managing Director of a UK- based arrears management firm to review and enhance the Society's credit management operations.
- An online arrears management system was re-launched in November 2009.
- Teams were augmented with resources that had been in lending and underwriting roles and additional credit resources were recruited.
- An external firm was appointed to manage abandoned properties.
- Engagements with our mortgage indemnity insurance providers increased substantially as arrears levels increased.

The Society's objectives were to put processes in place to ensure customers were treated speedily, fairly, consistently and with respect. I believe these actions taken to contain risk over the period 2008 to 2011 were appropriate for the environment in which we were operating.

New Lending and risk appetite

In terms of the Society's appetite for new lending it was challenging through 2009 and 2010 to balance the, at times seemingly competing, requirements of key stakeholders. The Department of Finance was strongly encouraging institutions covered by the bank guarantee to provide credit to the market as evidenced in repeated statements by the Minister for Finance. Both the Regulator and external economists warned about the detrimental impact on economic recovery if credit was not made available. Having recognised that it could not survive in its current form, EBS was working with the Government and in discussions with the Regulator on a survival strategy based on public or private equity investment with an objective of retaining the Society's status as a mutual organisation if at all possible. The provision of credit was deemed necessary to remain relevant as a mortgage provider. At the same time asset quality was deteriorating at a rapid pace resulting in increases in provisions quarter on quarter and few institutions were lending.

Adding to the challenge was the apparent turning of the tide at the end of 2009 / start of 2010. There was a consensus, voiced by government, the regulatory authorities and external economists that the worst was over. What transpired was very different; the Greek crisis, the shutdown of the wholesale funding market and the consequent need for the EU-IMF bailout in November 2010.

Whilst recognising the negative impacts of a full withdrawal of credit from the market, EBS's risk appetite and its capacity for new lending was low and reduced over the period 2008 to 2011. Lending volumes and risk profiles were reduced through a series of credit policy restrictions. Lending via the broker channel which had been established in December 2007 under a separate brand (Haven) was curtailed then ceased altogether. As a result of these actions the annual growth rate of the residential book reduced from 18% in 2006 to 8% in 2008 to 2% by 2010 and was negative in 2011.

This low risk appetite of the Society was codified in the Society's first formal Risk Appetite Statement, approved by the Board of Directors in July 2010, following a board meeting dedicated to the evaluation of the risks the Society was dealing with. The Risk Appetite Statement set limits in relation to different risk positions the Society was prepared to tolerate. Specifically it included the following statements (inter alia); *'Given the scarcity and cost of credit EBS appetite for new lending is low'*; *'Credit losses on the existing loan book will be minimised by endeavouring to have in place at all times the right resources, skills and experience, systems and processes to manage credit risk'*; *'Arrears management and recovery is a priority focus of each Board meeting'*; *'The preservation of capital is paramount ; no action or decision will be taken which will jeopardise meeting the new minimum capital requirements of the organisation'*.

Adherence to the Board approved Risk Appetite Statement was monitored by the Risk function and reported in the Chief Risk Officers' report to the Board each month. This report also incorporated an assessment of the risk status, the risk outlook, and actions being taken by management to address and or mitigate the risk.

Effectiveness of banks' credit strategies and risk management

b. Appropriateness of credit policies, delegated authorities and exception management.

I concur with the views expressed by Professor Nyberg in relation to the causes of the systemic banking crisis in Ireland insofar as they relate to EBS's credit risk appetite and oversight over the period[1]. Some of the key drivers were the relaxation of credit policies (on the back of strong economic growth and fuelled by competition), the 'slow slide' from lower risk to higher risk lending, higher loan to values, equity releases, interest only mortgages, the increase in buy to let mortgages and, specifically in the case of EBS, weaknesses in the commercial lending function, particularly in the area of Development Finance.[2]

The traditionally conservative approach to lending in EBS unravelled in the period 2000 – 2007. A process of rebuilding credit standards commenced in 2008 with a detailed evaluation of the credit risk position of the organisation and the steps required to manage it. Over the period 2008 – 2011 credit criteria thresholds and standards were raised. By June 2010 more conservative criteria relating

[1] Misjudging risk: Causes of the Systemic Banking Crisis in Ireland pages 12 – 50.
[2] As above, page 35

to the type of lending (residential property only), the quantum of new lending (book growth not to exceed 5%), market share of new lending (not to exceed 17%), residential investment property lending (a maximum of 10% of total lending), weighted average loan to value limits (limited at 75%), mandatory insurance for higher LTV loans were in place, as set out in the Society's Risk Appetite Statement and its credit policies.

In the pre-crisis period exceptions to standard policy guidelines for residential and commercial property lending (which were permitted by policy) were monitored by the Credit Risk Committee and included in risk reports to the executive management and the Board Risk Committee. Exceptions (by value of exposure) were higher for commercial property lending than residential lending given the 'lumpier' nature of that lending.

By 2008 exceptions to standard guidelines (approved by underwriters based on their assessment of the underlying risk) were less than 5% and were reduced to 1% over the following two years.

Delegated Loan Approval and Cheque Issue Authorities had always been incorporated in the Society's credit policies. The application of delegated approval authorities continued post 2009.

Impact of the property valuation methodologies on banks' credit risk management

- **Adequacy of valuation policies and assumptions to accurately assess loan security (B.4.a)**

EBS always required an independent, valuation report on all properties which were being provided as security for a loan.

- For commercial property lending these valuations were required to be undertaken in accordance with the Practice statements of the Society of Chartered Surveyors.
- EBS established a panel of valuers for commercial and residential property valuations.
- Valuation reports were requested by EBS and addressed to EBS and were reviewed as part of the case assessment prior to issuing funds.
- At regular intervals valuers were asked to submit their updated indemnity insurance certificates.
- EBS also commissioned independent firms to provide valuations for a sample of valuations received to back-test for appropriateness.
- The Loan to Value exposure calculation was based on the lower of the valuation amount or purchase price.

From 2008 these valuation standards, which we deemed appropriate, were maintained.

- **Adequacy of internal controls over perfection of security and policy exceptions (B.4.c)**

There were three methods by which security was perfected traditionally.

1. *Reliance on an Undertaking - in an industry agreed format - to certify title directly to the financial institution post funds issuing.*

This was the process in place in the industry from the mid 1990s. In EBS, as in the industry, this was the primary method of taking security for Homeloans in the 1990s, and for Buy to Let loans from the early 2000s.

2. *Certificate of Title provided to an EBS appointed panel solicitor.*

   In EBS this was the process used for commercial property loans up to €1m in exposure from the 1990s[3] and for all Buy to Let lending from 2007 (post the well-publicised alleged Solicitor fraud cases). The borrower's solicitor was obliged to certify title directly to EBS before the loans was drawn down / funds issued. Security was completed (signed charge, registration of charge and remittance of Title Deeds) by an EBS appointed solicitor following the issue of funds.

3. *EBS Solicitor conducted an investigation of title and certification of title.*

   This was the process used for commercial property lending for exposures greater than €1m from the 1990s. Title Deeds were independently verified by an EBS-appointed solicitor who provided a full title report before funds issued. The EBS appointed solicitor completed security post funds issue.

On the back of solicitor fraud events which were publicised in late 2007, EBS reviewed its policy in relation to security and its processes for tracking outstanding Deeds with a focus first on commercial property loans including the land and development book. A new process was built to produce lists of outstanding Deeds for each Solicitor Practice. These lists were issued to Solicitor's office followed by a visit by an EBS official to evaluate the status of Title registration and to agree a timeline on how and when Title would be registered and Deeds remitted.

A similar programme commenced in relation to residential mortgages. Both programmes proved effective in substantially reducing outstanding registrations.[4]

- **Analysis of risk concentration in base and adverse economic scenarios and impact on the capital structure (B.2.c)**

Given its status as a Building Society, EBS loans were secured almost wholly by property, the vast majority of which related to property in Ireland. As a result the balance sheet was highly concentrated.

Regular stress testing was conducted as part of the Society's internal capital adequacy assessment process (ICAAP) from 2008 in line with good practice and regulatory requirements.

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[3] EBS entered the Commercial Lending business in 1992 following changes in Building Society legislation.
[4] When EBS transferred its Land and Development related loan assets to the National Asset Management Agency (NAMA) there were no legal 'discounts' applied for missing or incomplete contractual documentation in contrast with some participating institutions.

Internal stress testing incorporated externally published downturn scenarios and internally approved scenarios. For example, the June 2008 stress test incorporated the adverse scenario as set out in the then ESRI Medium Term Review.

In addition, from 2009, there were quarterly increases in provisions which impacted available capital and, as a result, capital adequacy projections. For commercial credits stress testing took the form of management judgement in terms of the potential loss associated with the case in a downturn. For residential loans a statistical model, used for provisioning and loan loss forecasting, was used. The provisioning model was subject to an external review[5] which concluded that EBS was meeting good industry practice in its provisioning approach. What were believed to be conservative 'peak to trough' assumptions relating to property value reductions were incorporated in loan loss forecasts[6], and benchmarking of provisions levels in other institutions was conducted on an ongoing basis.

The appropriateness of provisions was, through this period, one of the most significant judgemental matters in terms of financial reporting and a key area of focus of external audits.

Between 2008 and 2011 EBS, like all institutions, was subject to four extensive external reviews of the financial and capital position of the Society, commissioned by the Financial Regulator culminating in the PCAR II exercise in March 2011.

At that time, it was felt that this was the final assessment of the extent of losses in a base and stress scenario. It transpired that these loss estimates were exceeded. Last year, as a precursor to the establishment of the Single Supervisory Mechanism, the European Central Bank conducted a Comprehensive Assessment of asset quality and capital adequacy for significant banks across Europe - the "European Stress Test" - the results of which were published in October 2014. This brought to an end the evaluation of asset quality, provisions adequacy and the appropriate level of capital – a process which took six years for banks, regulators and auditors, with significant input and challenge by external experts.

Effectiveness of banks' funding, liquidity strategies and risk management

- **Analysis of liquidity risks under adverse scenarios (B.3.b)**

In 1998 EBS's loan book was funded solely by deposits. Between 1999 and 2007 the loan book grew by 300% while deposits grew by 170%. Similar to other institutions the gaps had been funded through (cheaper) wholesale funding and international corporate deposits. As we now know, this was an unsustainable model and new regulatory requirements in relation to loan to deposit, liquidity coverage and net stable funding ratios are in place to prevent a re-occurrence of this situation.

[5] EY Risk Analytics UK October 2010 reported to EBS and presented to the Central Bank.
[6] 55% from February 2010 for residential property, 54% for EBS commercial property exposures

EBS undertook a quarterly stress testing of liquidity from 2006 in line with its Liquidity policy, based on Sound Practices for Liquidity Management published by the European Banking Authority[7]. These included scenarios specific to the bank (idiosyncratic) and those which were systemic in nature.

Given market conditions the Society's Liquidity Crisis Management process was instigated at the end of 2008 as per its Liquidity Policy.

- The liquidity crisis management team (including the Group Treasurer, the Finance Director and the CRO) met on a weekly basis to review liquidity positions, forecasts and plans to mitigate the impact of further unplanned outflows.
- From January 2009 the Asset and Liability Committee was meeting twice monthly and monitoring the liquidity and funding position of the Society tightly which had been negatively impacted by rating downgrades and concerns regarding sovereign risk.
- Deposit withdrawals were closely monitored and interest rates increased where possible/appropriate to retain them.
- On the treasury side, collateral was utilised as efficiently as possible to create lines of credit with the ECB and EBS issued public then retained bonds to support the Society's liquidity position.[8]
- Liquidity stress tests were run monthly and there was weekly reporting of the liquidity position and projections to the Regulator and, for a period of time, daily reporting of the Society's liquidity position.

Although the liquidity position of EBS had improved by the end of 2009, its ability to access funding and the cost of funding were directly impacted by the closure of markets to Irish institutions in mid 2010 on the back of the Greek crisis. Rating reductions meant that existing pools of collateral used for repo purposes were in some instances no longer eligible.

In October and November 2010 there was also some uncertainty in relation to the continuation of the government's Eligible Liability Guarantee scheme (ELG). The combined impact of these developments was that EBS ran out of contingency options in December 2010 and needed to avail of the European Central Bank's Emergency Liquidity Assistance, and again in 2011.

In summary, funding and liquidity risks were managed tightly throughout the crisis but despite the Society's best efforts, the scale of the crisis rendered these efforts unsuccessful.

- **Interest rate risk appetite setting and monitoring (B.3.d)**

Interest Rate risk in EBS was traditionally low as EBS did not operate a trading book (in accordance with the Building Societies Act). Hedging instruments were used to reduce interest rate risk, not to create it. Interest rate risk was managed by setting upper limits on interest rate sensitivities. The maximum permissible level was set by reference to the gap and sensitivity to a 1% parallel increase in interest rates. It was set at a low level of €12.5m. Throughout my tenure as CRO (and preceding it) it was monitored and reported on each month by an independent Treasury Risk team and reported to the Board in the Chief Risk Officer's report.

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[7] Then the Committee for European Banking Supervisors (CEBS).

[8] EBS had established a covered bond bank in Q4 2008 (EBS Mortgage Finance).

- **Capital structure and loss absorption capacity (B.3.e)**

EBS operated within regulatory capital requirements throughout the pre-crisis years, but its Tier 1 capital ratio of 7.9% at the end of 2008 was inadequate to absorb the unprecedented level of provision losses arising from the crisis.

Following the Q1 2010 PCAR exercise EBS was required to attain a Core Tier 1 capital ratio of at least 8% by December 2010 and 12% from end February 2011. This would require an injection of €875m of capital. The government became a majority shareholder in the Society in May 2010 following the provision of €100m in capital in the form of Special Investment Shares. A further €250m of capital was received in June by way of a Promissory Note with additional capital of €525m pledged.

EBS was required by the Department of Finance to secure the viability of the organisation through a sales process. A shortlist of preferred bidders was confirmed in October 2010 and a third phase of due diligence commenced in November 2010.

On the conclusion of the PLAR and PCAR exercises in March 2011, the level of recapitalisation required for EBS increased to €1.5bn and it was decided to merge EBS with AIB bank.

Clarity and effectiveness of nexus of institutional roles and relationships

- **Relationship between and appropriateness of relationship between the Central Bank, the Department of Finance and the banking institutions. (R.3.b)**

I had little personal interaction with the Department of Finance in the pre or post crisis period. As a covered bank requirements were placed on all institutions in relation to their governance and operations, which required internal review and external audit assurance on a quarterly basis. Requirements were increased following the recapitalisation of the banks in 2010.

In contrast, I have had a high level of interaction with the Central Bank throughout my career. This increased from 2008 given the nature of my role and the change in the approach to supervision. As is well documented, the approach of the Central Bank became more independent, challenging and intrusive following the crisis, as appropriate in the circumstances. The volume and depth of information required by the Regulator increased very significantly, there were more regular on-site reviews and observers from the Central Bank attended EBS Board, Board subcommittee and executive risk management committee meetings. I believe EBS represented itself in a professional, credible manner in the toughest of environments - for all involved.

Conclusion

The sustained success of the economic environment from 2000 to mid-2007 led to an incorrect consensus that early concerns of a housing bubble were misfounded .

The fundamentals of risk assessment that were employed were insufficient; the industry underestimated both the probability of an economic and property market collapse occurring and its impact in terms of loan losses. This was compounded by an international credit crunch.

It has taken more than six years to fully size the impact of the deterioration in asset quality which concluded with the publication of the European Central Bank's Comprehensive Assessment in October last year.

There is a reference in Professor Nyberg's report[9] that '*EBS had a system that was not adequately resourced and seems to have lacked influence within the bank*'. In retrospect, I think there is truth in that statement. The core risk team comprised three individuals in 2002 rising to 18 by end 2008. The risk agenda over this timeframe was very extensive, including compliance with new governance standards, the establishment of Board and executive risk committees, the adoption of new Accounting Standards in 2005, implementing the Basel II Programme 2004-2007 and building out risk modelling, management information and regulatory reporting capabilities in addition to the workings of the core risk function. Independent second line challenge in the form of a dedicated Chief Risk Officer role, a corporate governance requirement today, was not in place. That is not to say that the outcome would necessarily have been different if it was, and corporate governance standards were at an evolving stage. But it was a finding of Mr. Nyberg's review that warrants acknowledgement.

It is a source of great personal sadness and regret that a company I worked so long for and was proud to be a part of failed, and in so doing contributed to the banking crisis. The crisis and its aftermath have been debilitating in terms of Irish people's financial and in many instances personal health. I fully acknowledge my share of responsibility, together with others in EBS in the pre-crisis period, for that failure. As Chief Risk Officer of EBS I worked to the best of my ability with the executive team to minimise where we could its impacts on customers, on EBS and on the economy. I am sorry that I could not do more.

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[9] Misjudging Risk: Causes of the Systemic Banking Crisis in Ireland March 2011 – page 47.

Tithe an Oireachtais
Houses of the Oireachtas

Joint Committee of Inquiry into the Banking Crisis

Witness Statement of

Ethna Tinney

Session 53a (a.m.)

29 July 2015

Strictly Private & Confidential

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

Witness Statement of Ethna Tinney

Further to the direction of the Joint Committee of Inquiry into the Banking Crisis to make a statement in writing on the following lines of inquiry relating to my role as Non-Executive Director of the EBS Building Society (referred to below as EBS) I say as follows:

To Quality of the business model setting process (B1c)

There was no such process as the business model had been set prior to my joining the board.

In 1985 when I wanted to buy a house the rules of EBS were clear. Ninety percent of the purchase price was the maximum you could borrow and two and a half times your salary. If you had a spouse or overtime, half of what each of these brought in annually could be added. Documentation had to be produced to verify applications. All Irish banks had similar rules.

By the time I joined the board of the society fifteen years later in December 2000 those rules had been abandoned, not just by EBS but by most, if not all, lending institutions. Mortgage applicants' declared incomes were sometimes well in excess of reality and up to six times the applicant salary was approved.

This happened gradually as the price of houses went out of the financial reach of most people, had the old rules still applied. I paid up to 14% per annum on the mortgage I held from 1985-1996 but, in the new euro scenario, interest-rates had plunged which seemed to even out the risk. The risk of jobs being lost was not factored in, largely due to the country's booming economy.

The induction to my new role as an EBS non-executive director was pleasant. The staff were delightful, and the managers who explained their processes to me equally so. However, I was uneasy when I was introduced to the idea of securitisation.

In simple terms this is a way of packaging up mortgages into an asset and selling them on to a new layer of investors, who agree to pay a percentage of the nominal value of the loans in return for an agreed interest so that their money can be lent on again for new mortgages.

It is ingenious in its way, as it is a system that seems to offer limitless working capital for a lending institution. But there is nothing to stop the new investors selling on their asset at a profit, and so on ad infinitum. Viewed that way it has the look of a pyramid scheme, and all depends on the original mortgages continuing to be serviced, and becoming more expensive for the mortgagees. I could not get the image out of my head of a shark eating its own entrails. As time went by I became ever more doubtful of the fundamental banking concept of loans as assets, and indeed of debts in any business as assets. The only asset that reassures me is something I can control and I cannot control the repayment of debt owed to me.

To Adequacy of board oversight over internal controls, managed and monitored (B1d)

Unfortunately this proved inadequate, which became apparent when the board of EBS was finally advised that an employee in the treasury department had illicitly engaged in proprietary trading strictly against the rules of the society. Strangely, this same employee had been previously present with his manager at a board meeting when non-executive directors had probed the possibility of just such an illicit trade being made. The board was reassured at the time by the executive directors that such a thing could not happen because of so-called "back-room controls". These evidently failed and EBS sustained a significant loss. Similar scenarios unfold in other banks all over the world from time to time.

But far more damaging was the decision by the board to sell the headquarters in Westmoreland Street owned by the society in order to transfer to a rented premises in Burlington Road. Over time it became apparent that this was a catastrophe and the full board did not have oversight of the implications of the decision.

To Appropriateness of property-related lending strategies and risk appetite (B2a)

Lending large sums to developers was new to the society. The senior management in EBS, as in most of the lending institutions, were taken-in by Ireland's so-called developers and also by their professional and other advisors. So were the members of the board, including me. The belief that there were substantial profits to be made for the society from those developments led us to emulate our peers, although we had been cautious about joining the bandwagon. There was a sort of feeding-frenzy as the banks clambered over one another to get a piece of the action, especially as new foreign banks had entered the market as competitors.

To Appropriateness of credit policies, delegated authorities and exception management (B2b)

I was taken off the nominations committee at the end of 2006 and put on the credit committee. In the period from December 2006 to April 2007 I was inundated via email by proposals from EBS senior management on behalf of "developers" for quantities of cash in the tens of millions which appeared to be asset-backed and also to contain personal guarantees. Typically, as a member of the credit committee, your approval or lack of it had to be sent also by email to EBS by close of business the same day or the next day. The rationale was that if EBS did not facilitate the "developer" another bank would and we would simply be losing out on the business. All these proposals seemed fail-safe.

It did occur to me many times that the EBS credit committee should be meeting about each of these large proposals but my colleagues on the committee seemed happy to do the business this way, and as I had clashed with the majority of the board over several matters at this stage I had no appetite for further confrontation.

To Adequacy of the incentive and remuneration arrangements to promote sound risk-governance (B5a)

The bonus system in banks is crazy. You get a bonus for lending money out. There is no incentive to get it back in. Such a system encourages greed and recklessness. It is no wonder that banks go bust from time to time.

To Appropriateness of the bank guarantee decision (C3b)

Probably until the last syllable of recorded time this will be argued by politicians, economists and journalists. My personal view as a citizen of the Republic of Ireland, perhaps to some extent influenced by hindsight, is that it was indefensible for the government in September 2008 to in effect yield the sovereignty of this country in order to shore up a banking system that is entirely of and for itself and will never change. I do accept, however, that many grave problems would have arisen if one or more banks had failed and that the full extent of the bad debts were not known at the time.

To Analysis and consideration of the response to contrarian views (R4c)

I incorporate below in italics a letter I insisted on sending to the members of EBS Building Society in advance of the Annual General Meeting in 2007.

29th March 2007

Dear Member

Your EBS 2006 Summary Statement contains on the Notice of Annual General Meeting the following words:

"Ethna Tinney retires in accordance with the Society's Rules and offers herself for re-election. (Members should be aware that the Society's Board of Directors does not support Ms Tinney's re-election as a Director)"

There are three reasons why the Board does not support my re-election.

In the years 2003 and 2004 the Board was intent on pursuing a deal with a foreign bank. This deal was characterised by the executive as a bold transformational play. I saw it as selling the family silver without giving the money to the family-you, the members. I opposed the deal from first to last. Ultimately the deal collapsed, but not before millions of euro of your money had been spent pursuing it.

In 2005 the Society advertised for new non-executive directors. I was a member of the Nominations Committee. Ten candidates were shortlisted through an external recruitment process. All ten were vetoed without any reference to me. I objected in the strongest possible terms. Last December I was removed from the Nominations Committee.

In 2006 the Board fractured over corporate governance. Three members, including me, became unhappy about aspects of senior executive remuneration and the payment of a multi-million euro sum into the Senior Manager's Pension Fund without reference to the Board.

Am I right or wrong to oppose matters which appear to me to be against the interests of you, the members? If you believe that independent judgement exercised without fear or favour is a good thing on your Board then come to the AGM on April 16th or send your proxy to arrive not later than April 9th at EBS Building Burlington Road Dublin 4 and re-elect me.

Ethna Tinney

This letter does not mention that I had repeatedly raised concerns about the size of mortgages we were lending to people. Nor does it detail my explosive response at a meeting in early 2007 to a proposal by the executive to get involved in sub-prime lending. A non-executive director colleague told me in front of the board that my response was "intemperate", although the sub-prime industry in the US was already beginning to implode. Contrarian views were not tolerated on the board of the society.

To Appropriateness of the relationships between Government, the Oireachtas, the banking sector and the property sector (R5d)

I have never had a relationship with any member of the Government, nor the Oireachtas, nor the property sector. I do not golf, do not visit tents at racecourses and am not invited to dinners. But my sense, as a citizen of Ireland and as a director of EBS for nine years, is that there is a deeply unhealthy relationship between all four.

Conclusion

I wish to emphasise that this witness statement refers specifically to my time as a non-executive director on the board of EBS in the period December 2000 to April 2007 when I was removed from it. By the time I was re-elected onto it in 2008 there had been many changes to its composition and a new Chief Executive Officer had been appointed. Sadly, it emerged during the next three years that EBS was irrecoverable. I retired from the board at the end of my third three-year term in May 2011.

Ethna Tinney

THEME: B1

Effectiveness of banks' board governance, client relationships and business models

LINE OF INQUIRY: B1b

Integrity of financial reporting

Finance Report to the Board Audit and Compliance Committee

Critical Accounting Policies and Judgemental matters for the year-ended 31 December 2007

As of 26 November 2007

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Introduction

The Buildings Societies Act 1989 – 2006 requires the society's directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the society and the group and of the income and expenditure and cash flow statements for the period.

In preparing the financial statements the directors are required to:
- Select suitable **accounting policies** and apply them consistently; and
- Make **judgements and estimates** that are reasonable and prudent.

The purpose of this paper is to bring to your attention those critical accounting policies as well as judgements and estimates that need to be considered by the Board Audit & Compliance Committee ('BACC') in advance of the 2007 Annual Report & Accounts.

Accounting Policies

The accounting policies applied in the preparation of the societies annual accounts are consistent with those used in the preparation of the 2006 accounts and we do not recommend any change to those policies for the current year. The 2006 accounting policies are attached as *Appendix I.*

The new accounting standards applicable for 31 December 2007 are *IFRS7 Financial Instruments Disclosures* and the amendments to *IAS 1 Presentation of Financial Statements.* Both of these are discussed below.

Judgements and Estimates

In finalising the annual accounts directors and management must make judgements and estimates relating to the amounts included in the accounts. This is necessary as there may be various options relating to accounting treatments or the value of particular assets or liabilities may be uncertain or within a range of probable values.

The critical accounting policies and estimates were articulated in Note 1(d) to the 2006 Annual Report & Accounts, and as noted above these are attached in *Appendix I.* By way of update for the BACC, a brief summary of the **three critical accounting policies** highlighted in the 2006 accounts is set out below. Management continue to be of the view that these are a fair summary of those matters which most involve a high degree of judgement and complexity:

1. Critical Accounting Policies

- **Loan Impairment Provision**
  The Group's impairment provisioning policy and the underlying quantitative methodology being used by the business was approved by the Credit Committee and the BACC in detail, and was most recently reviewed again as part of the half-year review to 30 June 2007. In summary, our impairment provision is sub-analysed into specific provisions and a number of collective

incurred but not reported (INBR) provisions, an analysis of which is attached as *Appendix II.*

At the half-year aggregate provisions amounted to €21.0m, representing 13bps of loans and advances. The half-year impairment charge of €2.6m was driven primarily by some specific provisions arising from detailed loan reviews, largely stemming from commercial rather than retail credits; and an increase in the collective pool provision for development finance loans. The €5m provision for endowment loans was also held.

The full year-end review is scheduled for December led by the businesses with risk oversight, and the outcome of these will be assessed at the January Credit Committee and subsequent BACC. At this point in time, we are assessing the impact of the exposures [redacted] Oireachtas-P [redacted] In advance of the full year end review of impairment losses a preliminary review of development finance loans was undertaken and the merit of increasing this pool provision assessed.

Regarding the endowment provision of circa €5.0m established in 2005, our analysis, continues to support the merit of our retaining this collective provision in the current year.

- **Effective Interest Rate**
  Interest income and expense is recognised in the income statement for all interest bearing financial instruments using the effective interest rate method. The period over which to calculate effective interest rate is a key judgement. By way of illustration of the magnitude of this policy, our 2007 results up to 31 October 2007 reflect amortised origination costs in the order of €17.5m and a deferred balance sheet position of €75m.

  Our approach to determining the appropriate period over which to amortise such costs is based on expected lives, and a philosophy of 'more likely than not', i.e. at origination what do we estimate the expected life of an individual asset to be? In moving to this method under IFRS in 2005 we agreed to use 6 years for a residential mortgage loan, 5 years for a commercial mortgage loan and 2 years for a development finance loan, as we believed these would better reflect customer behaviour and future market experience, than those previously being used under Irish GAAP. This was assessed in 2006 by reference to our historical experience using the securitisation pools and we concluded that the expected lives continue to be appropriate.

  In concluding on our 2007 results, we will be performing our annual assessment of the appropriateness of these useful lives. On a cautionary note, a slowing market coupled with increasing competition and an increase in the share of broker versus branded lending may necessitate us revisiting the sense of a 6 year life in the near future. If we were to use a 5 year life rather than 6, this year's profit would be reduced by circa. €5.3m.

Legacy discount loans continue to be treated as a separate pool with a more prudent accounting treatment being applied, i.e. being written-off over a 5 year period and/or on their redemption whichever is the earlier. The current charge to the income statement as of 31 October 2007 is €1.6m and the deferred balance is €0.6m.

- **Pensions**

  Pension accounting and the key judgements determining our liability such as the appropriate discount rate and mortality rates are examined in detail every year with our pension providers, Mercer.

  In January 2007 Mercers provided us with an estimate of the pension charge for the year of circa. €3m. A final review of the key assumptions will be undertaken in January 2008 to finalise the pension charge and this will be available for the BACC in February 2008. In addition, income continuance will be in the region of €0.5m in the current year.

  The new hybrid pension scheme launched in October 2006 for new joiners & manager promotions will necessitate some added disclosure in the accounts this year for the first time as there were no new joiners to the fund until 1 January 2007.

In addition to the above critical accounting policies, in the current year, we would also draw attention to other judgements and estimates applicable in the current year:

- **Haven set up costs**

  During 2007 both EBS and Britannia Building Society ('BBS') incurred costs involved in the set up of a proposed joint venture. On 5 November it was announced that BBS would not be entering into the JV and that EBS would be setting up Haven as a 100% owned subsidiary.

  As part of the joint venture agreement EBS and BBS agreed to split the set up costs on a 50/50 basis. Indications to date are that this arrangement continues to be valid. Total costs up to 5 November 2007 are expected to amount to circa. €9.3m of which EBS will incur its 50% share. EBS will continue to incur both internal and external costs to develop the Haven subsidiary as a stand alone entity and these are expected to be capitalised in Haven. Total costs to be capitalised in 2007 are likely to amount to circa €6m to €7m.

  We are currently reviewing the nature of the set up costs and the basis for justifying their capitalisation under *IAS 38 Intangible assets and Goodwill.* Certain criteria is required to be met under IAS 38 such as separate identification of costs and the power to control the future economic benefits that will derive from this spend.

  EBS has also incurred internal and external project development time in establishing itself as an outsource service provider. These costs are expected to amount to circa €2.5m of which €0.5m is expected to be recovered from

BBS. Again, we are currently considering the justification of capitalising some or all of these costs under *IAS 38 Intangible assets and Goodwill.*

- **IFRS 7 Financial instruments Disclosures ('IFRS 7') & IAS 1 Presentation of Financial Statement (as amended) ('IAS 1')**
  The 2007 Annual report & Accounts will contain a number of additional disclosures in order to comply with IFRS 7 and the amendments to IAS 1.

  IFRS 7 does not require any change in the basis of accounting and therefore the income statement and balance sheet are not affected by this standard. The key requirements of IFRS 7 relate to the provision of addition information regarding risks arising from financial instruments, in particular more information will be supplied in relation to credit risk, interest rate risk, foreign exchange risk, loan loss provisions and hedge accounting.

  KPMG have been engaged by EBS to perform a gap analysis between our 2006 Annual Report & Accounts and the IFRS7 requirements. In addition, together with Finance they are updating the 2006 Accounts to reflect the new disclosures. This work is well advanced. A first draft of the revised 2006 Accounts will be reviewed by management over the coming weeks with a view to obtaining external audit technical sign off thereafter. The revised 2006 & 2007 Accounts will be presented to the BACC subsequently.

  The additional disclosures under IAS1 require us to provide a summary of the objectives, policies and processes for managing capital as well as a breakdown of our total capital into each of its component parts. This work is being completed in conjunction with that under IFRS 7.

- **Redundancy payments**
  During 2007 an early retirement payment was made to the CEO of circa. €2m. This is required to be disclosed in the Annual Report & Accounts in 2007 as part of the notes on directors' remuneration.

2. Property Plant & Equipment

The residual values and useful lives of all fixed assets are estimated in order to properly write down the carrying value of those assets. Land and building are held at fair value and all other categories of fixed assets are depreciated as follows:

Computer hardware	3-5 years
Fixtures & Fittings	10 years
Premises Adaptations	10 years
Motor vehicles	5 years

Assets' residual values and useful lives are required to be reviewed and adjusted as appropriate at each balance sheet date. We continue to believe that the period over which we are depreciating is reasonable.

Property valuations will be updated by our valuers as of 31 December 2007, and are expected to be finalised by the end of January 2008 to be available for the BACC in February 2008. Based on current market performance a modest uplift in values is expected.

3. Intangible Assets

Internal and external expenditure incurred in developing an intangible asset such as computer software must be capitalised if it meets the criteria set out in the accounting standard.

Such expenditure includes costs of materials and services and costs of employee time. Similar to Property Plant & Equipment the useful life of intangible assets must be estimated and the carrying cost amortised over that period. Intangible assets are currently generally depreciated over 5 years but with some projects (i.e. Common loans, Basel) selectively up to 10 years.

In 2006, we capitalised €1.8m relating to our ongoing Basel II and Common Loan projects. In 2007 we expected to capitalise circa. €2.0m in relation to these projects.

An annual review of useful lives and residual values of all intangible assets will be undertaken in December 2007. Any changes in the current residual values or useful lives will be presented to the BACC for consideration in February 2008. However given the extensive review undertaken in 2006 we do not believe there will be any material changes.

4. Provisions (other than loan impairment provisions)

The key provisions necessitating consideration are as follows:

<u>Voluntary redundancy</u>

The VR provision is currently €0.8m which relates to 5 known departures. This will increase to €1.1m by year end for an additional 2 departures. Out of the total of 7 cases, 3 departures will take place in 2007 with the remainder in 2008.

<u>Incentive accounting</u>

There are a number of incentive schemes in place which necessitate our accruing for such costs prior to Management and/or the Remuneration committee determining the actual bonuses to be paid.

This requires us to exercise our judgement and to estimate the level of performance of the Society and of its employees. To date these have been accrued on the assumption of the society meeting financial targets and a **payout of circa 75% arising.**

AIB profit claw back

As part of the sale of the credit card book to AIB it was agreed to set aside a warranty provision amounting to circa €0.5m as they are entitled to claw back an element of the sales proceeds within a 24 month period dependent on attrition rates and also AML experience. We intend to recognise this as income in 2007 Accounts net of any payment required to be made to AIB.

Mortgage write-offs

A provision of €0.8m is currently in place for mortgage write offs. In 2006 the run rate was €0.8m and hence a provision for that amount was set up. Our experience for the period to date is that the run rate has fallen to €0.7m. These write offs are made in the ordinary course of business as a result of interest adjustments and penalty write offs relating to the current and prior years, however it is not possible to confirm what the run rate for 2008 will be hence a provision of €0.8m will be retained at year end.

Litigation provisions

[redacted] Oireachtas-P

[redacted] Oireachtas-P

Insurance provision

An insurance loss provision of €1m was put in place in 2006 to cover premiums collected by EBS which has not been paid over to insurance companies; and claims payable by EBS where premiums were collected but policies were not put in place.

During 2007 a significant amount of work has been undertaken to establish the extent of uninsured lives and work is ongoing in conjunction with Hibernian to put cover in place for any uninsured lives. Currently there are circa 400 lives uninsured and back premiums of €228k are expected to be paid over to our insurers to provide cover for these customers.

[redacted] Oireachtas-P

We believe it is appropriate to maintain a provision of €1m in the 2007 Accounts for potential claims on uninsured lives in respect of all our insurance providers (i.e. Hibernian, Caledonian, Irish Life & Genworth). **We believe** this continues to meet the requirements under *IAS 37 Provisions, Contingent Liabilities and contingent Assets* as EBS clearly has a present obligation as a result of a past event.

<u>Finance provision</u>

A provision of €600k was put in place in the 2006 Accounts to cover a number of Finance related matters but mainly in respect of the potential write off that may result in resolving the Hibernian commissions reconciliation. Commission income is outstanding from Hibernian for the period from 1 January 2006 to date. A full reconciliation has been carried out in respect of the insured lives in place between both Hibernian and EBS and Finance are currently recalculating commissions due based on these policies. From the output of this work a reconciliation will be performed with our system generated commission reports. This work will be completed in December 2007. In light of current information we believe this provision is reasonable however the position will be more certain by year end.

5. Profit Share on Insurance contracts

We are contractually entitled to a profit share from both our Allianz home insurance and Genworth payment protection contracts.

In relation to Genworth this income assessment is relatively straightforward and predictable, and is modest enough at circa €0.2m, and as such we will include the 2007 profit share in this year's results.

The Allianz position was amended in 2007 to allow for the timely recognition of income. The annual cycle was amended from a calendar year to a year end of 30 September. Therefore we will know with certainty by year end what the Allianz profit share will be and will recognise this in the 2007 Annual Accounts. Current indications are that this will amount to circa. €0.2m.

6. Premises

EBS will be holding onto the lease on ***115 Grafton Street*** for the foreseeable future and therefore the onerous lease provision of circa. €1.0m continues to be applicable. In addition we are also required to carry out refurbishments under the lease and expect this to amount to €0.7m which will be provided for in the 2007 Accounts.

7. Taxation matters

Tier 1 Transactions 2005 and 2007

Throughout much of 2007, EBS Building Society has been in discussion with the Irish Revenue authorities about the tax treatment of interest arising on the 2005 Tier 1 transaction.

Initially Revenue's position was that the interest payable by EBS Building Society was not tax deductible. In later correspondence and without abandoning its stance on the interest deductibility point, Revenue advanced the contention that EBS Capital, the note issuing vehicle established in Luxembourg for the purposes of the 2005 transaction, was tax resident in Ireland in 2005. Revenue has now assessed EBS Capital to Irish tax for 2005 at the 25% rate on the interest receivable by it from EBS Building Society. The assessment is being appealed (time limit is 30 November) but it is unlikely that a date for a hearing before the Appeal Commissioners will be available until well into 2008.

It must be assumed that Revenue will also seek to raise assessments on EBS Capital for 2006 and 2007. This would involve assessing the interest receivable by it from both the 2005 and 2007 Tier 1 issues.

The assessment already issued in respect of the year 2005 is for a sum of **€676k** in tax terms. If assessments were to be issued for 2006 and 2007 also and if they were to include the interest arising on both the 2005 and 2007 transactions, the amount of tax due up to the end of 2007 would be approx, **€4.8m.**

Management accounts will have accrued a provision of **€2.4m** by end-2007. This has been calculated on the basis of disallowance of the interest on both Tier 1 transactions charged in the EBS Building Society accounts. No provision has yet been included in accounts for Irish tax assessed or potentially assessable on EBS Capital on the basis of the legal advice currently available. The position will be reviewed at year end in the light of further consultations planned with legal advisers and Counsel.

While Revenue seems to have moved away from a challenge to the deductibility of the interest in EBS Building Society, they have not formally indicated this and the point is still open. [redacted]

Oireachtas-P

Sale of shares in EBS Asset Managers
EBS sold the entire share capital of EBS Asset Managers in 2006. The tax treatment of this sale, which was structured as an earnout, is uncertain since there is minimal guidance in statute law and no decisions of an Irish court on the point are available. Current Irish Revenue practice is based on decisions of English Courts which have been widely criticised. Consequently, when filing the 2006 tax returns of EBS Building Society in September 2007, we 'expressed doubt' about the tax treatment and invoked a provision in Irish tax legislation which provides for tax exemption on the proceeds of disposal of shares in a trading subsidiary. The doubt relates to whether or not the earn out

proceeds may be attributable to the sale of the shares or rather to the (non exempt) periodic realisation of an intangible asset, being the 'right to receive the earn out proceeds'. Revenue has not yet responded to the 'expression of doubt' (but its published guidelines require it do so within a reasonable time.) Should tax exemption not be available, the tax payable on the earnout proceeds receivable in 2007 is projected to be in the region of **€525K.** Preliminary tax for 2007 is being calculated and will be paid on the prudent basis that exemption may not be available.

Sale of a Visa Card book to AIB in 2005
Under the sale agreement, AIB is entitled to a refund of part of the sale proceeds of €2.5m, based on the number of cardholders who migrate to MBNA post sale. Tax rules required the full amount to be brought into charge upfront in 2005, without taking any account of a potential refund. There is provision for repayment of tax (at the 20% rate) on any proceeds given back. It is anticipated that EBS may need to refund some €100k before the end of 2007 and if this proves to be the case, **a tax credit of €20k** will become available.

[redacted] Oireachtas-P

[redacted] Oireachtas-P

[redacted] Oireachtas-P

Costs incurred by EBS in connection with establishing Haven Mortgages

These costs will be deductible in EBS only to the extent that they can be attributed to reorganising its procedures and making itself ready for the purposes of providing future services to Haven (estimated at €2m net). It is intended that all other costs (EBS share estimated at €6-7m) will be invoiced to Haven. There is provision in legislation for allowing a tax deduction to a company which incurs non capital type costs prior to commencement of trading, for such amounts as would be deductible if it had incurred the costs after date of commencement. The relevant legislation appears to envisage that the costs in question would have been directly incurred by the company concerned in its pre-trading period but this is not made explicit and there is a reasonable case for claiming a deduction provided the relevant costs have been re-billed to that company before it actually commences to trade. However for 2007 any tax value may be obtained by EBS only by way of group relief from Haven and as the two companies will have a 'corresponding accounting period' in 2007 of approximately two weeks only, no value has been recognised.

VAT Recovery

During the year, EBS has submitted two separate claims for recovery of VAT incurred by it on bought in goods and services. One claim is based on a provision that permits normally VAT exempt traders, such as financial institutions, to recover a proportion of their input VAT costs, based on the percentage of total income which is generated from non EU sources. EBS generates a modest amount of non EU income in its Treasury function. The other claim relates to VAT inputs attributable to its staff canteen, which following a late 2005 decision of the European Court of Justice, are now partially recoverable.

The combined value of the claims submitted was in the region of €**650k**. (A 2007 claim for partial recovery, when formulated, may add another 170k) However Revenue is strenuously resisting the methodology used in formulating the partial recovery claim and has not yet responded to the second so at this stage it is not possible to estimate what amount will ultimately be recovered. It has been assumed that there will not be any recovery in 2007.

Finance Report to the
Board Audit and Compliance Committee

Critical Accounting Policies and Judgemental matters
Update for the year-ended 31 December 2007

As of 22 February 2008

Introduction

In preparing the financial statements the directors are required to:

- Select suitable accounting policies and apply them consistently; and
- Make judgements and estimates that are reasonable and prudent.

The purpose of this paper is to provide you with an update on those critical accounting policies, judgements and estimates that were considered by the BACC in November 2007. The original paper is attached as Appendix I and only key changes are commented on below:

- **Loan Impairment Provision**

  At the half-year aggregate provisions amounted to €20.6m with a budgeted increase of €1.5m for H2. In addition, we guided in November 2007 that a further impairment charge of up to [redacted]

  Following detailed assessments led by the businesses in conjunction with Risk, and the Credit Committee's review of these, [redacted]

  [redacted]

  Setting aside [redacted] the remaining balance sheet impairment provision has increased by €1.5m in H2. This increase is driven by the following factors:

  i. A prudential increase in specific provisions of €0.6m to cover a small number of problem loans in commercial.
  ii. An increase in the collective pool of €0.5m to cover development finance which reflects the developments in the construction sector and a more challenging economic environment.
  iii. An increase in the collective pool provision of circa €0.5m for legacy loans which have stopped charging offset by a reduction of €0.2m for unauthorised overdrawn balances.
  iv. [redacted]

  Based on experience to date, we have held our endowment provision constant at €5.0m as there have been no material changes to the assumptions underpinning this provision.

In summary, excluding [redacted] impairment provisioning level has increased from 12.3bps of customer advances in 2006 to 13.7bps in 2007.

- **Pensions**

Our pension assumptions have been updated based on recommendations from Mercers.

In summary the key changes are to the discount rate (this has been increased from 4.7% to 5.5% reflect prevailing corporate bond rates at year end) and to the future expected asset returns (increased to 7% reflecting increased government risk free rate returns). All other assumptions, such as inflation and mortality tables, are in line with the prior year.

The pension charge in the Income Statement amounted to €4m which is higher than the original charge of €3m estimated by Mercers for 2007. The increase is due to the death in service premiums (for 2006, 2007 and 2008) that were paid in 2007 to bring the premiums up to date with Irish Life.

The deficit in the current year is €2.3m compared to €8.1m in 2007 and takes into consideration the employer contributions paid in 2007 (for 2006 and 2007) as well as the increase in the actuarial gains due to the improvement of the discount rate offset by the reduction in asset values over the year.

The net surplus or deficit across the 4 schemes for 2007 and 2006 is as follows:

	2007 €m	**2006 €m**
EBS Staff scheme	0.6	3.8
EBS Managers scheme	6.7	7.9
EBS Senior Managers scheme	(5.4)	(4.1)
EBS Ex- NIBS scheme	0.4	0.5
Total	**2.3**	**8.1**

- **Haven set up costs**

Total Haven set up costs incurred by both EBS and Britannia Building Society ('BBS') amounted to €13.2m. These costs comprised internal and external time, computer equipment, furniture and fittings and operational costs.

BBS incurred €4.6m of this spend and the remaining €8.6m was incurred by the EBS group as outlined below.

Haven recognised €5.6m in its accounts, €4.2m of which was capitalised and is being amortised over a period of 4 to 10 years depending of the type of asset. €1.4m was written off to the income statement in Haven in 2007.

EBS recognised €3.0m in setting itself up as a third party service provider. €2.3m of this spend was for external consultants such as PWC, Haplin International and Matheson Ormsby Prentice, €0.5m was for internal time and the remainder was for operational costs.

E&Y have reviewed our intangible assets in detail and are comfortable with our conclusions on the appropriateness of capitalising costs under *IAS 38 Intangible Assets & Goodwill.*

- **IFRS 7 Financial instruments Disclosures ('IFRS 7') & IAS 1 Presentation of Financial Statement (as amended) ('IAS 1')**

We worked with KPMG during Q4, 2007 to prepare the IFRS 7 and IAS1 disclosures to the Accounts. The key changes to note are in relation to credit risk, liquidity risk, interest rate stress testing and capital.

Credit Risk
Further information has been provided under Note 33 to the Accounts in relation to how credit risk is managed in EBS. Specific reference is made to the existence of the credit risk models that are in place, the credit review process, the credit policies and procedures as well as the role of the Credit risk committee.

The credit quality of our book is disclosed by reference to retail and commercial originated loans and it is noted that over 96% of both the retail and commercial loans are performing.

An analysis is also provided of past due, impaired and neither past due nor impaired loans. This highlights that over 92% of our retail loans and 83% of our commercial loans are neither past due nor impaired.

The credit quality of our other treasury related assets is disclosed by reference to counterparty rating and the vast majority of these assets are rated A1 or higher.

Liquidity Risk
In relation to liquidity risk, which is also included under Note 33, additional information has been provided as to how this is managed in EBS. The maturity mismatch approach is explained together with the management of liquidity ratios and the role of the Asset & Liability Committee ('ALCO').

Albeit that the actual maturity mismatch approach is prepared using 'expected' maturities IFRS 7 requires only that the 'contractual' maturities of our financial liabilities be disclosed. This is provided for both the Group and the Society, however it is questionable as to the added value this provides to the reader of the accounts.

Interest rate stress testing
The analysis provided in respect of stress testing shows the present value that would be realised on an accrual basis on the banking and reserve investment books over the life of the assets within those categories.

Capital
An analysis of our capital position is now disclosed under Note 37. This details the components of Tier 1 and Tier 2 capital together with the related capital ratios at the end of 2007 of 9% and 11.9%.

- **Reclassifications**

Some reclassifications were made to the 2006 Accounts to aid comparison with other lenders and to reflect more appropriately the nature of certain transactions. The main area of reclassification involves amounts previously disclosed within Deposit by credit institutions which have been re-allocated to Debt securities in issue. In addition, the non recourse funding issued by the Society in relation to the securitisation transactions has been reclassified from Loans and advances to customers to Customer accounts in the Society's balance sheet. Neither reclassification has any impact on the Income Statement and the latter reclassification only impact the Society balance sheet.

- **Property Valuations**

Property valuations were carried out by our valuers Quinn Agnew and valuations increased from €46.9 to €47.7m in line with our expectations.

- **Provisions**

The following changes arose compared to that agreed at the November BACC meeting:

Exit provisions

A provision of €3.0m was charged in the Accounts in respect of 30 planned exits which are budgeted to take place by the end of H1 2008. As a result, our year end provision amounts to €3.7m which covers the 30 planned exits together with an additional 5 named persons identified during 2007.

AIB profit claw bank

The deferred income from the sale of the AIB credit card book of €0.4m has not been recognised in the Accounts in 2007 as the calculation of the attrition rate on the book sold has not been finalised with AIB. This will be completed during 2008.

Insurance Loss provision

The insurance loss provision of €1m has been retained to cover any claims that may become payable in relation to uninsured lives. [redacted]

Finance Loss provision

The finance provision has increased from €0.6m to €1.6m mainly to cover commissions outstanding from Hibernian which are currently at €1.9m. At a recent meeting of the Finance Directors of both organisations Hibernian indicated that they have not concluded whether they owe EBS these commissions given the fact that the relationship was formally terminated in 2006. Hibernian have committed to revert to us by the end of February 2008 however we believe it is prudent at this time to provide for the majority of the amount outstanding.

Term Extension provision

A provision of €1m was made in 2007 for the SWAT team approved by the Board to address the term extensions issue. Circa €500k of this provision is to cover the contractor costs for new hires and the remainder is to cover potential write offs of loans that may arise as a result of EBS pro-actively addressing this matter with our members.

- **Taxation matters**

Critical Accounting policies

An additional policy has been included under our critical accounting policies in the current year to reflect the judgemental nature of some of our taxes. In summary it outlines that the final tax outcome may differ to the amounts recorded. However, in our opinion the judgements made are appropriate and the provisions adequate to cover the likely liability.

[redacted]

Sale of shares in EBS Asset Managers

As a protective measure, we had 'expressed doubt' on the tax treatment of the earn out proceeds when filing the Society's 2006 tax return. The Inspector has indicated that he wants to have a meeting with us to discuss it but this has not yet been arranged.

Haven set up costs

We have calculated that for tax purposes, of the €5.6m expended on the setting up of Haven, some €3.6m should be tax deductible in Haven over a period of years and a further €1.4m should qualify for capital allowances. Tax rules will prevent the surrender of these expenses (but not the capital allowances) to EBS by way of group relief so the tax value for the greater part of this expenditure will not be available until Haven becomes profitable.
Of the related costs incurred by EBS in establishing itself as a service provider to Haven, some €2.5m has been treated as tax deductible in 2007 and an additional amount of €1.4m is being treated as qualifying for capital allowances over an 8 year period.

Appendix I

THEME: B1

Effectiveness of banks’ board governance, client relationships and business models

LINE OF INQUIRY: B1c

Quality of business model setting process

MINUTES OF BOARD MEETING OF EBS BUILDING SOCIETY

HELD AT 10:00 ON FRIDAY, 31 MAY 2002.

PRESENT:

Brian Joyce (Chairman); Ron Bolger; John Cullen; Ted McGovern; Michael Moroney; Yvonne Scannell; Joe Ryan (Secretary); Ethna Tinney; Noel Windle.

MINUTES:

Minutes of the meeting held on 26 April 2002 were agreed and signed.

COMMERCIAL PROPERTY LOANS:

In attendance: Joan Barron, Brian Healy

[redacted] ***loan of Stg£5.84 million:***
Approved on the terms and conditions set out in paragraphs 6 and 7 of the report.

[redacted] ***- loan of €1.3 million:***
Approved on the terms and conditions set out in paragraph 6 of the report.

COMMERCIAL PROPERTY PRESENTATION:

(a) Update on Performance and Outlook
(b) Credit Policy

In attendance: Joan Barron, Brian Healy

(a) Update on Performance and Outlook
Brian Healy made a presentation dealing with current performance in the Commercial Property Business area and the outlook for the future.

The principal points covered were as follows:

The Strategic Plan

- Conclusions of SWOT analysis
- Market opportunities considered
- Rationale for introduction of Development Finance
- Risk factors in Development Finance
- Two approaches for Development Finance
  - 'Go for Broke' or
  - 'Toe in the Water'

  The Toe in the Water approach is the favoured one
- Summary of five year targets in the plan for each sector:
  - Residential Investments
  - Commercial Investments
  - Owner managed business
  - UK lending, and
  - Development finance.

(Contd.)

COMMERCIAL PROPERTY PRESENTATION (Contd.):

(a) Update on Performance and Outlook
(b) Credit Policy

In attendance: Joan Barron, Brian Healy

Commercial Property Market

- Annualised total returns over period 1990 to date (peaked at 38.2% in 1998, now down just below zero)
- Quarterly returns by sector (offices, retail, industrial) 1998 to date
- Yields by sector
- Dublin office market - availability of space is principally in third generation suburban developments
- Table showing, in square metres, market size, takeup in 2001, year end availability, vacancy rate, amount under construction and proportion prelet or presold.

Commercial Lending Market

- Estimate of market size (in the sectors which EBS is interested) is €23 billion
- EBS has 2%/3% marketshare
- Comparison between EBS and First Active - gross commercial advances in 2001: EBS €164 million, First Active €439 million, including significant UK and development finance lending
- Comparison of EBS and First Active portfolio, by sector.

Year to Date Performance in 2002

- Total advances year-to-date is €75.1 million (€49.6 million in same period 2001)
- However, budget variance is €26.6 million adverse
- Activity in the investment property area is down on last year (not surprising in view of negative returns) but activity in RIPs area has more than doubled
- 'Pipeline model' chart used to highlight additional business needed in each sector to meet the budgeted level of advances
- Chart showing portfolio mix, by sector
- Asset quality remains high - no serious problem cases in large exposures, low level of arrears.
- Significant progress on issues identified in the course of preparing the Strategic Plan, but some areas are "still to do"
- Staffing structure has been re-organised to improve the focus on new business development.

(b) Credit Policy

Brian Healy referred to the draft Credit Policy document for Commercial Property Business, which had been previously circulated. In the presentation, he showed the results of an analysis of recent approvals for "fit" with the proposed policy, which indicated:

- 94% of cases meet the interest cover multiples **(Contd.)**

COMMERCIAL PROPERTY PRESENTATION (Contd.):

(a) Update on Performance and Outlook

(b) Credit Policy

In attendance: Joan Barron, Brian Healy

- 76% of cases are within the LTV guideline
- 60% of cases meet both criteria
- 73% of cases meet either the two main criteria or they are cases where the net worth of the customer is high.

In view of the fact that Commercial Property cases are examined individually, it is not possible to come up with a policy to cover all good cases; in the circumstances, Management is of the view that the proposed policy is in line with our current practice and is workable.

The Board discussed the presentation and the policy document. The proposed Credit Policy was approved, subject to the addition of "Health and Safety issues" in the items to which consideration is given in the development finance policy.

It was suggested that, with a view to widening the base of Commercial Property customers, a greater level of business networking will be needed in the future; in this respect, Brian Healy will contact individual Board members to establish whether they have contacts who may be a source of additional business.

[redacted]

Updated EBS Strategic Review

and

Plan for 2004 – 2008

November 2003

Joe Ryan

19 December 2003.

Copy: Joe Ryan

3.2 Summary Financial Information

Full financial detail is provided in Appendix B of this document. The following tables provide an overview of some of the key figures:

Profit and Loss

Profits grow on average by 13% p.a. from 2002 to 2004 and by 25% p.a. thereafter. The increased growth rate from 2005 onwards is driven by high levels of lending and tightly managing the growth in operational costs to 5% p.a.

EBS Summary Profit & Loss Account							
(Amounts in €m's)	2002 €m's	2003 €m's	2004 €m's	2005 €m's	2006 €m's	2007 €m's	2008 €m's
Total Operating Income	124.7	135.0	151.2	171.5	201.1	230.6	267.4
Total Operating Costs	(66.3)	(71.3)	(79.5)	(83.6)	(87.8)	(92.4)	(97.2)
Provision for bad and doubtful debts	(4.0)	(1.1)	(2.4)	(2.4)	(3.2)	(3.7)	(3.9)
Profit or (loss) on ordinary activities before tax	54.4	62.5	69.2	85.5	110.1	134.5	166.4
Growth in Surplus %	20%	15%	11%	24%	29%	22%	24%

Stripping out exceptional Change Programme costs provides a truer picture of the underlying profitability of the business.

Profit & Loss less Exceptional Strategic Plan Costs (Incl. in Operating Costs)

EBS Summary Profit and Loss Account (Less Strategic Costs)							
(Amounts in €m's)	2002 €m's	2003 €m's	2004 €m's	2005 €m's	2006 €m's	2007 €m's	2008 €m's
Profit or (loss) ordinary activities before tax	54.4	62.5	69.2	85.5	110.1	134.5	166.4
Exceptional Change Programme Costs	5.6	6.1	7.8	5.4	5.4	5.4	5.4
Profit or (loss) on ordinary activities before tax (Incl	60.0	68.6	77.0	90.9	115.5	139.9	171.8
Growth in Surplus %	32%	14%	12%	18%	27%	21%	23%

Note: There are further exceptional costs relating to Nova which are not shown here as they are not considered part of our ordinary business or organic Change activities, these costs are highlighted in Appendix B – Section 2

EBS Building Society

Minutes of Board meeting held on Friday 22 July 2005 (Strategic review)

Present:	Brian Joyce (chair), Ron Bolger, Cathal Magee*, Ted McGovern, Alan Merriman, Mark Moran, Michael Moroney, Tony Moroney, Barbara Patton, Joe Ryan (secretary), Ethna Tinney
Apology:	Yvonne Scannell
In Attendance:	Emer Finnan (secretary designate), Mike Freedman (Kepner Tregoe)

[redacted]

Section 3: Key Business Drivers Behind the Plan

Inputs Presentation:

- Macro economic assumptions 2005 – 2010: continued strong performance forecast over the next five years; gradual increase in interest rates over this period (ECB at 3% by 2008).
- Mortgage market assumptions: national book growth to be 23% this year, reducing to 11.1% in 2008; refinance and equity release markets to grow over the period.
- Growth in EBS residential mortgage lending expected to exceed market growth in the period to 2008, through a combination of an increase in EBS outlets, re-mortgages to existing savings members along with the development of the broker and credit union channels. These will result in the EBS share of national residential mortgage balances rising from 12.2% at present to 14.6% in 2008.
- Tracker mortgages will account for an increasing proportion of business – rising from 5% today to 60% by 2008. This will push mortgage margins down.
- Savings market will be distorted in 2006/2007 by maturing SSIA accounts. A comprehensive action plan on capturing maturing SSIA accounts is being developed.
- As regards investments and protection, sales projections have been developed in conjunction with our prospective bancassurance partners; the number of product sales is expected to double by 2008 – most of the increase being in the non mortgage related area.
- The commercial property market size is expected to remain fairly static over the planning period. EBS currently has a small market share (2.5%) and plans to more than double this (to 6.3%) by a combination of –
  - doubling the size of the sales team,
  - increasing our risk appetite, in particular development finance, and
  - entering new business areas such as property fund manufacture and funding, and pension loans.
- Combining the above plans will result in growth in EBS membership (from 385k to 468k) and in product holdings per member (from 1.7 to 2.12).
- Key factors contributing to the growth will be –
  - Investments being made in sales capability;
  - Expanded distribution network;
  - Partnerships with proven players.

Discussion:

In the discussion on the presentation up to this point, the key themes covered were:

- The ability of EBS to grow faster than the market; the development of new channels (brokers, credit unions), will be key to this. Also, re-configuring the business around *relationships with our members*. We estimate that 80k of our (savings) members have mortgages from other financial institutions.
- While EBS will be targeting the mortgage customers of other financial institutions, our competitors will be targeting our book. Our pricing policy (i.e. absence of higher pricing on the back book) should assist us in defending our book; the experience of the UK's Nationwide Building Society, which has a pricing policy similar to ours, is that retention is better than average.

EBS Commercial
Business Plan from 2005 to 2008

26th September 2005

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EBS Commercial – The story so far...

•**2001/2005 Strategic Plan – Commercial Business**

•An era which has seen the business more than triple in scale to c €660m this year & a loan book of €1.6 billion

•Still very much in the mould of lower risk lenders, so our asset quality is good but our margins are low. Given our 100% capital weighting, this positioning presents a particular problem for us going forward, in times where capital is becoming scarce.

•**2005 Strategic review process**

•A number of work shops held to date – emphasis on determining our driving force going forward

•Identified a need to re-think our current numbers in the plan to include:-

•An acceptable solution to the low Return on Capital in our current business, while recognising the reality of down ward margin pressure in the market.

•Strike a better balance between the new higher risk businesses & the overall commercial book.

EBS BUILDING SOCIETY

We have considered 4 alternatives going forward.

"Rocket" Strategy

- High Growth strategy enabled by doubling team capacity (to 73).
- Growing new high margin business in development lending
- Grow our existing business lines also, by following the downward pressure also.

"Hold" Strategy

- Modest growth strategy restricted to existing team capacity.
- No major shift in current business mix.
- Downward pressure on margins continue.

"Lean & Mean" Strategy

- Restrictive strategy due to the high capital usage of commercial.
- Downsizing the team.
- Get out of all low margin business (below 1.75%) and focus on squeezing more out of a smaller volume / book.
- Moving into the INBS space.

"Step Up" strategy

- Growth strategy broadly linked to the pace of EBS growth.
- New skills needed but fewer than in the Rocket strategy.
- Grow high margin business in development finance,
- Low emphasis on growing current business lines which have low ROC.

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How do these options measure up in scale & ROC?

Strategic option	Order of magnitude in 2008	ROIC	Comments
"Rocket Strategy" **73 people**	Gross Lending - €1.68m Book Size - €4.1b **PBT €25.3m**	**12.9%** **13.8% on new business**	•6 more lending teams •High Execution risk due to reliance on new people/ teams. •Capital availability an issue
"Hold Strategy" **36 people**	Gross Lending - €870m Book Size - €3.0b **PBT - €18.2m**	**12.1%** **12.6% on new business**	•Safest route as we already have this infa-structure. However limited possibilities for dynamic change.
"Lean & Mean Strategy" **29 People**	Gross Lending - €525m Book Size - €1.9b **PBT - €14.4m**	**14.4%** **16% on new business**	•Good ROC but smaller scale & a lot of lost customers. •Exclusively concentrating on high risk business.
"Step Up Strategy" **60 people**	Gross Lending - €1.18m Book Size - €3.6b **PBT - €23M**	**13.5%** **On new business 15%**	•3 more lending teams •Good return on capital •Can evolve into any other of the alternatives as circumstances allow.

EBS BUILDING SOCIETY

2006: Organising to deliver the step up strategy

Head of Commercial

- Direct & Brokers Channels
  - Direct Business
    - •Two man team
  - Broker Business
    - •Two man team
- Development Finance
  - Specialist team
    - •Four man team
- Specialist Syndicate Unit
  - Specialist team
    - •Two man team
- EBS Network Support units
  - Dublin 1 — •3 man team
  - Dublin 2 — •3 man team
  - Dublin 3 — •3 man team
  - Cork — •3 man team
  - Galway — •3 man team

•8 new lenders needed to make the model work & this includes specialist expertise in Development Finance.

•3 back office staff needed in Operations to maintain service / risk management

•Volume of €850m (+28% on 2005)

•Fees €2.2m (+83% on 2005)

EBS BUILDING SOCIETY

Step Up Strategy – Financials 2005 - 2008

Volume Movements	2005 €M	2006 €M	2007 €M	2008 €M
Gross Lending	660	850	1,000	1,180
Growth %	+25%	+29%	+18%	+18%
Portfolio Scale	1,600	2,200	3,100	4,300

Contribution	€M	€M	€M	€M
Margin Income	13.8	17.7	23.9	31.0
Arrangement Fees	1.4	2.2	3.1	4.3
Total Direct Costs	(4.5)	(6.2)	(7.3)	(8.9)
Provisions / Write-offs	(1.3)	(1.9)	(2.5)	(3.3)
Net Contribution	**9.4**	**11.8**	**17.1**	**23.1**
	+25%	**+26%**	**+46%**	**+34%**

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How does this plan compare with first draft of submission?

Original Plan

	2006	2007	2008
Net Contribution	16.5	23.2	31.8

Revised Plan

Net Contribution	11.8	17.1	23.1

Differences reconciled as

Increased Transfer Price to Treasury for external capital	(1.4)	(1.9)	(2.4)
Costs from Operations / Rent	(0.7)	(0.8)	(1.1)
Total Internal Adjustments	(2.1)	(2.7)	(3.5)

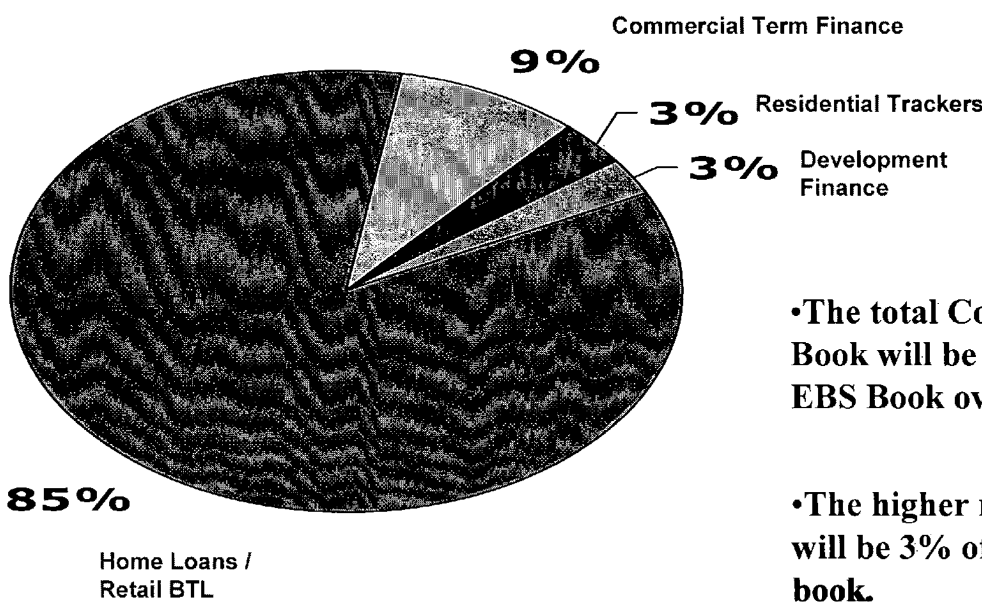
Re-pricing the tracker margin assumptions	(1.0)	(1.4)	(1.9)
Changes in Commercial Income assumptions	(0.2)	(0.3)	(0.5)
Lower Fee Income	(1.0)	(1.2)	(1.3)
Additional Cost assumptions	(0.4)	(0.5)	(1.5)
Total Lost from new or corrected assumptions	(2.6)	(3.4)	(5.2)

Mostly bad debt provision

EBS BUILDING SOCIETY

Risk Profile for EBS

EBS Loan Book in 2008 = €23.6 Billion



- **The total Commercial Book will be 15% of the EBS Book overall.**
- **The higher risk lending will be 3% of the overall book.**

To Conclude - Questions for the Board

•Do you agree with the strategy of maintaining a sense of proportionality between Commercial & rest of EBS i.e the "Step Up" strategy?

•Do you agree with the strategy of building member value by substantially increasing PBT (rather than a narrow focus on ROCE)?

•Do you agree with the expansion of the risk appetite needed to support growth?

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Broker Market Entry

Board Update

21/01/05

Introduction & Background

At the December '03 Board Meeting a presentation outlining the significance of the Broker market for the residential mortgage business and the ways in which EBS could enter this market was delivered.

The principle points of that presentation were:

- Mortgage brokers are now an integral and growing distribution channel in the Irish mortgage market and are estimated to account for 35% of new mortgages.
- EBS could enter the Broker market and achieve a market share of 11% within 5 years.
- Issues around cross selling and membership could necessitate "ring-fencing" the operation under a separate subsidiary and brand.
- Nova discussions could present opportunities for the Broker business and therefore should be concluded before finalising plans.

Rationale for entering the Broker market

There is a clear rationale for entering the Broker market:

- Brokers now account for 40% of the mortgage market. In other mature markets they have increased this market share to typically account for upwards of 60%
- Our competitors leveraged this channel to great effect to complement their owned network channels in 2004.
  - PTSB Broker unit accounted for €2.71bn (61%) of cheques issued
  - Ulster Bank Broker unit accounted for €1.3bn (48%) of cheques issued
- Mortgage brokers now represent so great a proportion of new business, it is a significant disadvantage for lenders to dismiss them as a distribution channel
- Mortgage brokers:
  - provide lenders with an alternative to fixed cost branch networks and a low cost means to replace closed outlets.
  - provide lenders with an opportunity to broaden their market reach and acquire new customers
  - depend on commission for their livelihood and as such are a highly incentivised sales force.

EBS BUILDING SOCIETY

Broker Project

- Kieran Tansey hired to setup and lead the Broker business
- Consultation with the Network commenced in June
- Arising from the protracted nature of Nova discussions a Steering Committee was formed September 1st 2004. The committee members are:
  - Ted McGovern
  - John Flanagan (project sponsor)
  - Tony Moroney
  - Neil Copland
  - Tom Doherty
  - Dara Deering.
- Project resources were allocated on a full-time basis to facilitate speed to market.
- Recruitment commenced in September – 10 experienced resources recruited to date.
- The project adopted the working title of: abc mortgages

Guiding Principles

A number of guiding principles were established upfront:

- ABC Mortgages must not compromise the EBS brand in any way.
- EBS Credit Policy will apply to ABC Mortgages (this may need to be modified to reflect the ABC Mortgages business objectives and will be addressed at the February Board meeting)
- ABC commits to being open, honest and transparent in its dealings with appointed Brokers and the EBS owned network
- ABC will offer a comparable mortgage product set to EBS – although certain rates will differ.
- The integrity of client information supplied by a Broker to ABC will be protected. EBS will not use this information to cross-sell its products. EBS will maintain a normal member relationship and the right to cross sell to an existing member who subsequently decides to purchase an ABC product.

Vision

To become the clear supplier of choice to the mortgage intermediary market in Ireland.

Strategies to achieve our vision

- Partner with selected large intermediaries to develop a mutually beneficial and enduring business relationship
- Set new industry standards in speed and quality for mortgage fulfilment through automation and e-enablement.
- Hire people with a "can-do" attitude operating within a culture of innovation and entrepreneurship
- Leverage strategic alliances/partner arrangements to maintain competitive advantage through innovation in the marketplace

Vision (translated into) business volumes

New Lending Targets (€m)	2004	2005	2006	2007	2008	2009
Strategic Plan '03	300	405	547	738	1,004	-
Revised Plan '05	-	500	810	1,094	1,476	2,008
% of Broker market		7%	11%	14%	17%	23%

Financial Overview

A positive contribution is forecast in Year 2 of operations.

Broker ABC Mortgages							
Contribution Statement							
Amounts - €m's		**2005**	**2006**	**2007**	**2008**	**2009**	**2010**
Volumes	*Opening Balance*	0.0	500.0	1,272.5	2,271.1	3,576.7	5,316.5
	New Lending	500.0	810.0	1,094.0	1,476.0	2,008.0	2,200.0
	Redemptions	0.0	37.5	95.4	170.3	268.3	300.0
	Closing Balance	500.0	1,272.5	2,271.1	3,576.7	5,316.5	7,216.5
Revenue	*Interest Income*	1.8	6.4	12.8	21.2	32.2	45.4
Total Revenue		**1.8**	**6.4**	**12.8**	**21.2**	**32.2**	**45.4**
Direct Costs (Commission, MIG, Staff, Admin, IT, Marketing)							
Total Direct Costs		**-3.8**	**-5.3**	**-7.6**	**-10.7**	**-14.9**	**-16.2**
Marginal Contribution		**-2.0**	**1.1**	**5.2**	**10.5**	**17.4**	**29.2**
Establishment Costs							
(Rent)		0.3	0.3	0.3	0.3	0.3	0.3
Contribution after Burlington Rd rent		**-2.3**	**0.8**	**4.9**	**10.2**	**17.1**	**28.9**

Business Solution - Overview of key deliverables

- Company formation – legal advice on establishment of non-member subsidiary received
- Regulatory approval – IFSRA have been briefed on 2 occasions, positive reaction received on both occasions – formal submission by 31st Jan.
- Risk – Amendments to credit policy proposed, presentation at February Board meeting
- Compliance & Governance – PWC engaged to provide recommendations
- Business Planning – Finance model developed and included in '05 budget process
- Business Process Development – Broker processes mapped and procedures in development
- Finance Process – Reviewed and approved by E&Y and communicated to IFSRA
- Mortgage Brain selected as preferred technology solution – system development complete and currently in test
- Brand – A brand for the new subsidiary has been developed with Broker involvement
- Recruitment – At an advanced stage, appropriate training in progress
- Location – Interim location setup on 4th floor
- Broker Selection – Process developed for Broker appointment, c.70 identified for appointment
- Broker Training – 171 Brokers/staff have attended Level 1 training
- Communication – Ongoing programme with Network, Head Office staff & identified **Brokers**

EBS BUILDING SOCIETY

Branding – Design Brief

A design brief was developed to facilitate the development of the Broker branding. The following guidelines were issued.

- ABC is the intermediary arm of EBS Building Society. It is being established to allow the Society to compete on equal terms in the highly competitive and commercial mortgage intermediary market.
- ABC is a separate Company, but is an integral part of the EBS Group. The values of the two organisations are inextricably linked. The cross impact must be understood and managed.
- Whilst ABC is being established to service and grow non-member business, which has not previously been available to the Society, everything it does is ultimately intended to support and benefit EBS members.
- Our Desired Market Positioning is around:
  - ***Differentiation*** through the quality of our ***relationships*** and our ***service*** to Mortgage Intermediaries, whom we will create a unique and special relationship with. This relationship will be at the centre or our thinking and decisions in a spirit of genuine ***partnership***.

EBS BUILDING SOCIETY

Timetable & Next Steps

#	Action Item	Timeframe
1	**Establish a subsidiary for operating in the Broker business with associated memo and articles of association**	January
2	Incorporate company	January
3	Proposal submitted to IFSRA for regulatory approval	January
4	Proposed Credit Policy/Risk modifications to be reviewed by Board	February
5	User Acceptance Testing completed	February
6	Finalise Broker selection	March
7	Recruitment completed	March
8	Soft launch – pilot with 3 Brokers	March
9	Go-Live – bring remaining Brokers with Mortgage Brain	March

* Board approval sought

EBS BUILDING SOCIETY

EBS Building Society Board Nominations Committee

Minutes of Meeting held on 19 February 2009

Present:	Fergus Murphy, Liam Mulvihill (Chair), Mark Moran Philip Williamson (by telephone). **In attendance:** Fidelma Clarke (Secretary)
Minutes & Matters Arising	The minutes of the previous meeting were approved. Matters arising were evaluated.
AGM – Correspondence with Financial Regulator	The correspondence between the Society and the Financial Regulator relating to a proposal to extend the date by which an AGM would be held from end April 2009 to end May 2009 was noted.
Combined Code – directors serving more than a six year term	It was noted that under the Combined Code for Corporate Governance, the appointment of non executive directors for a term beyond six years should be subject to particularly rigorous review, and should take into account the need for progressive refreshing of the Board. (Code Provision A.7.2). It was resolved that a rigorous review be undertaken for the two non executive directors retiring by rotation after a six year period, namely, Mark Moran and Barbara Patton. The review will encompass, *inter alia*, board and individual performance assessments and attendance and contribution at Board and Board subcommittee meetings. Following this evaluation, the candidates may be invited to meet with the chairman of the Nominations Committee or attend a Committee meeting. It was agreed that Mark Moran will absent himself from the evaluation of his performance by the Committee. **Action** A detailed evaluation of the non executive directors retiring by rotation will be undertaken at the next Committee meeting.
Executive and Non-Executive Director Nominations	The increasingly negative external media coverage in relation to the banking sector in Ireland and the dynamic nature of the political environment in recent weeks was noted. Against this background, the issues of accountability and credibility were discussed. The Committee agreed that the primary objective must be the to ensure that an appropriate Board was in place to best shepherd the Society through these challenging times and into the medium term. This required an evaluation of the appropriate board size, balance between non-executive and executive directors and skills and capabilities of board members both individually and collectively. The Committee deliberated at length on each of the directors (executive and non executive) retiring by rotation, and the candidacy of the director standing for election for the first time, Fergus Murphy. In relation to board size, the committee agreed that it would be preferable to have a smaller board, and that with the appointment of two additional directors on 1 January 2009 in connection with the Government Guarantee scheme, a board of 14 members was larger than optimal. It was agreed that the Committee would recommend to the Board that it would be preferable to reduce the board size over time, starting with a reduction from 14 board members to 13.

Contd.\... **Executive and Non-Executive Director Nominations**	The make-up of the board in terms of executive and non-executive members was evaluated. Fergus Murphy confirmed that as CEO he was willing to put himself forward for nomination, and the committee approved the nomination for recommendation to the Board. Tony Moroney's candidacy was evaluated. The Committee discussed at some length the prospects for the Society's subsidiary Haven. New business sourcing will be significantly curtailed as a result of the international credit crunch, and new business activity in Haven – a non member business – will be severely restricted vis-à-vis original plans. On this basis, it was agreed that the role of CEO of Haven no longer warranted representation at Board level, and that therefore Tony Moroney would not be invited to stand for a second term. Alan Merriman's candidacy was evaluated. The Committee was mindful of the losses which will be reported as a result of the Society's commercial property development exposures and discussed the issue of accountability and the perception of accountability by external stakeholders. Cognisant of Alan's role over the preceding three years as Finance Director, Executive with responsibility for Commercial Business and Chief Risk Officer it was agreed that in the interests of the Society Alan would not be invited to stand for election as a director for a second term. It was agreed that Fergus Murphy would hold discussions with Tony and Alan and update the Committee at its next meeting. The Committee also evaluated the non-executive director's candidacy. It was noted that Barbara Patton was willing to serve a third term as non executive director. On foot of these deliberations the Committee agreed that, at this time, its recommendation to the Board would be that the number of seats be reduced to thirteen, that the CEO be put forward as a candidate, bringing the agreed number of candidates to four (including the three external candidates). The candidacy of the other non executive directors will be assessed following the detailed reviews, scheduled for 26 February. The timing of the conclusion of Nominations Committee deliberations was discussed. It was agreed that the Committee would not be in a position to make a final recommendation to the Board on 27 February, one day after the next Nominations Committee meeting. It was agreed that a final recommendation would be made before the publication of the Annual Report & Accounts at a specially convened Board meeting if necessary.
	Signed: [signature] **Date:** 4-11-10

THEME: B1

Effectiveness of banks' board governance, client relationships and business models

LINE OF INQUIRY: B1d

Adequacy of board oversight over internal controls to ensure risk is properly identified, managed and monitored

3(c)

Proposal to establish a Board Credit Approval Committee

1. We need to focus the board meetings more on strategic discussion – dealing with loan approvals, however large, is not really strategic.

2. Our commercial property customers expect decisions at very short notice: that is what they get with most of our competitors. Often the amounts involved in individual loans are small, but our rules requiring total connected exposure to determine the approval level mean that a small loan may require board approval. (Our treatment of total connected exposure is logical, and we are not suggesting it should be changed.)

3. The use of emailed reports and telephone decisions has worked well up to now: the response from board members has generally been prompt. However it needs to be recognised that this process gives individual directors little say in the decision; it is difficult for one director with reservations about a case to air and discuss these reservations. As we move from five to eight non-executive directors, the use of telephone decisions becomes more problematical: it is going to take longer for management to get the views of all board members, and the ability of individual directors to express serious doubts about a case is further diluted.

4. Other small credit institutions (but not the larger ones) involve the board in credit decisions – typically IR£10m (say €13m) upwards. We are not therefore suggesting that credit decisions be handled entirely outside the Board.

5. Our proposal is as follows:

   (a) A board sub-committee would have the authority to approve loans where the connected exposure is up to 10% of our shareholders funds (c. €30m).

   (b) Membership of the sub-committee would be determined by the Board: our initial proposal is that membership would comprise four non-executives and the three executive directors.

   (c) Sub-committee meetings may be called at short notice; except in exceptional circumstances, there would be at least 24 hours notice. All sub-committee members who can be readily contacted will be invited, but the meeting can proceed provided a quorum of at least three directors (of which at least two are non-executives) is present.

   (d) As is the practice with board decisions, "telephone decisions" may be sought where necessary. In these circumstances, we would endeavour to contact all sub-committee members. If there is a consensus to proceed with the credit among those contacted, and if they form a quorum, the case will be minuted as approved.

   (e) In general, reports for consideration by this sub-committee will be tabled at the meeting, although, if possible, they will also be emailed in advance; however, management will not be *required* to issue reports in advance.

   (f) Minutes of decisions taken by this sub-committee will be circulated for noting by the Board.

Joe Ryan
11 February 2003

Joe Ryan

25 April 2003.

4

Board Report

Circulated on: 22 April 2003

The establishment of a Board Credit Approval Committee – to handle credits up to 10% of our shareholders' funds (c. €33m) – was approved in principle by the Board on 14 February 2003, and confirmed at the meeting on 28 February. Proposed formal Terms of Reference for this committee – which are along the lines considered by the Board at the meeting on 14 February – are set out below, for approval.

Joe Ryan

Joe Ryan

Board Credit Approval Committee Terms of Reference

1. Composition and functioning

1.1 The Board Credit Approval Committee ("the Committee") is a sub-committee of the Board, consisting of at least five directors, appointed by the Board.

1.2 The Board shall periodically review the membership of the Committee.

1.3 The Board shall appoint the chair of the Committee.

1.4 A quorum shall consist of three directors, of which at least two are non-executives.

1.5 The Secretary of the Society shall be the secretary of the Committee.

1.6 The Committee shall meet as required. Meetings may be called at short notice; except in exceptional circumstances, there would be at least 24 hours notice. All Committee members who can be readily contacted will be invited, but the meeting can proceed provided a quorum is present.

1.7 "Telephone decisions" may be sought where necessary. In these circumstances, management will endeavour to contact all Committee members. If there is a consensus to proceed with the credit among those contacted, and if they form a quorum, the case will be minuted as approved.

1.8 In general, reports for consideration by this sub-committee will be tabled at the meeting, although, if possible, they will also be emailed in advance; however, management will not be *required* to issue reports in advance.

1.9 Minutes of the Committee shall be circulated to all board members.

2. Duties

The Committee shall have the authority to approve loans where the connected exposure is up to 10% of the Society's shareholders funds, as shown in the most recent audited accounts.

3(c)

Proposal to establish a Board Credit Approval Committee

1. We need to focus the board meetings more on strategic discussion – dealing with loan approvals, however large, is not really strategic.

2. Our commercial property customers expect decisions at very short notice: that is what they get with most of our competitors. Often the amounts involved in individual loans are small, but our rules requiring total connected exposure to determine the approval level mean that a small loan may require board approval. (Our treatment of total connected exposure is logical, and we are not suggesting it should be changed.)

3. The use of emailed reports and telephone decisions has worked well up to now: the response from board members has generally been prompt. However it needs to be recognised that this process gives individual directors little say in the decision; it is difficult for one director with reservations about a case to air and discuss these reservations. As we move from five to eight non-executive directors, the use of telephone decisions becomes more problematical: it is going to take longer for management to get the views of all board members, and the ability of individual directors to express serious doubts about a case is further diluted.

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   (a) A board sub-committee would have the authority to approve loans where the connected exposure is up to 10% of our shareholders funds (c. €30m).

   (b) Membership of the sub-committee would be determined by the Board: our initial proposal is that membership would comprise four non-executives and the three executive directors.

   (c) Sub-committee meetings may be called at short notice; except in exceptional circumstances, there would be at least 24 hours notice. All sub-committee members who can be readily contacted will be invited, but the meeting can proceed provided a quorum of at least three directors (of which at least two are non-executives) is present.

   (d) As is the practice with board decisions, "telephone decisions" may be sought where necessary. In these circumstances, we would endeavour to contact all sub-committee members. If there is a consensus to proceed with the credit among those contacted, and if they form a quorum, the case will be minuted as approved.

   (e) In general, reports for consideration by this sub-committee will be tabled at the meeting, although, if possible, they will also be emailed in advance; however, management will not be *required* to issue reports in advance.

   (f) Minutes of decisions taken by this sub-committee will be circulated for noting by the Board.

Joe Ryan
11 February 2003

Joe Ryan

Board Report

Circulated on: 22 September 2003.

26 September 2003.

4

Delegation arrangements – Commercial Property Lending Establishment of a Business Unit "Credit Forum" within EBS Commercial.

This memorandum seeks approval of the Board to:

(i) Delegate a connected exposure approval limit of €1.0m for a new committee based decision vehicle known as the "Commercial Credit Forum" which will operate within the Commercial Business Unit. This is required to offer an alternative decision making vehicle to the Head of Commercial Business delegated authority (also €1m).

(ii) Increase the approval limits of the Executive Committee and the Credit Committee to €7.5m and €5m respectively. This is required to streamline our decision making process for some of our larger credits.

(i) Establishment of the Commercial Credit Forum

One of the strengths of our approval process for larger loans are very flexible committee structures, from Credit Committee up to the Board Credit Approval Committee. However for cases lower down in the approval process, we have a weakness in that we still depend on the availability of ***named individuals*** to be the sole executor of the delegated approval limits. This can create bottlenecks in the process, especially during times of absence or limited availability of those people.

We are recommending a shift towards a committee based decision process for all exposures up to €1m (i.e those that are handled by the Commercial Business Unit). A table outlining how this arrangement will look is given in the attached Appendix. Effectively the Credit Forum will become the underwriting vehicle for the Commercial business, and will take over from the individual delegated limits mentioned above (we feel it wise to nonetheless maintain the individual limits also in case of need).

Advantages of the Commercial Credit Forum

1. Faster decisions for the exposures up to €1.0m.
2. Strengthening of the control environment, as ensures more than one person involved in the underwriting decision.
3. Better sense of participation and involvement from staff in the Commercial business unit, particularly for trainee lenders who can sit in on the meeting.
4. Can be expanded to be the decision vehicle for a range of other issues, from pricing to negotiation of terms and also minor procedural matters.
5. Consensus based decisions rather than unilateral decisions (the latter often perceived in the network as very "personality" based).

We recommend the changes as outlined above. It should be noted that for the past year the Commercial Business Unit has been operating a version of the Credit Forum and it has worked very well. Internal audit have highlighted that we need to have this arrangement agreed by the Board, and this paper will regularise this.

(ii) Increase in the Credit Committee and Executive Committee limits

We are also recommending an increase in the approval limits of the credit Committee to €5m, and the Executive Committee to €7.5m.

In the event that this new arrangement is approved, I summarise the new delegated arrangements for Commercial Business as follows:-

The current delegated limits operational for Commercial Loans are:-

	Previous Approved Limits	New Approval Limits	
	€ M	€M	
Board Credit Approval Committee	10% of EBS Reserves.	No Change	
Executive Committee	5.0	7.5	(Up €2.5m)
Credit Committee	3.0	5.0	(up €2.0m)
One Executive Director	1.5	No Change	
Head of EBS Commercial / Commercial Credit Forum	1.0	No Change to limit. Limit shared with Commercial Credit Forum	
Senior Manager – EBS Commercial	0.75	No Change*	
Designated Manager – EBS Commercial	0.50	No Change*	

* These are individual limits which still stand. However in practice the Credit Forum (which will usually include these individuals) will take over the underwriting of the cases falling into this criteria.

The increase in the Executive and Credit Committee limits is requested to match our flexibility to deliver fast decisions (an ever growing differentiator and service measure) with the growth in deal sizes generally in the Commercial market.

Brian Healy
Head of EBS Commercial

Alan Merriman

26/01/2006 08:39

To: brianjoyce@eircom.net, ron.bolger@ely.ie, mlmoroney@eircom.net, barbarapatton@eircom.net, scannell@iol.ie, mmoran@materprivate.ie, tinneye@rte.ie, Tony Moroney/HO/IEEBS@IEEBS, Alan Merriman/HO/IEEBS@IEEBS, Ted McGovern/HO/IEEBS@IEEBS, cmagee@eircom.ie

cc: Emer Finnan/HO/IEEBS@IEEBS, Patricia Brady/HO/IEEBS@IEEBS

Subject: Lending Opportunity for Approval - exception to policy

Dear all,

Please find attached a paper on the lending proposal referred to in my email of earlier this week. If you could revert to Patricia with your decision by noon tomorrow, that would be much appreciated.

If you have any queries, please feel free to contact Brian Healy directly or myself.

CLP260106.doc

Regards,

Alan

Alan Merriman
FINANCE DIRECTOR

EBS Building Society
2 Burlington Road
Phone - 665 9284

Memorandum to: **Board**

Date: **25th January 2006.**

Re: [redacted] & [redacted]
3 loans totalling €54.7m, increasing connected exposure to €88.7m

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I attach a recommendation for approval of three credit applications from existing clients [redacted].

The first of these (Proposal A) involves a credit of €50m for the purpose of financing the retention of an entire block of [redacted] Oireachtas-P at [redacted] by these clients on a long term basis.

The second application (Proposal B) is a committed standby facility of €2m secured on different security (to the security offered for Proposal A) at [redacted]. The purpose of this facility is to provide some assurance of liquidity in respect of the funding of Proposal A, should unforeseen issues arise with servicing interest payments on that debt.

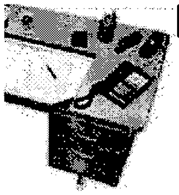
The third application, Proposal C, is for a relatively modest loan of €2.7m to acquire a [redacted] for eventual redevelopment purposes. This proposal is independent of the other two credits.

If we approve all three of these credits our connected exposure to these clients will increase to €88.7m which represents 17.65% of EBS reserves (excluding PIBS) as at 31 December 2005. If approved by the Board, this will be an exception to policy – based on the size of the connection. A more detailed credit report reviewed at Loan Advances Committee is available for any member of the Board to review if required.

In summary, having carefully assessed the merits of the proposals, I am personally supportive and in particular note that the maximum likely loss in a doomsday scenario would be relatively modest in the context of our likely overall profitability.

I would be grateful if you would revert with your views by noon of Friday 27th January. If you have any queries do please call Norman Burns or Brian Healy at 6658026.

Alan Merriman
25.01.06



[redacted]ricia Brady
12/04/2006 14:37

To: brianjoyce@eircom.net, ron.bolger@ely.ie, mlmoroney@eircom.net, cmagee@eircom.ie, mmoran@materprivate.ie, barbarapatton@eircom.net, scannell@iol.ie, tinneye@rte.ie, ted.mcgovern@mail.ebs.ie, mark1.moran@gmail.com, alan.merriman@mail.ebs.ie, Tony Moroney/HO/IEEBS@IEEBS
cc: emer.finnan@mail.ebs.ie
Subject: URGENT - Board decision required

TO: Board of Directors

DATE 12 April 2006.

re: Meeting (by telephone/email) as soon as possible.

I attach a loan report for urgent consideration by the BOARD.

We require an urgent decision on before the Easter break.

So, if you could communicate your decision to me by early afternoon tomorrow that would be great.

If you have any queries contact:

- Joan Boarron 665 9120 OR mobile 087 283 3238)

Regards.

[redacted]tricia..

323.pdf

THEME: B2

Effectiveness of banks' credit strategies and risk management

LINE OF INQUIRY: B2a

Appropriateness of property-related lending strategies and risk appetite

B2a – Appropriateness of Property-Related lending Strategies

and Risk Appetite

Information Summary (Section33AK)

Note: All references are aggregated

Document Category	Time Period
Internal memos	
Correspondence	Q1 – 2008
External consultants reports	

In Q1 2008 the Financial Regulator wrote to EBS detailing its findings and recommendations following its inspection of Commercial Property Lending activities.

This review highlighted 18 Medium Priority Findings and 1 Low Priority Finding. No High Priority findings were made.

EBS was invited to consider the matters raised and to respond to the Financial Regulator setting out follow-up actions and associated timeframe.

Medium Term Priorities

These were listed under the following headings;

1. Credit Policy (3 Findings)
2. Reporting (1)
3. Procedures (3)
4. File Reviews (1)– Issues Arising
5. Arrears and Watch List (2)
6. Security (1)
7. Loan reviews (2)
8. Internal Audit (1)
9. Business Continuity Planning (1)
10. Credit Impairment Policy (3)

1. Credit Policy

The Financial Regulator identified a need to ensure that all amendments to Credit Policy are documented in a timely manner, that there are procedures in place to advise all staff of policy amendments and that the Board and the relevant Board committees comply with the procedures for approving these amendments. The Regulator also identified 10 specific items which it considered should be amended in the Credit Policy.

The Regulator noted a very high level of exceptions (29%) in the previous 11 months and requested EBS to advise whether any steps would be taken to address this. Reporting to Board should include information on the reasons that gave rise to the exception.

2. Reporting

Reporting of Commercial Property Lending Activities to Senior Management and the Board should be more granular, including details of geographic spread, refinancings and redemptions.

3. Procedures

The Regulator identified 8 procedures which it recommended be amended. These related mainly to sign-offs for amendments to Letters of Approval and for cheque-issuance. It also recommended that an approved list of valuers be established for Commercial Lending. The procedure relating to the threshold for credit-checks also needed to be clarified.

4. File Reviews

A long list of queries were identified on files reviewed.

5. Arrears and Watch List

The Regulator recommended that arrears reporting to the Board should distinguish between Commercial and Residential arrears; that the Aged Analysis Report should include details of all arrears and that EBS should have a policy on the capitalisation of arrears.

The Watchlist report as presented to the Credit Risk Committee should include all relevant exposures, not just those over a certain threshold.

6. Security

The Regulator highlighted the number of deeds outstanding for commercial loans (1,123) and the fact that 12.5% of that number were outstanding from the period 1996-2002.

7. Loan Reviews

The Regulator found that loan reviews for Commercial Property loan files had not been done in 2007 due to resources being committed to other projects. They recommended that EBS review its staffing levels to ensure that it was satisfied that loan reviews could be undertaken annually.

8. Internal Audit

The Regulator recommended that Internal Audit should review the Commercial Property lending function more frequently than at present. Last review done 2½ years ago.

9. Business Continuity Planning

Commercial Business Continuity Plan should be amended to include Commercial Underwriting function. Urgent need to test the Disaster Recovery Site as it had not been tested in over a year.

10. Credit Impairment Policy

The Regulator required that the Impairment Provisioning Policy should be reviewed annually and that an internal independent review of the credit risk processes and methodology for determining provisions should be done at least every 2 years in line with regulatory requirements

To Board

From Alan Merriman

Date: 12 January 2009

Re: Development Finance Paper

Attached is an explanatory paper which summarises the origins of our development finance business, the rationale for stepping this up in 2005 and includes management commentary on some of the key questions raised at Board and/or the BRC.

The paper covers aspects such as strategy, risk concentrations, governance, execution, reporting lines, and provisioning reporting.

The paper concludes that mistakes were made within EBS and that these together with a sharp property price correction and wider global dislocation events have left the Society overly exposed to this hard landing.

Risk, strategy and operational mistakes have been made. These include:

- The risk characteristics of the development finance book were not monitored or controlled from a portfolio perspective as effectively as they should have been;
- Higher loan to value levels should not have been permitted as the risk of a market adjustment increased through 2006 and 2007; and
- The Finance Director should not have had the dual reporting responsibility for commercial lending and risk.

The primary responsibility for what has emerged rests within the executive and line management, and this is fully accepted.

Regards,

Alan

Alan Merriman
Finance Director

DEVELOPMENT FINANCE PAPER

DISCUSSION PAPER FOR BOARD CONSIDERATION

1. Origins of EBS involvement in development finance from 2001

Attached, as Appendix I is a summary paper setting out a chronological account of the build up of the Society's circa €500m development finance business.

In summary, whilst the Society's initial move into development finance commenced in 2001, very little business was executed during 2001 and 2002 and it was primarily throughout the 2005 to end-2007 period that a substantial step up in such lending activity was brought about. The table below illustrates this.

	2003 €m	2004 €m	2005 €m	2006 €m	2007 €m	2008[1] €m
Approvals	71	94	148	395	370	136
Advances	13	42	85	197	263	115
Book	23	76	108	257	445	500

Appendix II provides a more detailed quantitative analysis of the build up of the development book - analysed by quarter for 2005 through to 2008.

Step up 2005

The "step up" in development finance followed on from a Society wide strategic review during 2005, which was advocated by management and endorsed by the Board. The 2005 three year plan envisaged growing development finance to 3% of total book or €800m by the end of 2008 and the greater capital capacity this would bring.

The context in which this strategic decision was made was post the failure to execute Project Nova; an environment in which EBS was struggling to compete and grow its member business; and a recognition that EBS needed to transform itself if it were to survive and prosper as an independent mutual. Increasing risk appetite was seen to be a necessary part of such a transformation ....as had been done by others such as First Active; ACC and INBS. This step up move in development finance was determined following an extensive six month strategic review in H1 2005 and was very much seen as a key part of a wider strategy to help EBS survive as an independent mutual post the collapse of merger discussions.

Another key driver of thinking at that time was the recognition that the commercial business was not delivering an adequate return on capital at that time (it was circa 9%) and as a non-member business this needed to be nearer 15%. Achieving this would necessitate moving up the risk curve with development finance being a key component of this.

The main rationale for the 'step up' strategy and specifically a greater proportion of development finance lending was to help deliver:

- Meaningful commercial scale to our commercial lending business to bring about higher profits & returns on capital to support our member business and mutual pricing
- Higher enterprise value for the commercial business with a view to a potential medium term JV or hive down
- Better income diversification and growth in non interest income – which were key Rating agency and Regulator concerns at that time

The "step up" strategy was compared to three others – a "rocket" strategy; a "hold" strategy; and a "lean & mean" strategy. The step up strategy was recommended as being the preferred option of

[1] In April 2008 we took a policy decision to be closed for new commercial business

APPENDIX II

QUANTITATIVE ANALYSIS OF THE BUILD UP OF THE DELVELOPMENT FINANCE BOOK ANALYSED BY QUARTER

Development Finance Loan Book

Annual Figures 2002 to 2005

	31/12/2002	31/12/2003	31/12/2004	31/12/2005	31/12/2006
Approvals	N/A	70.9	94.3	148.3	395
Advances	N/A	12.6	41.5	84.8	196.7
Fee Income	N/A	0.3	1.25	1.2	1.32
Loan Book Size	N/A	23	76.3	107.5	257

2006

	Quarter 1 2006 €M	**Quarter 2 2006€M**	**Quarter 3 2006€M**	**Quarter 4 2006€M**	**Full Year 2006€M**
Approvals	69.7	93.3	101	131	395
Advances	19.2	42.8	51.7	83	196.7
Fee Income	0.15	0.2	0.49	0.48	1.32
Loan Book Size	113	148	183	257	257

2007

	Quarter 1 2007€M	**Quarter 2 2007€M**	**Quarter 3 2007€M**	**Quarter 4 2007€M**	**Full Year 2007€M**
Approvals	142.6	139.1	39.9	48.4	370
Advances	66.8	80.2	67.8	48.5	263.3
Fee Income	0.85	0.875	0.72	0.11	2.555
Loan Book Size	312	377	416	445	445

2008

	Quarter 1 2008€M	**Quarter 2 2008€M**	**Quarter 3 2008€M**	**Quarter 4 2008€M**	**Full Year 2008€M**
Approvals	121.9	8.9	5		135.8
Advances	18.2	85.1	11.3		114.6
Fee Income	0	0.7	0.1		0.8
Loan Book Size	461	480.1			490

The Q 1 2008 approvals uplift is primarily attributable to a single exposure of circa €50m with a LTV of circa 58%

Joe Ryan

Board Report 19 December 2003.

6(b)

Revision of Residential Lending Delegation Arrangements

Circulated : 15 December 2003
By : Sarah Hanratty – *Head of Underwriting & Residential Loan Operations*
Fidelma Clarke – *Head of Credit Policy*
For : **Approval**

1. Introduction

Our residential lending delegation arrangements were last reviewed by the Board in March 2002. Residential business volumes (including retail Buy to Let) have since increased and are set to increase by a further 17% (excluding broker business) in 2004. At this stage in order to maximise the efficiency of the team and improve the service we provide to our members, we propose increasing two of the limits – those which apply to Assistant Managers and Staff Underwriters. The need for higher delegated authority level was borne out in a recent analysis which showed 67% of all home loans needing sign off at either Manager or Senior Manager level.

2. Proposed Changes to Delegated Approval Authority Limits

The following table shows the current limits and proposed limits. We believe that these new limits can be operated safely given that they apply to low and medium risk cases only and to cases within 5% of standard Credit Policy guidelines. In addition, the Credit Policy & Review team analyse the profile of approvals on a monthly basis and report their findings to the Credit Risk Committee and the Board.

Authority level	Current limit €000's	Proposed limit €000's	Change
Credit Committee	5,000	5,000	-
One Executive Director or designated Senior Manager Group member	1,500	1,500	-
Designated Senior Managers	750	750	-
Designated Managers	500	500	-
Designated Assistant Managers	350	**400**	+14%
Designated staff underwriters	200	**250**	+25%

3. Operating Principles

The delegation arrangements approved by the Board relate to the maximum loan size which underwriters at all levels may approve. Within these maximum limits a range of specific restrictions also exist.

..... /

Contd. /...

(i) Designated underwriters
Approval authority for each underwriter is designated on the basis of their experience and changes are effected by recommendation of the relevant Senior Manager Underwriter and the approval of an experienced Executive Director.

(ii) Restrictions for different risk categories
Restrictions on approval limits are enforced in relation to the
- risk classification of the loan
- typical guidelines on affordability, security and debt servicing capability
- Specific circumstances such as self employed cases, guarantor cases, credit histories (bureau search findings), bridging requests, age, employee loans, connected exposure
- Amendments to applications such as changes in loan amount, substitution of security, margin changes and loan term changes.

4. Conclusion
In recent years we have amended delegated approval authority levels as the experience of the underwriting team increases and to allow us to optimise the service we provide for our members. We have seen significant increases in the volume of business over the past six years and our strategic plan involves significant increases in business volumes going forward.

The proposed changes to increase the delegated approval authority ceiling for Assistant Manager and Staff underwriters does not represent an increase in credit risk exposure given the increased experience of the individuals underwriting credits, the designated approval limits operated by the business and the monthly credit review process. In addition, the introduction of credit scoring and decisioning and the automation of Irish Credit Bureau checks from January 2004 will provide additional sophistication and support for the residential credit assessment process in EBS. Providing excellent service for our members is one of the strategic objectives of EBS and this proposed change will support this business requirement.

For all of these reasons we are happy to recommend the changes as outlined above.

EBS
BUILDING SOCIETY

Emer Finnan

24 November 2005.

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To: EBS Board Members
From: Tony Moroney
For : **Approval**
Date: 18 November 2005
Subject: 100% Mortgages : Move from Pilot to Permanent Solution

1. Background

EBS launched a 100% mortgage solution as a pilot on August 16th, five weeks after the launch of the first official 100% offering from First Active subject to:

- Undertaking to review with Board post pilot
- Cap on business of €300m
- MIG cover from GE (at higher prices)
- Specific lending criteria – additional affordability ceiling of 4.5 times multiple
- Ongoing review by Credit & Operational Risk and Credit Risk Committee
- Change to loan sales documentation so that customers acknowledge security exposure

The product was launched on a three month pilot basis. This pilot ended 18th November 2005 and was extended for one week to coincide with this week's Board Meeting.

2. Business Recommendation

2.1 Business at Risk

Since the launch, the 100% Mortgage offering has accounted for 21% of all First Time Buyer approvals equal to €46m. Based on the experience to date, we are forecasting that the business at risk (should EBS not have a 100% solution in the market) would be in the region of €988m over the course of our three year plan. For this reason, we are proposing that we retain a 100% product offering as part of our overall suite of mortgage solutions.

2.2 Improving the Return on Equity

The Return on Equity for 100% product is less than a typical 92% loan. This is primarily driven from higher costs for Mortgage Indemnity Insurance. In order to drive up the ROCE for the 100% product, we considered three options

Option	Consideration	Recommendation
1. Increase Price	Market pricing would make it difficult to charge a higher rate for this product. Most lenders are charging between 3.1% and 3.25% for this product.	Not an Option
2. Reduce Cost (MIG Premiums)	Genworth have indicated that they will not reduce pricing for this cover. We may be able to negotiate some reduction base lending to state guaranteed employment sector; not agreed at this juncture.	Under Negotiation
3. Increase Return (Introduce an Unsecured Deposit Bridging Loan)	We currently offer a Deposit Loan through GE Money. We are proposing offering a Deposit Bridging Product through EBS at a higher rate to increase return on capital There are system implications and therefore we expect delivery in Q2 of 2006.	Recommended Option

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2.3 Financial Impact (ROCE)
Providing a Deposit Loan improves financial return to EBS

ROCE	Core Channels	Broker Channel
Current 100% Product	11.1%	9.9%
100% Product with EBS Deposit Loan	11.8%	10.0%

3. Credit Risk Review [F Clarke]
The Credit Risk Committee unanimously supports the continuation of a 100% mortgage offering subject to a number of conditions as follows :

- Full MIG cover is required on all 100% loans with the right reserved to do exceptions to policy where the loan is approved by the Chief Residential Underwriter or higher approval authority. No other change in delegated authority is required.
- All current criteria in relation to affordability assessment apply, i.e., the debt service ratio limit of 40% (NDI%) and the affordability assessment or 'test' (remaining income to household expenditure test). In addition, a minimum income earnings thresholds of €40k will apply for single applicants (€37k if a Civil Servant or Garda) and €60k for joint applicants.
- There will be no income multiple cap on 100% business; however, all 100% LTV cases will be monitored by Credit Risk and reported to the Credit Risk Committee for review.
- Product applies to FTBs for owner occupier loans only and does not exceed 10% of total owner occupier lending approvals.
- A deposit bridging loan to be offered by EBS as part of the 100% offering to improve ROCE.

In ratifying the business proposal, the Committee took into account the attendant risks, including the increase in credit risk (increase in average LTVs), the recognition of the important of income quality and underwriters' discretion to refuse to approve credits where they feel that this is not the case, and, in the absence of risk based pricing for owner occupier business, some 'cap' on the total amount of business being written at lower ROCEs.

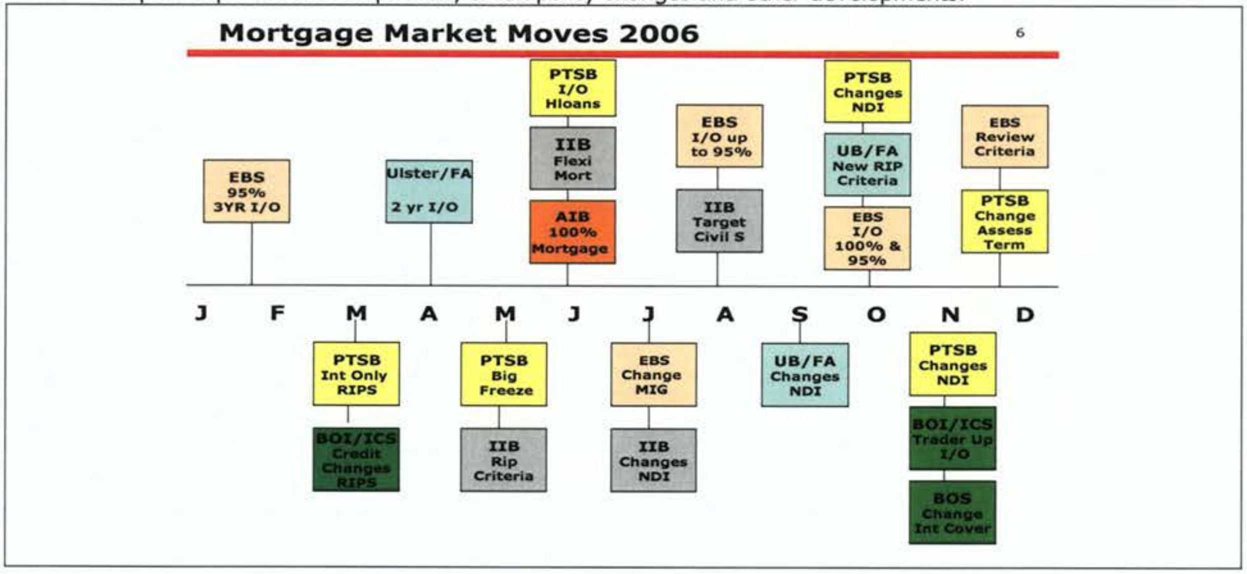
4. Recommendation – for Approval

We are recommending a change in Residential Credit Policy to allow EBS offer 100% mortgage lending to First Time Buyers subject to the conditions outlined above.

This proposal will be considered at the Board on Thursday. Norman Burns, Head of Credit and Fidelma Clarke, Head of Risk will be in attendance.

4.0 Relative Market Positioning

Given the slow down in the market, lenders have responded in order to protect their business volumes. The graph below summarises the number of developments which have taken place over the course of this year which incorporate product developments, credit policy changes and other developments.



I/O – Interest Only Big freeze – Moratorium on repayments NDI – changes in debt service ratio caps

In addition, the level of advertising of special offers has increased substantially, reflecting the marked increase in competitive pressures.

5.0 Individual Policy Changes – Business Rationale

51. Homeloans and associated top up loans

There are five main changes being proposed in relation to Homeloans and their associated Top Up loans.

Proposal	Change	Business Rationale
1. Extend Loan Term Assessment to 35 years where 35 year term selected	**Current Policy** EBS currently assesses over 30 years even if the customer is opting for a 35 year loan term **Proposal** Use actual term of loan for loan assessment [as long as both applicants' ages do not exceed maximum for loan term assessment – see 5 below].	The market reality is that borrowers are borrowing for a longer loan term and we have an anomaly in our assessment. If a borrower is taking a loan over 35 years, then there is no business logic to assess over 30 years. All other lenders with the exception of PTSB assess over the term of the loan BOS/UB & FA offer terms up to 40 years and assess over 35 yrs.
2. Allowable Income **Increase Overtime/Bonus and Commission for Second applicants**	**Current Policy** 50% for 1st applic, 25% for 2nd 100% if 'guaranteed' **Proposal** Increase to 50% for 2nd applicant.	What is being proposed is now standard in the Industry and a reality that in the case of most joint applications, both applicants remain in full time employment
3. Change the Stress Test on Interest Rate **[Proposal revised following detailed review at CRC]**	**Current Policy** Stress test at SVR +2% **Proposal** Use a flat rate of 6% for assessment for 2007. Review quarterly.	This is the most significant change. It has the effect of reducing the stress test we would otherwise have on loans. However, it eliminates the variability of loan assessment (where changes in rates have an immediate impact on the amount EBS would lend) and it builds a 'permanent' stress test of 1% above where we expect rates to end up in March 2007.
4. Extend the Debt service Ratio cap for higher income earners	**Current Policy** Maximum Debt Service Ratio of 40% **Proposal** Introduce higher debt service ratios for higher income earners Income NDI% < €75k 40% < €150k 45% >=€150k 50%	We are turning away or approving by exception good business today due to the DSR cap. Other lenders have changed significantly this year and this move will improve our position, albeit we will not be in the top quartile. However by introducing these bands, we will have a greater opportunity to attract business from higher income earners and gain greater understanding of the profile and needs of these applicants.
5. Change policy on max age to use 70 as standard [current policy is 65 with 70 as upper limit]	**Current Policy** There is an anomaly between practice and policy with underwriters interpreting the maximum age of 70 while policy states 65 as standard with a cap of 70. **Proposal** Formally amend credit policy to allow max age at end of loan to be 70.	The business wishes to formally amend the EBS Credit policy to preserve the offering of loans up to age 70 or maximum term of 35 years (whichever is greater) to stay competitive with most other lenders. To reduce our practice to 65 year maximum age would place us behind all our competitors. As it is, BOS and AIB will lend up to 75 years of age.

Appendix 1 EBS Policy After Changes versus Competitors' Policies Today

	permanent tsb banking only better	First Active / Ulster Bank	ICS	IIB Homeloans	BANK OF SCOTLAND Ireland	AIB Republic of Ireland	EBS AFTER CHANGES
LTV	100% (98% Take 4)	FTB's >92% - 100%	100%	85%	100%	92%	100% 95% as standard
No of Basic Incomes	2	2	2	2	2	2	2
Overtime Bonus Commission	10% 10% 30%	75% n/a 50% over 2 yrs 50% v 50% over 2 yrs 50% v	100% if gtd 25% if reoccurring	10%- 75% 10% - 75% 100% for govt emplys. (5 times up salary scale for one affinity group)	20% of basic 20% non prof 25% prof 50% of basic	15% 15% 15%	100% if guaranteed 50% for 2nd applicant
Lodger Income	Not factored	€320 per month added to net income. (UB) €425 per month added to net income capped at additional loan amt of €22K (FA)	Not factored	Additional loan amount of €25,000	€250 per month net income	Not factored	50% of €7,618 tax free = €3,809 per annum tax free Adds €49.7k to loan amount
DSR/NDI Cap	< 75K: 35% NDI <125K : 40% NDI >125K : 45% NDI Single & Joint Will go to 60% NDI in some cases	Single & Joint <50K 40% NDI >50k 50% NDI	< €35K : 4.5 IM €35K - €60K 4.75 IM >€60K 5 .0 IM	44% DSR	< €75K: 40% <€125K : 45% >€125K : 55%	€25K 30% DSR <€65K 44% DSR >€200K 49% DSR JT: €25K 30% DSR <€65K 39% DSR >€200K 49% DSR	< €75K: 40% DSR < €150K: 45% DSR > €150K : 50%
Stress Test Rate	Base + 2%	Base + 2%	Base Var + 2%	Base + 2% or 3 yr fixed rate	Rate + 2%	Base + 2%	Flat Rate of 6%
Max Term Assessment	30 yrs	40 yrs Assess over 35	35 yrs	35yrs	40 yrs up to age 65 PAYE up to 70 yrs self employed	35 yrs	35 yrs
Remaining Income	NDI No formal RI assessment	NDI No formal RI assessment	S €1,600 J €2,600 Dep €100 each	NDI No RI assessment	S €1,400 J €2,000 No costing for deps	NDI No formal RI assessment	S €1,324 - €4,668 J €1,539 - €4,997 €165, €100

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Board Report

For Approval - Residential Credit Policy Changes
30th November 2007

We are recommending two changes to our Residential Credit Policy which were presented and evaluated at Credit Risk Committee on 23rd November 2007. The first change relates to Stress Testing which was highlighted by the Financial Regulators following their on site review in February. The second change relates to Mortgage Indemnity Insurance for our Member Business which was considered as part of the 3YP Budgeting process. These changes have the support of the Member Business, the Risk Unit and Credit Risk Committee.

Stress Testing

As part of the Financial Regulators on site review in February, they made a recommendation that our Debt Service Ratio (DSR), which measures the proportion of a persons income that they need to allocate to meet their mortgage repayments, be stress tested. Traditionally EBS has fulfilled the stress testing requirements by examining the absolute amount a person has left to live on after meeting their mortgage repayments. This new requirements is in addition to the Financial Regulators requirements that all residential loans (fixed, variable and tracker) be stress tested at ECB + 2.75%.

Our current policy on DSR's includes three bands depending on income, recognising that people on higher incomes can afford higher mortgage repayments. We have completed a significant amount of analysis to determine what the DSR's should be using a stress testing mortgage repayment. Further analysis including competitor analysis is contained in Appendix 1, but in summary we are proposing the following changes

Income Band	Current DSR	Proposed DSR
<€75k	40%	45%
>=€75k<€150k	45%	50%
€150k+	50%	55%

We are also proposing to add a further 5% to the bands for 5 and 10 year fixed rate loans which are not stress testing in EBS today but need to be stress tested using the new requirements from the Financial Regulator

Mortgage Indemnity Insurance

Over the last number of years, we have made a number of changes to the level of Mortgage Indemnity Insurance for our Member Business. We have conducted a further review as part of the 3YP and are recommending the continuation of mortgage insurance in general for our membership business, for the following reasons

- The Business Model: EBS originates mortgage business and retains 'most' of this business on balance sheet. At the same time, a significant amount of our income is derived from the residential mortgage business and therefore it is important that we protect this income stream going forward.
- The views of external stakeholders re mortgage insurance protection : the regulator, the rating agencies and investors
- The protection against concentration risk for our largely mono-line business
- The potential for capital relief under Basel 2
- The investment made in establishing a B2B link with Genworth in systems, processes, and time
- The fact that we had negotiated a profit share rebate and flat pricing for 5 years

While the costs of Mortgage Indemnity Insurance continues to be c€6m per year on a cash flow basis (€1m on a P&L basis for each year of origination due to the fact that the cost is amortised over 6 years), we believe that the benefits outweigh the costs. At a business level, it supports our higher LTV business, in particular 100% lending which if withdrawn or restricted further would eliminate c €165m of mortgage advances in 2008. On a P&L basis, this new business will add c€0.7m to the Member Business profitability in '08 and €1.4m in '09

We are also recommending forgoing mortgage insurance for Affordable Housing loans given the lower than expected risk of this lending segment. Further detailed analysis is outlined in Appendix 2.

Fidelma Clarke, Head of Risk
Dara Deering, Director of Membership Business

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Appendix 1 – Stress Testing Mortgage Applications

1. Analysis – Inclusion of Stress Test in Debt Service Ratio

Analysis was conducted on 50 cases. The analysis carried out looked at the impact separately to the standard variable rate loans and the different approach for 5 and 10 years fixed rates

(a) Inclusion of stress test in Debt Service Ratio for Variable Rate loans :

- Debt Service Ratio increased by 7% on average (Current SVR is 5.25% ; the stress test rate is 6.75%)
- If we leave our policy on Debt service Ratio unchanged, we will not write business tomorrow which we are happy to write today – or our exception levels to policy will substantially increase.

It should be noted that the move to the use of ECB + 2.75% positively impacts the results of individual affordability tests for variable rate business, as the stress tested rate is reducing from 7.25% to 6.75%.
This should lower exceptions to the affordability test ; approximately 75% of exceptions in September were due to affordability.

(b) Inclusion of stress test in Debt Service Ratio for 5 and 10 Year Fixed Rate loans :

- The Debt Service Ratio increased by 7% on average (varying slightly depending on Product & rate)

It should be noted that the move to the use of ECB + 2.75% negatively impacts the results of individual affordability tests for fixed rate business by 12% on average, following the introduction of the use of the fixed rate itself, rather than a stress tested rate, in affordability calculations in Q2 2007. The current 5 year fixed is 5.33% against a stressed ECB rate of 6.75%.

2. Competitor Analysis

IIB have changed their policies to reflect the new stress test by increased the Debt Service Ratio Bands for different income earners. UlsterBank / First Active have introduced a higher Debt Service Ratio for 5 year fixed rate business.
AIB has not yet announced any changes, nor has PTSB. Bank of Ireland / ICS uses income multiples as a policy which are not impacted by interest rate stress tests.

4. Recommendation on Change in Debt Service Ratio Bands

We are recommending a change in our debt service bands to reflect the introduction of a stress test in the DSR calculation. The proposed change is 5% across the board. Where customers chose to fix for 5 or more years, we recommend a higher DSR to reflect the reduced interest rate risk. The table below shows the impact of the proposed changes against current competitor policies. In debt service ratio terms, these changes put EBS's risk appetite as 1st for incomes below €50k, joint 2nd (behind IIB) with Ulster/First Active for incomes up to €100k and 1st again with Ulster First Active and IIB for incomes above €100k.

DSR Rates per Income band

Variable

	AIB	BOI/ ICS	BOS/ Halifax	EBS Before	EBS After	First Active	IIB	PTSB	UB
<=€50k	30%	Use income multiples	40%	40%	**45%**	40%	45%	35%	40%
<=€60k	44%		40%	40%	**45%**	45%	50%	35%	45%
<=€70k	44%		40%	40%	**45%**	45%	50%	35%	45%
<=€75k	44%		40%	40%	**45%**	45%	50%	35%	45%
<=€100k	48%		45%	45%	**50%**	50%	50%	40%	50%
<=€125k	48%		45%	45%	**50%**	50%	50%	40%	50%
<=€150k	49%		55%	45%	**50%**	55%	50%	45%	55%
€150k+	48%		65%	45%	**55%**	55%	50%	45%	55%

Fixed

	AIB	BOI /ICS	BOS/ Halifax	EBS Before	EBS After	First Active	IIB	PTSB	UB
<=€50k	30%	Use income multiples	40%	40%	**50%**	45%	45%	35%	45%
<=€60k	44%		40%	40%	**50%**	50%	50%	35%	50%
<=€70k	44%		40%	40%	**50%**	50%	50%	35%	50%
<=€75k	44%		40%	40%	**50%**	50%	50%	35%	50%
<=€100k	48%		45%	45%	**55%**	55%	50%	40%	55%
<=€125k	49%		45%	45%	**55%**	55%	50%	40%	55%
<=€150k	48%		55%	45%	**55%**	60%	50%	45%	60%
€150k+	49%		65%	45%	**60%**	60%	50%	45%	60%

It is important to highlight that EBS relies more on the detailed individual affordability tests which it conducts for each application for loan assessment purposes than on the blanket DSR bands. For this reason, we are satisfied that the proposed changes do not, of themselves, present a higher risk appetite than the credit risk appetite we have today.

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Appendix 2 – Mortgage Indemnity Insurance

1. Estimated Costs 3YP

MIG premiums increase with the increase in risk profile. However, with recent increases in interest rates and the moderation experienced in the mortgages market coupled with EBS's tightening of its 100% offering it is expected that the risk profile of EBS borrowers will remain relatively unchanged for the next three years (average loan to values on new loans may in fact decrease in the changing market). Therefore we expect MIG costs to rise modestly from **€5.8m to €6.3m over the 3YP,** the timing of which coincides with our current contract with Genworth – our mortgage insurance provider. This compares against a projection of €15.5m for 2008 alone (including broker business) which was forecast in April 2006 when we last concluded a comprehensive review of insurance.

MIG Costs	2008 €k	2009 €k	2010 €k
Owner Occupier	5,523	5,840	6,011
BTL	314	314	314
Total Cost	5,836	6,154	6,324
% Growth	2.5%	5.4%	2.8%

2. Credit Risk Considerations

EBS conducted a comprehensive review of mortgage insurance options, and a detailed cost / benefit analysis in 2002/3 – when RSA, our previous mortgage insurance provider existed the market, and again in 2005/6 when the initial 3 year contract with Genworth had expired. The Board approved the reduction in MIG cover for owner occupier business following its own consideration of the risk issues, but the maintenance of mortgage insurance in the market.

3. Developments since 2006

A number of developments have taken place since April 2006, all of which increase the 'benefit' case for mortgage insurance protection; these include

- the reduction in insurance cover for Buy to Let in line with owner occupier in June 2007 ;
- the offer of 100% mortgages on the back of having mortagge insurance in place ;
- the increased credit risks in the market associated with falling house prices and slowing jobs growth and quality ;
- the Financial Regulator's formal recognition of mortgage insurance in its CRD Implementation Guidance published in December 2006 ;
- The views of investors, rating agencies and the Regulator in relation to the deteriorating Irish mortgage property market – exacerbated by the recent credit repricing and liquidity crunch, and not helped by the recent cases of apparent large scale fraud by two solicitors and the implications of this for collateral security in Ireland.

On any of these core credit considerations, the case for maintaining mortgage insurance is if anything stronger now than it was 18 months ago when last reviewed by management and the Board. The medium term economic outlook is positive. Mortgage insurance is disaster insurance however, to protect EBS in the event of the unexpected happening – not the expected. MI protects EBS against the risk of two events occurring simultaneously, i.e., unemployment increases and nominal house prices falls. We have already seen a real fall in house price growth in 2007 and some pockets of unemployment emerging.

4. Affordable housing loans

In August 2005, EBS launched Home Access, our mortgage product for affordable housing customers. This launch followed two years work with the Department of Environment to agree an appropriate solution and mortgage ranking structure. At the time, the DOE were not in a position to provide any real insight into the type of applicant that would be eligible for an affordable housing solution. On this basis, we believed it prudent to MIG this business, and agreed a separate contract with Genworth. The cost of mortgage insurance for affordable housing loans is higher than standard loans due to the fact that the local authorities discount ranks second to our original mortgage.

We have conducted a review of the profile of the applications for Affordable Housing Loans. The average loan to value is 67%, considerable lower than expected and affordability is very positive in all cases. Based on our assessment and the lower risk nature of these loans, we propose removing mortgage indemnity insurance for all new affordable housing loans. Cost saving to EBS is c €0.4m on a cash flow basis.

Provision Estimates Nov 2008

BUDGET FY 2008 *[AIMED TO MINIMISE : WORST CASE ENVISAGED WAS €15M FOR YEAR]*

	CHARGE €	BPS	BOOK €	BOOK PROV €	BOOK BPS
H1 2008	5.0 M	3	16.2 BN	41.9 M	26
H2 2008	5.0 M	3			
Full Year Charge	**10.0 M**	**6**	**17.0 BN**	**46.9 M**	**28**

CURRENT PROVISON ESTIMATES FY 2008 *[AS AT END OCT : 4 MONTHS TO ACCOUNTS SIGNOFF]*

	CHARGE €	BPS	BOOK €	BOOK PROV €	BOOK BPS
H1 2008	5.0 M		16.2 BN	41.9 M	
H2 2008 (Curr Forecast)	85.0 M				
Full Year Charge	**90.0 M**	**529**	**17.0 BN**	**126.9 M**	**746**

OUTLOOK FOR 2009

Full Year Charge	**35.0 M**	**218**

- EBS taking the pain up front.
- **AIB**
- forecasting charge of 75 bps for group for 2008 and 90-110 bps for group for 2009 (forecast was 60-80 bps for 2009 at the half year) : they claim that long run average is 35 bps
- AIB forecast Ireland : 4 bps for personal house mortgages, 140 bps for remainder of book (€700m in total)
- Charge for residential development in Ireland = 300 bps in 2008, and 490 bps in 2009

REASONS FOR CHANGE

(a) Commercial Property values deterioration – in particular development land banks

- Deterioration in outlook for commercial property values.
- In particular, very material reduction in asset values for incomplete developments / land banks.
- Original LTV spread for development cases we are now providing for was 62% - 87% : Average around 75%. We are seeing property values falling by between 30 and 40% here – so 15% 'in red'.
- Cannot recover by selling land banks – with or without planning. Cannot improve situation by disposing of other property assets ; market is illiquid.
- Speed of deterioration markedly increased in Q3 2008 ; unprecedented / unanticipated
- EBS not alone ; very significant changes in provisions / impairment outlooks published by other institutions since half year
    - e.g. AIB 40 bps at half year ; forecast 75 bps for 2008 and 90-110 bps (for group) for 2009. Irish development (residential) forecast to be 300 bps for 2008, 480 bps for 2009.

(b) Significant investment in time and resources to evaluate extent of commercial exposures

- Over past 8 weeks over €1.6 BN or 2/3rds of Commercial loan book has been reviewed by Business / Credit on an obligor by obligor basis
- Commercial loan book is small enough to review ; 400 'material' obligors (> €1m) and 900 smaller obligors (<€1m).
- Development Finance book comprises 75 obligors : all are reviewed quarterly

WHY DID WE GET INTO DEVELOPMENT FINANCE ?

- Focus from 2006 was to increase return on equity of commercial lending (c. 10% in 2006) including a drive for high levels of non-interest income through fees
- Led to increased risk appetite for higher rewards
- Development finance experts recruited : (Martha Widger etc) and team put in place
- Credit increased from 3 to 6 individuals 2007
- Strong approval oversight : all cases with connections> €5m went to LAC. Of 15 development cases were are proposing to make a significant provision for now, 10 were approved by BCAP, 4 by LAC.

BREAKDOWN OF PROVISIONS ESIMATE FOR 2008 AS AT 5 NOVEMBER - €90M ON NEXT PAGE

Provision Estimates Nov 2008

Component	Amount €M	Comments
H1 Charge	**5**	• Commercial individual cases circa €7 [redacted] • €3m release in retail endowment provision
Retail Individual Cases	**2.5**	• All cases falling into this category reviewed at high level in October. Very small number of cases
Retail Pool Provisions	**10**	• Mathematical model used for this. 42% reduction in prices peak to trough built into model • Change in prediction now incorporates a number of things including ➔ Deterioration in property prices which impacts LDG calcs ➔ Higher probability of default model calcs based on economic outlook ➔ New Loss Given Default Model – better predictor ➔ Increased cost of recovery (more collections activity) ➔ More prudent assumptions on what will result in case being repossessed – future proofing
Commercial Individual Cases	**43**	[redacted]
[redacted]	**5**	
Commercial Pool Provisions	**9**	• Mathematical model predicts this requirement. We have made loss assumptions for the different categories of loans (Term debt, Commercial Buy to Let and Development) and for the different risk grade profiles (i.e. loss rate estimates increase the higher (worse) the grade.
[redacted]	**15**	[redacted]

RESIDENTIAL MORTGAGE MARKET & EBS CREDIT RISK APPETITE

30th May 2008

Dara Deering
Director Member Business

Fidelma Clarke
Head of Risk

EBS BUILDING SOCIETY

Approved / Recommended Changes – Membership Business

No	Segment	Change	Comment
1	FTB	Maintain but restrict further 100% lending	**Requires Board approval.** Only 3 institutions offering this product. EBS volumes modest. MIG in place in all cases.
2	FTB	Extend max term to 40 years from 35	**Requires Board approval**. Brings EBS in line with competitors. Max age limit of 70 applies.
3	FTB	Extend interest only to 3 years for self build	In line with other interest-only offerings
4	STB	Increase reserve facility to €50k from €30k and LTV cap from 75% to 85%	Low take up on reserve facility. More for marketing purposes.
5	Existing members	Interest only available for high earners, top ups on BTL and 4 x 3 month period over life of loan	To support retention of good business
6	Existing members	Relax approval rules for top up loans up to €30k where LTV at 70%	Low risk cases. Cannot take out more than 2 and requires good payment history
7	FTB	Formalise approach to allowing parents be co-borrowers from tax and assessment perspective	Formalises approach, and ensures EBS meets it tax policy requirements.

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Conclusions & Takeaways

Credit risks are increasing

- Strength of employment, components of income ↑
- Affordability – tax rates →
- Affordability – interest rates → (until end 08)
- Security collateral ↑
- Willingness to pay considerations ↑
- Availability & Cost of Credit ↑
- Asset Quality Outlook ↑
- Views of Financial Regulator ↑
- Views of rating agencies ↑
- Views of external commentators ↑

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and we are monitoring credit risk trends closely

- We monitor residential credit risk appetite in a number of ways
  - External Economic Assessment → [Reviews by Economic Experts eg ESRI]
  - Mortgage Market Outlook → [EBS specific review by Jim Power]
  - Internal Credit Risk Trends → [Independent reports from CRCU]
  - Capital requirements → [Monitored by Capital Committee]
  - Competitive landscape → [Monitored by Credit Risk Committee]
  - Business Volume Objectives → [Agreed by Management Team]
  - Network Feedback / insight → [Credit Engagement Council]
  - Credit Risk Mitigants → [Monitored by Credit Risk Committee]
  - Asset Quality → [Monitored by Credit Risk Committee]

In addition, we furnish the Board with key credit risk indicators in the detailed management activity report for each meeting.

EBS BUILDING SOCIETY

In conclusion …

- The Irish Economy, Housing and Mortgage Markets have gone through a period of significant growth and are now going through a period of readjustment
- EBS has experienced strong growth through this period and now has a residential mortgage book of c €14.3bn
- Our approach has been reasonably prudent, particularly in respect of the Buy to Let segment and all high LTV lending has MIG in place.
- We expect to see growth return to the housing sector in 2009 albeit at more modest levels and for affordability to continue to improve for new buyers
- The member business will continue focus on its core customer segments and will continue to MIG high LTV lending.
- Maintaining some higher risk products is placing a heavier burden on our Retail credit underwriting team, and continued network engagement is key to operating in a difficult market in a difficult year.
- We are not complacent about the deterioration in asset quality evidenced to date : approval has been given to appoint an external task force lead (contact basis) to support the credit team in tackling higher arrears levels now in evidence.
- We will continue to monitor and report on credit risk trends to the Board

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TABLED

EBS
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To: Board Risk Committee
From: Brian Healy – EBS Commercial
Supported by : Credit Risk Committee
Recommended by : Management Risk Board

Procedure for exceptions to key guidelines – development finance.

The attached note is a procedure to assist the Commercial Underwriting team to implement the delegated approval limits in relation to our development finance lending.

In our development finance policy we have a reference to situations where cases which are outside of our guidelines must be referred upwards to the next level of authority for approval. At our discussions with the Management Risk Board, a suggestion was made that we should document a procedure which clarifies the key criteria which would trigger a decision for an escalation of the case to a higher approval authority.

Given that development finance is a higher risk business, this suggestion has merit, as it ensures that cases which are outside of key risk criteria, are being considered by our most experienced people.

Our development policy has a large number of guidelines, and it will not be feasible to adopt a literal interpretation of all of the criteria for the purposes of implementing the escalation concept. However we have drafted a procedure which shall be implemented by Commercial Underwriting and Loan Advances Committee which identifies three key guidelines which are such that we would wish for the escalation concept to be in place.

This procedure is attached.

We are recommending this procedure be adopted as soon as the new development finance policy is approved.

Brian Healy
15 November 2006

Procedure for implementation of delegation arrangements for our development finance policy..

All development lending is subject to the delegated approval limits detailed by the Board Risk Committee from time to time.

Given the higher risk profile of development lending, there are some exceptions to the delegated lending arrangements as it applies to development lending. These are detailed below:-

Key Guidelines	**The following exceptions to guidelines (if they are sanctioned) are outside of the normal delegation arrangements for loan approvals.**
Cases where the Loan to Value on the site finance exceeds the maximum range of 80% (incl. roll up and capitalised fees).	➢ All such cases that normally are considered by levels below Loan Advances Committee must be referred upwards to the next highest approval authority. ➢ Loan Advances Committee cases however, need not be referred upwards. ➢ Minimum approval authority level shall be Chief Commercial Underwriter for these development finance cases which are outside of LTV guidelines.
Developments Under Licence proposals.	➢ All such development under licence cases (or similar structured land deals) must be referred to the next highest approval authority. ➢ Minimum approval authority shall be Chief Commercial Underwriter.
Proposals involving an unproven developer at the scale of project / borrowings being contemplated.	➢ All such cases that normally are considered by levels below Loan Advances Committee must be referred upwards to the next highest approval authority. ➢ Loan Advances Committee cases however, need not be referred upwards.

Minutes of Board Risk Committee Meeting on 16 January 2006 (Cont'd.)

	Joe Kerrane left the meeting. ***Brian Healy and Fidelma Clarke joined the meeting.***
Commercial Property Lending:	A self assessment process has been completed on commercial property lending and 29 risks were identified, one of which was external. There are 6 risks that are considered high in nature: • Concentration risks on large exposures which could provide a bad debts exposure or large redemptions • Making losses due to bad lending decisions • Failure to deliver on ambitious margin growth. Plan is to increase margins with declining pressure in market • Risk appetite not aligned between key decision makers and plan • Need for further Development Finance expertise. • Loosing key people.

In terms of these risks the planned actions are as follows:

RISK	ACTION
Concentration risk	• Review large exposure policy • Revise sector policy guidelines
Risk appetite alignment	• Communication/education process on impact of development finance
Loss of key staff	• Recruit outside expertise in development finance • Broaden team depth
Bad lending decisions	• Expand risk grading model • Review and clarify arrears management procedures • Skills review of underwriting • Enhance reporting on loan quality
Failure to deliver ambitious margins	• Develop a capital policy • Develop risk adjusted ROC • Enhance reporting on margin and use of capital
Develop further expertise	• Better and more frequent communication • Workshops

It was noted that the risk control self assessment process has developed and is signed off by the head of function and the Management Board member responsible.

A question was asked around connected exposures. The Central Bank definition is a party which could have a financial effect on another party. EBS is currently considering this definition from its own management perspective.

A point was made that may need to look at the risk management process as it is lengthy and we should just focus on key risks.

/..............

Minutes of Board Risk Committee Meeting on 16 January 2006 (Cont'd.)

Commercial Property Lending (Contd):	A question was posed as to whether we look outside of our business at other organisations and it was felt that by recruiting people we do. Deeds tracking was discussed and a risk approach is being taken on this issue. On the commercial side we ensure we take security before cheque issuance. A status update will be provided to the BRC in March.

[redacted]

EBS Response to Category 16

Category 16

"Board approved exceptions to credit policy for commercial real estate and residential real estate loans – number and aggregate amount for the period 2001 to 2008. If necessary and if not otherwise identified in existing documents, please create a document containing this information."

EBS Response

The aggregate number of loans that were approved by the Board as exceptions to credit policy for commercial real estate and residential real estate loans for the period 2001 to 2008 was 171, including 22 loans denominated in GBP£.

The aggregate amount of loans that were approved by the Board as exceptions to credit policy for commercial real estate and residential real estate loans was €1,209,636,597 and £118,725,000.

EBS Response to Category 18

Category 18

"Any other exceptions to credit policy in respect of any loan that was subsequently acquired by National Asset Management Agency, whether the exception required board approval or not – number and aggregate amount for the period 2001 to 2008."

EBS Response

The aggregate number of loans that were approved as exceptions to credit policy and subsequently acquired by National Asset Management Agency for the period 2001 to 2008 was 57.

The aggregate amount of loans that were approved as exceptions to credit policy and subsequently acquired by National Asset Management Agency was €444,818,000, representing 55 loans denominated in EURO, and £6,134,000, representing 2 loans denominated in GBP£.

THEME: B2

Effectiveness of banks' credit strategies and risk management

LINE OF INQUIRY: B2C

Analysis of risk concentration in the base, the adverse economic scenarios and the impact on capital structure

Emer Finnan
(copy - for information)
BRC 16 November 2006.

EBS
BUILDING SOCIETY

To: Board Risk Committee
From: Brian Healy – EBS Commercial
Supported by : Credit Risk Committee
Recommended by : Management Risk Board

Changes to Large Lending Exposures Policy

I attach a policy document which is being recommended for approval by the Board Risk Committee. This policy was considered in detail at the Credit Risk Committee at its October meeting, and subsequently evaluated by the Management Risk Board.

This revised policy is substantially more risk sensitive than the current policy in aligning the level of exposure which EBS is satisfied to hold for a single obligor (client) or group of connected obligors to the risk rating of that obligor (or group of obligors).

The benchmark limit is based on General Reserves (Core Tier 1 capital) which is more prudent than the current limit set by the Central Bank in its 1995 guidance[1] which uses Own Funds (Tier 1 and Tier 2 capital) as its basis. The proposed approach sets limits on a tiered basis in line with the risk grade of the obligor, with an upper limit of 25% of General Reserves for lowest risk obligors (grade 1) and a lowest limit of 6.5% for highest risk grades (grade 5).

Approval of the policy is recommended.

Brian Healy
10 November 2006

[1] Licensing and Supervisory Requirements and Standards for Credit Institutions (1995)

EBS Building Society

Large Lending Exposures Policy

November 2006

1. BASIS OF LIMITS

Under IFSRA Licensing and Supervisory Requirements and Standards for Credit Institutions (1995), institutions may not incur an exposure to 'a client or group of connected clients' the value of which exceeds 25% of 'Own Funds', generally Tier 1 and Tier 2 capital which includes subordinated debt and PIBS and both on and off balance sheet commitments.

On the basis of these Regulatory requirements, our maximum limit on a "connected" basis would have been €194m as at December 2005.

Rather than use Own Funds as the basis of limit setting for large lending exposures, EBS adopts a more prudent approach of using General Reserves as its basis which is a core, but not exclusive, element of Tier 1 capital and which excludes all Tier 2 type capital (such as subordinated debt). EBS believes that this is the most appropriate benchmark to use as it is a relatively stable figure and one which is predominantly our "core profit".

2. INDIVIDUAL OBLIGOR LIMITS

Each distinct borrowing entity (comprising one or more parties to a loan) is regarded as an Obligor. All loans issued or approved and committed to the same borrowing entity are combined to ascertain the exposure to that Obligor. Only loans with identical parties are included in the same Obligor relationship. Loans to a single individual comprise a different Obligor relationship to loans that individual may hold jointly with other parties, for example :

Loan	Borrowers	Obligor
Loan 1	Borrower A	Obligor 1
Loan 2	Borrower A and B	Obligor 2
Loan 3	Borrower B and C	Obligor 3
Loan 4	Borrower A and C	Obligor 4

EBS operates a tiered approach to our large exposure policy by having different limits set by reference to the credit risk grading system used for commercial property assets. This credit risk grading system effectively applies a risk ranking according to the quality of the credit. EBS operates a nine point grading system which covers all commercial property assets ; grades 1 – 5 relate to 'performing' assets, grade 6 relates to obligors who are on credit risk watch, and grades 7 to 9 relates to non-performing credits. An outline of the current grading structure is set out as an Appendix to this document.

The limits for individual obligors are set out in the table below.

Obligor Grade	Obligor Limit as % of General Reserves (€466.9m as at 31/12/2005)	Approximate value of limit as at 31/12/2005
Grade 1 Obligor	25% (Previously 15%)	**€117m**
Grade 2 Obligor	20% (Previously 15%)	**€93m**
Grade 3 Obligor	15% (Unchanged)	**€70m**
Grade 4 Obligor	10% (Reduced from 15%)	**€47m**
Grade 5 and below	5% (Reduced from 15%)	**€23m**

Grade 1 and Grade 2 obligors relates to our highest quality clients, with strong repayment capacity and security cover and net worth / experience of client being the key determinants.

Grade 3 remains unchanged from its previous limit with the higher risk grades of 4 & 5 lower than the previous limit which had applied irrespective of the risk rating of the credit. These grades relate to loans with weaker repayment and security cover and also to development finance credits.

3. CONNECTED OBLIGOR LIMITS

Obligors are regarded as "Connected" and their individual Obligor exposures combined where;

(a) they constitute a single risk because one of them, directly or indirectly, has control over the other or others; or

(b) whilst there is no relationship of control, they are regarded as constituting a single risk because they are so interconnected, that if one of them were to experience financial problems, the other or others would be likely to encounter repayment difficulties.

This definition is based on the 'connected exposure' definition set out by the Regulator in relation to large exposure limits. By imposing a limit, EBS restricts the risk that one borrower entity may straddle several obligor level relationships, and thus result in a higher than desired exposure. The limit for connected obligor is 25% of general reserves which would have been €117m as at 31/12/2005.

4. CONCENTRATED PROJECT LIMITS

This is a limit on the level of exposure EBS is happy to accept on any one individual building or site / project. This limit is currently 10% of general reserves which, based on December 2005 levels would have amounted to €47m. EBS acknowledges that there is one exception to this limit ; this is the facility currently extended on our own head quarters at 2 Burlington Road, Dublin 4 where we currently have a €61m facility drawn. However this case is exceptional, and will be partially sold down which will reduce our exposure in 2007.

Appendix 1 **Current Credit Risk Rating System for Commercial Property Assets**

Grade	PD	LGD	Risk Category	Brief Summary of Grading Definitions
1	**Min**	**Low**	**Minimal Risk**	Top quality lending, confined to clients with a satisfactory track record, substantial net worth and whose ability to discharge their obligations is undoubted. Generally EBS clients or new with a confirmed pedigree. Loans with a LTV of less than 65% and repayment cover within policy guidelines. Formal and timely financial information is held.
2	**Low**	**Low**	**Excellent Risk**	Lending of excellent quality where the client has significant net worth & income. New or existing Client with a confirmed pedigree. Loans are within policy guidelines for LTV & repayment cover. Formal and timely financial information is held.
3	**Low**	**Low/Med**	**Good Risk**	Lending of a satisfactory quality which may be outside policy guidelines for LTV but where repayment capacity criteria are met. Formal and timely financial information is generally held.
4	**Med**	**Low**	**Satisfactory Risk**	Lending of good quality which may be outside guidelines for repayment capacity but within LTV criteria. Client's net worth and gearing are deemed sufficient. Financial information may not fully satisfy targeted standards.
5	**Med**	**Low/Med**	**Acceptable Risk**	Lending of acceptable quality which may include the following: • Where repayment capacity is marginal or reliant on particular occurrence. • New start up business has yet to establish a positive track record. • Lending maybe outside policy guidelines for repayment cover **and** LTV. Financial information deemed sufficient.
6	**High**	**Low/Med**	**Active Watch Risk (Impairment Alert)**	Existing exposures where there is evidence of deterioration in the performance of any account, or credits which – in EBS opinion – imply additional credit risk and where customer contact is necessary to resolve the position. Arrears less than 90 days may be a permanent or sporadic feature of the loan profile. Loan is not deemed to be in default.
7	**Actual**	**Med/High**	**Unacceptable Risk (Loan in Default - Impairment assessment)**	Existing lending where the adverse trends are sufficient to call into question the ability of the customer to repay and where we as a result wish to recover the debt. Loan loss is not anticipated at present. Credit is in default, i.e., it is more than 90 days past due the scheduled payment date.
8	**Actual**	**High**	**Impairment Loss confirmed/Provision applied**	Where a loss of principal or interest is confirmed and an individual provision is created.
9	**Actual**	**High**	**Write-off**	Full or partial write off has been approved by Credit Risk Committee.