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

Volume 1: Report
Volume 2: Inquiry Framework
Volume 3: Evidence

Oireachtas
OIR : Core Book 50

January 2016

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R2: Effectiveness of the Supervisory Practice (Central Bank, Regulator and Department of Finance)

R2b: Nature and effectiveness of the operational implementation of the macro economic and prudential policy

R4: Appropriateness and effective utilisation of the Expert Advice

R4a: Appropriateness of expert advice sought, quality of analysis of the advice and how this advice was used

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THEME: R2

Effectiveness of the supervisory practice (Central Bank, Financial Regulator and Department of Finance)

LINE OF INQUIRY: R2b

Nature and effectiveness of the operational implementation of the macro economic and prudential policy

Effective Regulation, Fostering Innovation, Competitiveness and Competition in the Financial Services Industry

Mitigating Risk through Compliance

A principles-led approach to regulation is the right model for Ireland. It means that the responsibility for the proper management and control of a financial service provider, and the integrity of its systems, rests with its board of directors and its senior management. This approach focuses on outcomes, is robust and internationally credible. It both allows and requires financial service providers to manage themselves. This vital work is overseen by the Prudential Director. Financial service providers must have systems and policies in place to mitigate risk and monitor compliance with their internal policies. Our role involves oversight of the quality of the institution's corporate governance, including risk management and internal control systems.

We fully expect boards and senior management of all financial service providers operating in Ireland to adopt ethical behaviour and transparency in business dealings as key values. We do not examine each transaction or contract entered into by institutions to test compliance. Neither do we seek to interfere with the design of financial products. We expect all financial service providers, whether engaged in international or domestic activities, to comply with best practice. Where a financial service provider does not fulfil these reasonable expectations we have a number of enforcement measures available to us, culminating in administrative sanctions. I am satisfied that the majority of financial service providers operate to a high standard. This is borne out by the very small number of cases that required such actions in 2006.

Better Regulation

We strive for a regulatory system that is robust, is internationally credible and that allows financial service providers the freedom to run their businesses properly. We want to implement European regulation in a manner consistent with this approach. However, in keeping with this form of implementation, we must be able to depend on industry to honour the obligations and commitment that this model of supervision demands. We are committed to ensuring that our regulatory requirements do not become a barrier to competitiveness and innovation. We apply the Government's 'Better Regulation' principles and are active members of the Taoiseach's Better Regulation Group.

In accordance with the 'Better Regulation' principle of transparency, we consult publicly before introducing a new regulation. The Consultative Consumer and Industry Panels provide an important mechanism for ensuring that the consultation process with stakeholders is effective and efficient. Both Panels were invited to make a number of valuable submissions to us on a range of regulatory proposals, including our Strategic Plan for 2007-2009 and provided us with comments on our draft statement of income and expenditure. 2006 has been a year of further development in our constructive relationships with the two Consultative Panels.

Pictured at the Insurance Institute Industry Leaders Conference with the Chief Executive Patrick Neary who spoke at the event are (l–r) Michael Brennan, President, The Insurance Institute of Ireland; Mary Fulton, Partner, Deloitte; and Cormac McCarthy, Group Chief Executive Officer, Ulster Bank Group.

NIRSA Working Paper Series
No 59 – July 2010

NIRSA
National Institute For Regional and Spatial Analysis
An Institiúid Náisiúnta um Anailís Réigiúnach agus Spásúil

NUI MAYNOOTH
Ollscoil na hÉireann Má Nuad

A Haunted Landscape: Housing and Ghost Estates in Post-Celtic Tiger Ireland

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HEA
Higher Education Authority
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NDP
NATIONAL DEVELOPMENT PLAN

A Haunted Landscape: Housing and Ghost Estates in Post-Celtic Tiger Ireland

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NIRSA Working Paper 59

July 2010

This working paper is accompanied by an Excel workbook containing all the original data and data sources used in this report. References in the text refer to specific datasheets (see http://www.nuim.ie/nirsa/research/documents/a-haunted-landscape.xls)

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Executive Summary

During the Celtic Tiger boom Ireland experienced a phenomenal growth in property construction and house prices. Construction became a major component and driver of the Irish economy. Both development and its underlying finances were allowed to become massively over-extended, creating an enormous property bubble. Rather than the much hoped for 'soft landing', the bubble popped in spectacular fashion leading to a radical transformation of the property market, with tumbling house prices and widespread negative equity, and a collapse in construction activity.

Government has two principle levers through which it can seek to regulate property development. The first is through fiscal policy with respect to regulating access to credit and determining taxation rates. The second is through planning policy and the zoning of land and the granting of planning permissions. Explanations of the Irish property bubble have focused almost exclusively on the former, and the role of the banks, tax incentive schemes, and the failures of financial regulators. **To date, the role of the planning system in creating the property bubble has been little considered.** And yet, the banks could have lent all the money they desired, but if zonings and planning permissions were not forthcoming then development could not have occurred in the way that it did.

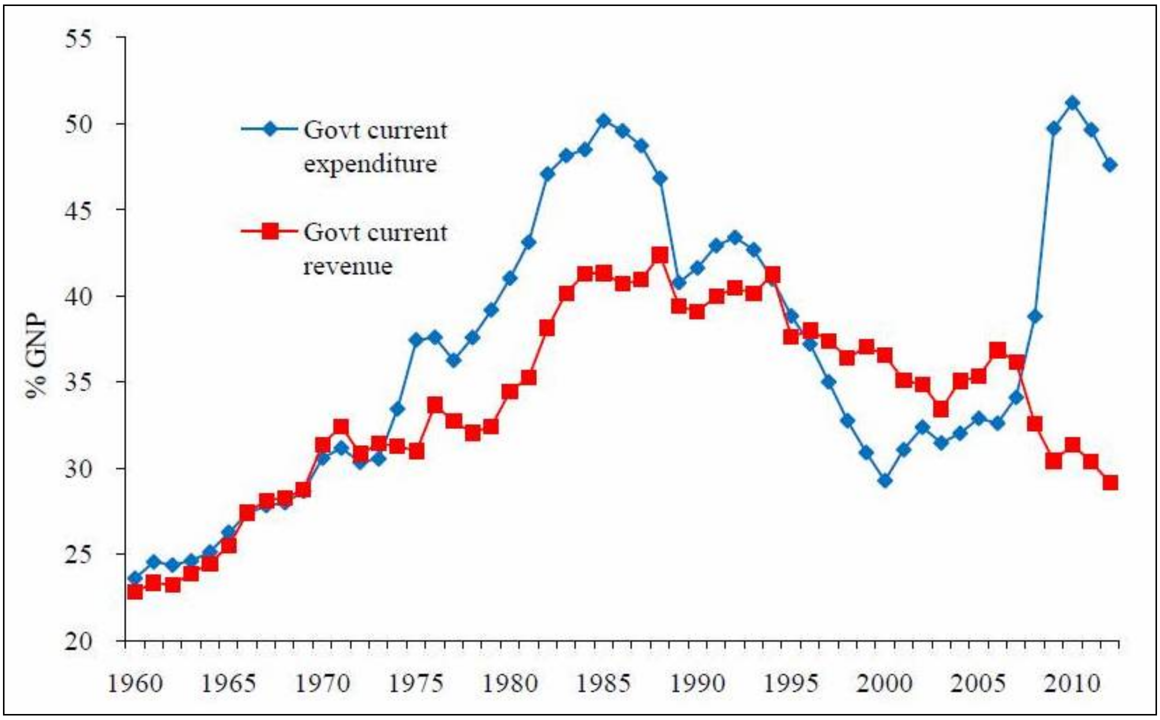
As well as a catastrophic failure in Ireland's banking and financial regulatory system, **there has been a catastrophic failure of the planning system**. In a housing boom planning should act as a counter-balance to the pressures of development in order to maintain a stable housing market and try to prevent boom and bust cycles. Planning should provide checks and balances to the excesses of development and act for the common good, even if that means taking unpopular decisions. However, during the Celtic Tiger period a laissez-faire approach to planning predominated at all levels of governance that was insufficiently evidence-informed with respect to long-term demographic demand, market conditions and issues of sustainability, and which marginalised and ignored more cautious voices. Both the fiscal and planning levers of development were overly pro-growth. As a result, not only was there an unsustainable growth in property prices, but this was accompanied by a property building frenzy that led to a significant oversupply of housing (as well as offices, retail units and hotels) in almost all parts of the country. The level of over-development that has occurred will take years to correct and seriously hamper the recovery of the housing market and the operation of NAMA. Indeed, **there are legitimate questions as to whether NAMA can succeed** in its aims over its intended life-span.

It is our contention that an independent review of the operation of the planning system during the Celtic Tiger years be undertaken to consider fully the role of planning in the creation of the property bubble, similar to the Honohan (2010) and the Regling and Watson (2010) reports on banking and financial regulation. The review would examine planning policy formation and application, and the organisation, operation and regulation of planning within and across different agencies and at all scales in Ireland. It would investigate all aspects of the planning system and its operation, including charges of localism, cronyism and clientelism where appropriate. The inquiry should not take the form of a witch hunt or a blame game, but rather constitute a systemic review of how the planning system failed to counter and control the excesses of the boom and provide a more stable and sustainable pattern of development.

In this working paper, we examine the creation of 'a haunted landscape' – the recent boom and the bust of the Irish housing market, and the creation of a new phenomenon, 'ghost estates'. We draw on and analyze numerous different government and industry datasets to provide a rigorous evidence base for our conclusions. **What the data reveal is a pattern of development that ran counter to what one would have expected or hoped for - those local authorities that had the most vacant stock in 2006, subsequently built the most new housing, now have the highest surpluses of stock, and have the most land zoned for future use.** Essentially, a number of local authorities did not heed good planning guidelines and regional and national objectives; conduct sensible demographic profiling of potential demand; or take account of the fact that much of the land zoned lacks essential services such as water and sewerage treatment plants, energy supply, public transport or roads. Instead, permissions and zoning have been facilitated by the abandonment of basic planning principles by elected representatives on the local and national stage and driven by the demands of local people, developers and speculators, and ambitious, localised growth plans framed within a zero-sum game of potentially being left behind but by the property sector, the crisis has been felt more strongly and deeply in Ireland than in many developed countries. In particular, the dependence on the property market as a key driver of the economy and a vital source of tax revenue has left the country with a set of serious problems that may take a generation or more to resolve. As the global crisis deepened, the Irish property bubble burst, and the vast over-exposure of Irish banks to toxic property loans became apparent. The collapse of the property and banking sectors has led to: a contraction in the wider economy, with the drying up of credit, markets and tax receipts, leading to a huge hole in the public purse; an extensive bank bailout, including the establishment of the National Assets Management Agency (NAMA) that has acquired €88b of property debt and rolled up interest from Irish banks; bank recapitalisation (Bank of Ireland, Allied Irish Bank) and nationalisation (Irish Nationwide Building Society, Anglo Irish Bank, EBS); massive state borrowing to service the bank bailout and the public sector spend; rising unemployment; and plummeting house prices.

By the end of 2009, the Government's tax take had shrunk to €33 billion, yet net expenditure for the year was €47 billion, with the hole in the public finances standing at a €24.6 billion and rising at over a billion a month (Irish Times, 5th January 2010). Figure 1 illustrates this taxation crisis by detailing government expenditure vis-à-vis GNP. As of May 2010, bank recapitalisation had cost €21.8bn with a projection for a further €10b (Carswell et al 2010), and NAMA was projected to pay €47bn for its property portfolio (Finfacts 2010). The Central Bank predicts that the State will have to write-off €25bn in unrecoverable capital injections into Anglo-Irish Bank and Irish Nationwide Building Society (Honohan 2010). The numbers of people signing onto the Live Register has risen from 160,139 in January 2006, with a seasonally adjusted standardised unemployment rate of 4.4%, to 439,100 by May 2010, with an seasonally adjusted standardised unemployment rate of 13.7% (see CSO 2010a; datasheet 1). House prices have depreciated substantially to the extent that 250,000 households are in negative equity and, as of the end of Q1 2010, 32,321 mortgages are in arrears for 90 days or more (4.1 per cent of residential mortgages) (Mortgage Arrears and Personal Debt Expert Group 2010).

Figure 1: Current government expenditure and revenue, 1960-2010



Source: Honohan (2010: 30)

For the past twenty years, Ireland has grappled with rapid transformation socially, economically and intellectually, and the country is yet again experiencing another seismic shift. In this paper, we document the crisis in Ireland through a lens that focuses on the Irish housing market and so-called ghost estates – speculative, under-occupied, often unfinished housing developments that now litter the Irish landscape. In so doing, we highlight how the Irish housing boom and collapse was inextricably shaped by the institutionally and place specific nature of Irish neoliberalism.

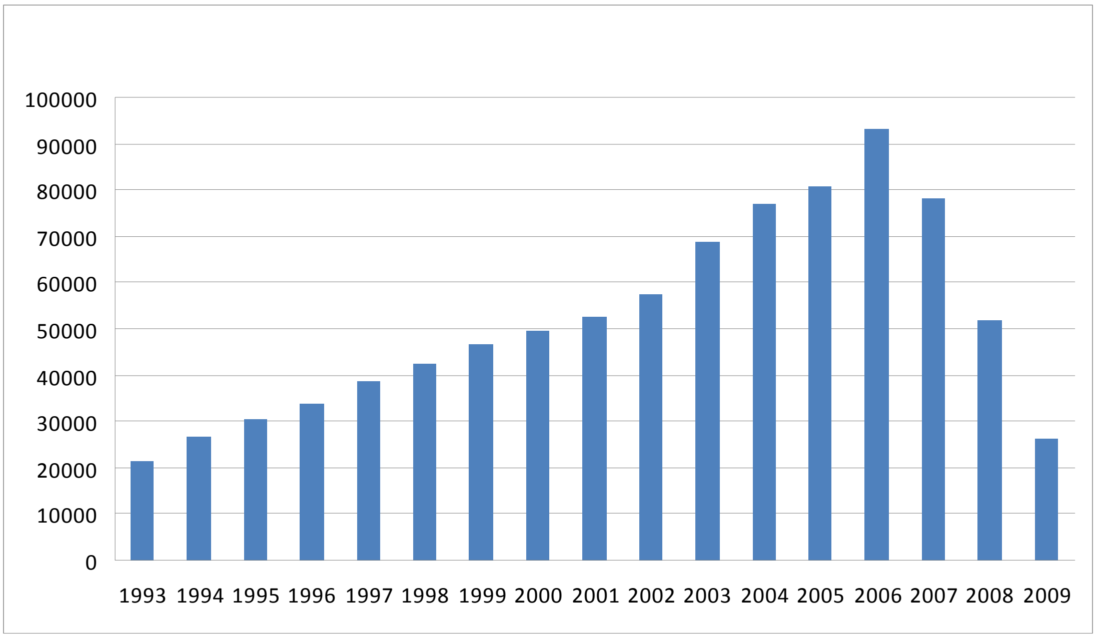
The paper has seven parts. First, we detail how the Irish economy and property sector was transformed in the Celtic Tiger period. Second, we document the extent of the present housing crisis in Ireland. Third, we examine levels of vacancy and oversupply throughout the country. Fourth, we explore the new phenomena of ghost estates. Fifth, we explain the Irish housing bubble, providing an analysis of political, economic and planning systems and policies that operated during the Celtic Tiger era. Sixth, we examine the government's response to the crisis, focusing in particular on

City) from their peak at the end of 2009 (see Figure 6; datasheet 7). The Permanent TSB/ESRI Index reported in April 2010 that the average national prices, based on mortgage data, had fallen to the end of April 2002 levels, with a 34% decrease in prices since they peaked in Quarter 4 2006, falling from €311,078 to €204,830 (outside of Dublin from €267,484 to €183,309 (-31.4%); in Dublin from €427,946 to €250,872 (-41.3%)) (datasheet 8; also Figure 3 and datasheet 4). Many economic commentators are now predicting that house prices will fall 40-60% from peak values (e.g., M. Kelly 2009; Whelan 2010a). Similarly, rents fell for seven quarters in a row to Q1 2010, with private rents being almost 25% below their peak value in Q2 2008 (DKM 2010).

Further, there has been a steep decline in land values since the height of the boom. For example, in late 2009 the Dublin Docklands Development Authority (DDDA) estimated that the 24.9 acre Irish Glass Bottle site in Ringsend (bought for €412m in 2006) is presently worth €50m (a drop of 87%), while its Long Term Economic Value (LTEV) is €62.5m. This is a prime city centre site with high development potential, and other sites have taken similar falls in value. For those sites outside of the urban centres, it is questionable as to whether these lands, in the short to medium term, will return to the prices paid for them, reverting to agricultural prices. Knight Frank Ireland (2010) detail that the national average price paid for farmland in 2009 was €9,678 (€11,236 per acre if one excludes one very large transaction of 1,540 acres in Clare), a drop of 43.3 per cent on the average price of €17,081 per acre in 2008. The biggest fall in value was in the Dublin-Kildare-Wicklow region where prices dropped by 56.6 percent (Figure 7; datasheet 9).

DKM (2009) reports that from 2006 to 2009(est.) the total value of construction output fell from €37,611m to €19,857 (a drop of 47.2%; see Figure 8; datasheet 10). Further, the number of construction workers fell from their Q2 2007 peak of 269,600 to 155,400 in Q2 2009 (CSO 2009b; datasheet 10), and as of June 2010 were estimated to be 129,000 (Press Association 2010). Property related tax receipts (stamp duty, capital gains tax, VAT, development levies) have also dropped dramatically given the much smaller percentage of sales and the reduction in new commencements. For example, for the period January to end of December 2009, A key factor driving down house and land prices is not simply a lack of confidence or difficulties in accessing credit, but a marked oversupply of housing stock and zoned land. Ireland was in the middle of a building and land speculation frenzy when the crisis initiated. The DEHLG records that there were 88,419 housing completions in 2006 (recorded as 93,419, but 5,000 were delayed reporting from 2005; see Figure 9). This high level of production continued into 2007 (78,027 units), slowing dramatically in 2008 (51,724 units) and 2009 (26,420 units). All told, there were 244,590 units built between January 2006 and December 2009 (that were connected to the ESB electricity grid) (datasheet 3). This is despite the fact that in April 2006, the Census revealed that 266,322 housing units were unoccupied (216,533 vacant units and 49,789 holiday homes; 15% of stock; datasheet 11). The result was a significant volume of property coming onto an oversupplied market at a time when it was at first softening and then outright plummeting. According to irishpropertywatch.com in May 2010, 112,506 housing units were for sale in Ireland (both new and secondhand) and another 20,463 available for rent. Given the oversupply and the flat market, planning permissions granted were down 63.9% in 2009, housing registrations are down 95% since their peak in September 2006, and housing commencements are down 90% on their peak in 2005 (DKM 2010).

Figure 9: House completions in Ireland, 1993-2009



Source: DEHLG

(N.B. 5000 of the completions recorded in 2006 were completed in 2005)

4. The Present Rate of Oversupply of Housing and Zoned Land

Calculating the level of oversupply in the Irish housing market is not straightforward due to the paucity of data - vacancy rates are only measured every five years through the Census, and potential oversupply is not measured at all. To date, there have been four studies that have sought to estimate present rates of vacancy and oversupply (see Table 1), plus an estimate of the oversupply of brand new, unsold homes (c.40K) by the CIF (Construction Industry Federation; CIF 2009). Two other estimates – Derek Brawn (2009) and propertypin.com - also place overall vacancy (inc. holiday homes) at over 330,000, but do not provide detailed workings, nor an estimate of oversupply. Excluding the CIF estimate, there is general alignment between the estimates produced by ourselves (NIRSA), UCD (Williams et al. 2010), DKM/DEHLG (2009) and Goodbody (pers comms; Hennessy 2010). All four organisations estimate that vacancy including holiday homes is over 300K, that vacancy excluding holiday homes is over 228K, and that the potential oversupply is over 103K (and if the top rates are used for DKM/DEHLG and Goodbody then the alignment is relatively strong).

Table 1: Comparison of housing vacancy rate studies (as of 2009)

	(1) Vacancy (inc holiday homes)	(2) Holiday homes	(3) Vacancy (exc. holiday homes)	(4) Base vacancy[a]	(5) Obsol[b]	(6) Potential oversupply[c]
DKM/DEHLG	301,682-326,685	73,476	228,206-253,209	106,177	-	122,029-147,032
Goodbody	302,475-343,480	73,000	229,475-270,480	126,189	-	103,286-144,291
NIRSA	352,414 (338,031)[d]	49,789 (86,002)[e]	302,625K (252,029)	(87,356)[f]	(44,425)	(120,248)
UCD	345,116	64,520	280,596	98,980	9,898	171,178

Notes:

a) Base vacancy refers to the expected underlying rate of vacancy normal in any housing market.

b) Obsolescence refers to the expected number of houses falling out of the live stock because they are no longer habitable or change from residential use.

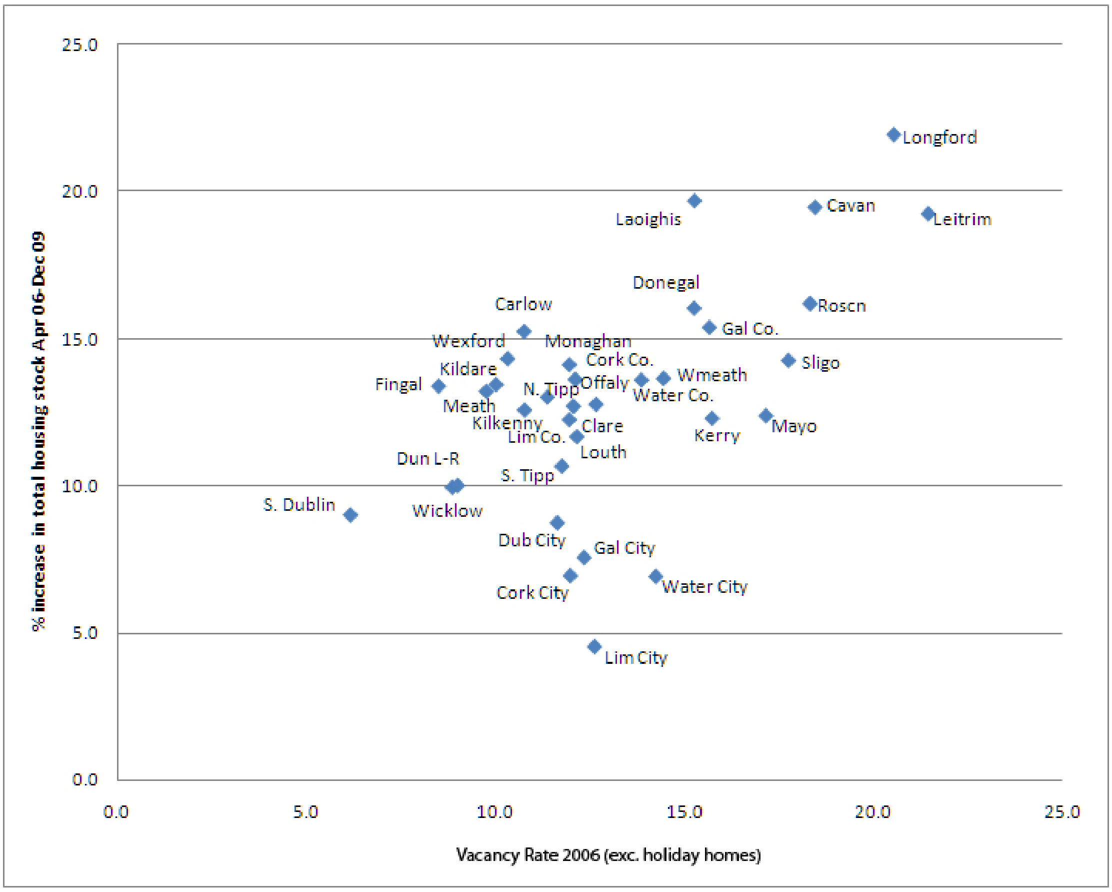
2006 and December 2009 (F). The estimated demand (M) is calculated by determining the household growth between 1996 and 2006 (J), projecting forward household growth between April 2006 and December 2009 based on the same rate of increase (K), and adding potential holiday home demand (L) (calculated as 5% of total stock). Potential oversupply is calculated by subtracting potential demand (M) from estimated supply (G). To provide some context as to the extent of potential oversupply we have calculated how long available stock would last (O) if the number of households continued to grow at the rate they did between 1996 and 2006 (representing somewhat of a best case scenario given that household growth has slowed in recent years and may well be falling given the recent growth in emigration). Whilst the model does not take account of local effects such as development plans or strategic investments, or the functioning of local labour markets, it nevertheless provides a robust estimate of oversupply based on existing data.

At the global level, the model suggests that given the household increase 1996-2006 and potential holiday home demand there was a need to supply 139,784 units in the period April 2006 and December 2009 (126,782 units to accommodate new households; 13,002 houses for holiday homes). There were 87,356 vacant surplus stock above the 6% rate in Apr 2006, and 217,101 houses built between Apr 06-Dec 09, and during the same period we would expect 44,425 to become obsolete (giving a total potential available stock of 260,032). This would indicate that as of the end of 2009 there was a potential surplus stock of 120,248 units. This stock would last on average 3.5 years if household growth continued to rise at the same rate as it did between 1996 and 2006 (a period of rapid growth which is not being mirrored at the present time) and the stock was appropriately distributed around the country vis-à-vis potential demand (which it is not).

There is considerable local variation in potential oversupply rates, with some counties having relatively low levels of potential oversupply and others having several years worth of stock. For example, the local authorities surrounding Dublin City (Fingal, Kildare, Meath, South Dublin, Wicklow) have constructed housing approximately in line with demand, and it is likely that when the Dublin economy starts to recover excess housing will be absorbed within a few months (although there is a relatively large stock of vacant investment properties that might flood onto the market –

Tenant's First (2009), citing the IAVI, report that there are 40,000 of these in Dublin alone). However, Dublin City and Dun Laoghaire-Rathdown, like Cork City, have constructed units far in excess of the demand experienced during the Celtic Tiger years. To some degree this oversupply is the result of unfortunate timing, as much of this build was part of a broader programme of planned urban development, renewal and densification, though the scale of development was overly ambitious given previous rates of growth. Similarly, counties in the north midlands and along the border (Cavan, Donegal, Leitrim, Longford, Mayo, Roscommon, Sligo) have constructed far more houses than one would expect demographically, though the reason is quite different. Based on the model, Leitrim and Longford both have housing stocks that would take over ten years to fill if households grew at the 1996-2006 rate. The reason for this is clear if one plots the vacancy rate in 2006 (as recorded in the Census) against the percentage increase in stock between 2006 and 2009 (as recorded by the DEHLG) (see Figure 11).

Figure 11: Percentage of increase in housing stock 2006-2009 in relation to vacancy (exc. holiday homes) in 2006

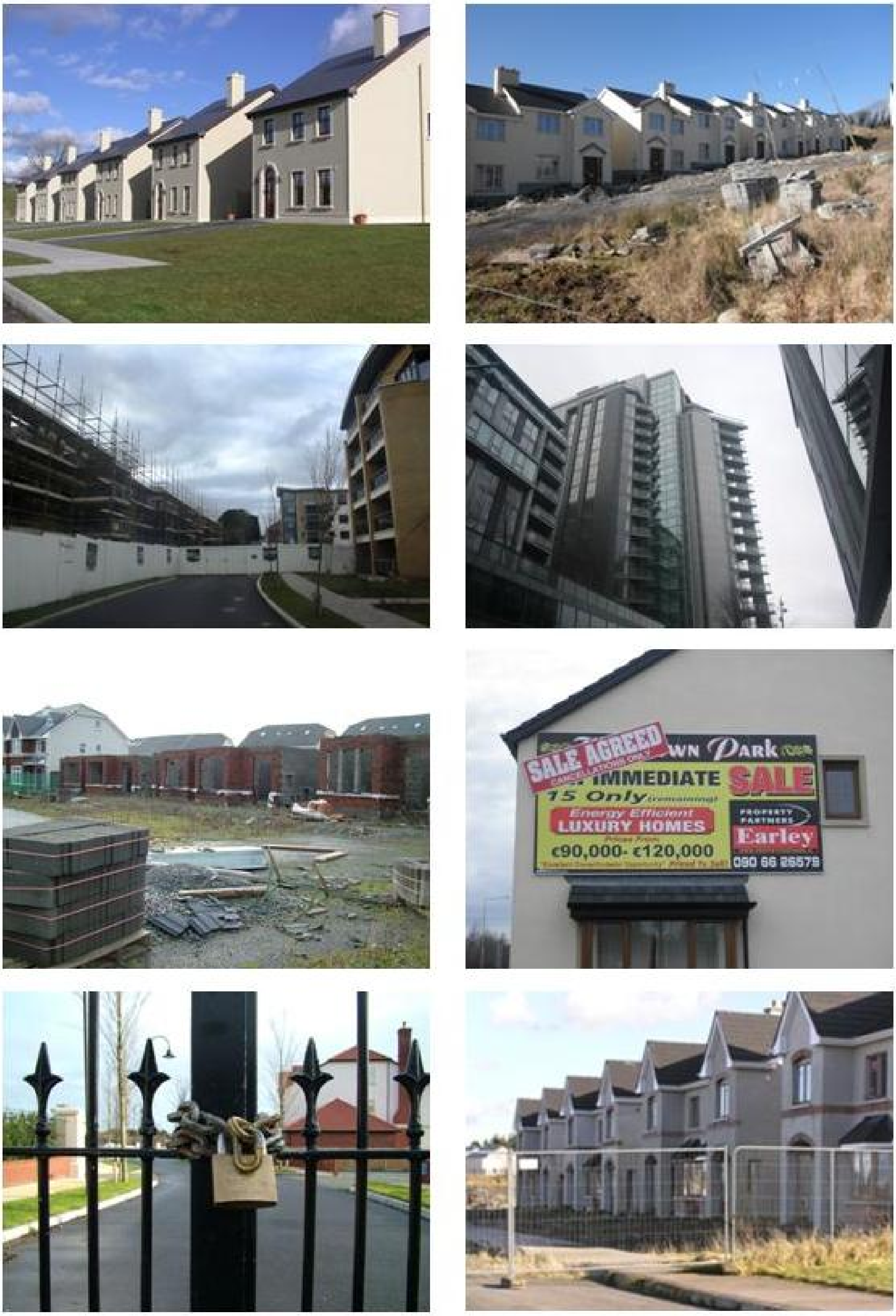


Collectively, the data we have presented in this section demonstrate that housing and land supply and household demand became uncoupled from early on in the Celtic Tiger era and progressively grew further apart. This is abundantly clear from comparing housing completions with household growth between 1996 and 2006. While 553,267 housing units were built between January 1996 and December 2005, the number of households grew by only 346,400 between April 1996 and April 2006. An additional 244,590 units were built between January 2006 and December 2009, and yet the number of households did not increase by anywhere near the same amount. The number of households in June 2008 was 1.58m (CSO 2009d), up 110,000 from 1.47m in April 2006, and growth is presently thought to be static or falling given rising emigration. All through the boom years the vacancy rate was rising - in 1996 the rate was 8.5%, in 2002 it was 9.8%, and in 2006 it was 15% (includes holiday homes). The 2006 rate is double the EU average rate of 7.3% (skewed upwards by Spain, Portugal and Ireland) and is way in excess of what one would expect as an acceptable base rate (3-4%). Even accounting for obsolescence and replacement, and holiday homes, it is obvious that there is presently a wide disparity between the total stock of housing and the number of households (in December 2009, Geodirectory reported that there were 1.98m residential units in the state).

5. Ghost Estates

One result of housing supply being out of sync with housing demand has been the creation of a new phenomenon, so-called 'ghost estates'. We have defined a ghost estate as a development of ten or more houses where 50% of the properties are either vacant or under-construction. Using that definition we have analyzed the Geodirectory database in order to identify all properties built post-2005 where 10 or more units share the same estate/street address and more than 50 percent are coded as either vacant or under-construction. We have then undertaken a ground-truthing exercise using two methods. First, we have cross-checked the results with house sale websites such as daft.ie and myhome.ie. Second, we have visited 60 of the estates in three locations (South Dublin/Kildare, South Leitrim/North Roscommon, Cork City and county) to verify their status. It is important to note that ghost estates vary markedly in their condition, from sites that are 100% under-construction through to completed estates that are finished and fully serviced (see Figure 15).

Figure 15: Example ghost estates



The total number of ghost estates developed post-2005 identified by this method is 620, and includes 19,262 units, 11,670 of which are vacant and 3,823 are under-construction (with average vacant/under-construction rate of 80%). There are 86 estates with more than 50 properties (of which more than 50% are vacant/under-construction), 252 with between 21-50 properties, and 282 between 10-20 properties. Having driven round the towns we visited it is clear to us that our method under-counts ghost estates, most probably because the Geodirectory database under-records vacancy and under-construction as they have to maintain this status for quite a while to be coded as such and they are still engaged in a rolling process of identifying vacant properties. There is some noise in the data because they are only collected twice a year in urban areas and once a year in rural areas, meaning that units in some estates will have been sold, although in the vast majority of cases this does not move them under the 50% threshold. The number of estates would certainly increase if we were to change the parameters down to a 30% vacancy/under-construction rate, depending on how we want to define a ghost estate.

As Figure 16 reveals, there are multiples of ghost estates in every county in the state. Simply detailing the number of estates per county, however, can give a false impression because it takes no account of the size of the overall population (datasheet 24). Whilst Cork County (not including the Cork City area) has 90 ghost estates, it had a population of 361,788 in 2006. Leitrim has 21 estates, but a population of 28,950. We have therefore standardised the number of estates by per 1,000 head of population (see Figure 17). Leitrim (21 estates), Longford (19) and Roscommon (35) have a particularly high ratio of estates per head of population, indicating that these estates constitute an oversupply in the market. This is perhaps unsurprising given that it was these counties who built the most properties in relation to their overall stock and vacancy levels between 2006 and 2009 (see Figure 11). These are followed by Sligo (24), Cavan (21), Monaghan (18), Carlow (15), Cork County (90), Tipperary North (16), Kilkenny (21), Westmeath (18), and Laois (15). Whilst some estates are vacant holiday home developments, they nevertheless are presently surplus to demand and are unlikely to be purchased in the short term whilst the market is still trying to find its bottom.

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ADVISORY FORUM ON FINANCIAL LEGISLATION
Report of meeting 12 December 2007 and Action Points

Attendance
Attendance list attached as Appendix I.

Introduction
The Forum approved the minutes of the previous meeting.

Terms of Reference
The terms of reference were adopted. The Chair confirmed that the composition of the Forum reflects the community of stakeholders involved in the consolidation and modernisation project including employees.

Themes Paper
A detailed discussion of the "Themes" paper followed. The main strands that emerged from the discussion are summarised at Appendix II. The Chair indicated that the themes paper was intended to initiate a structured discussion on the macro issues facing the Forum in reforming the legal framework and to help define the overall direction it would take. This discussion, by its nature, will be constantly evolving and will be developed and informed in the context of the specific issues as they arise.

Working Methods
The Chair updated the Forum on his proposed approach to the establishment and composition of drafting groups in the main sectoral areas and the need for membership with deep specialist knowledge and expertise in each of the sectoral areas (see Appendix III and IV for further detail).

He highlighted the primary role of the Forum in relation to policy issues that emerge from the work of the drafting groups as well as the centrality of the consumer interest in all of the drafting work. It was agreed that the Funds Group and Securities Group ('securities' currently including all legislation in relation to intermediaries) would as their first task review and report to the Forum on the practicality of including funds legislation and market supervision legislation (i.e. Prospectus, Market Abuse and Transparency Directives) respectively as part of a single cross-sectoral bill. A different skill set may be required in the funds group if it is decided that funds are to be included in the consolidation. The Securities Group would also consolidate the legislation on MiFID and intermediaries.

It was noted that the Department of Finance was undertaking in Q1 2008 a review of the Consumer Credit Act (CCA) 1987 in consultation with the Financial Regulator taking into account the expected outcome of EU Consumer Credit Directive. This work would provide the Forum with an opportunity to examine the scope for the inclusion of the CCA as part of its work.

EU Proposals
The presentation highlighted key legislative developments at EU level that the Forum needs to be aware of in the context of the drafting process.

07/09

Dates of future meetings
16 January 2008 (Government Buildings). Tánaiste is expected to attend.
23 January 2008 (Arthur Cox, Earlsfort Centre, Earlsfort Terrace).

The project team will issue further dates for meetings to end March (possibly Wednesdays at fortnightly intervals).

Action Points

- Project Manager to send out schedule of meetings up to March.
- Members to remit to the project manager any changes to the Forum members' booklet.
- Chair to select co-coordinators and agree composition of drafting groups in advance of the next meeting with membership to be advised to the forum.

Appendix I - Attendance at Meeting

Forum

Pádraig Ó Ríordáin	Chair of Forum
John Cradden	Consumers Association of Ireland
Kieran Crowley	Small Firms Association
Muireann O'Neill	Nominee of the Minister for Enterprise, Trade and Employment
Larry Broderick	Irish Bank Officials Association
Gwen Harris	Society of St Vincent de Paul
William Beausang	Department of Finance
Vincent Madigan	Department of Enterprise, Trade and Employment
Joe Doherty	Central Bank and Financial Services Authority of Ireland
George Treacy	Financial Regulator
Damien Moloney	Office of the Attorney General
Bernard Sheridan	Financial Regulator
John O'Halloran	Irish League of Credit Unions
Paul Kierans	Dublin International Insurance & Management Association (DIMA)
Deirdre Somers	Irish Stock Exchange
Brian McNelis	Irish Brokers Association
Frank O'Dwyer	Irish Association of Investment Managers
Gary Palmer	Irish Funds Industry Association
Pat Farrell	Irish Banking Federation

Apologies and Alternate attendees

Alex Schuster	National Consumer Agency	John Maher (alternate)
Mike Kemp	Irish Insurance Federation	Paul McDonnell (alternate)
Aileen O'Donoghue	Financial Services Ireland	Brendan Kelly (alternate)
Diarmuid Kelly	Professional Insurance Brokers Association	Liam Carberry (alternate)

Project Team

Michael Manley	Project Manager
Karen Cullen	Project Team Member
Kevin Nolan	Project Team Member
Ciara Lonergan	Project Team Member
Jean Carberry	Project Team Member

Appendix II - Summary of main strands of the discussion on the Themes Paper

Themes Paper

- Proportionality is key to effective and efficient regulation

- The Forum should be mindful of scale/materiality when framing the legislation – i.e. one size does not fit all in regulation.

- Better Regulation principles will underpin the drafting of the legislation. However, the case for 'hardwiring' these principles into legislation requires careful consideration.

- Clarity regarding the definition and interpretation of each Better Regulation Principles would assist the Forum in its work.

- The Forum should adopt a principles-lead approach to the task. There are important differences and distinctions to be drawn between:
    - 'principles' to guide the drafting of legislation
    - 'principles' that might be considered as statutory objectives in legislation to guide the performance Regulator's statutory functions
    - 'principles' that are required as part of 'policies and principles' in legislation to provide a sufficient legal basis in primary legislation for the exercise of delegated powers; and
    - a 'principles based' approach to financial regulation as followed by the Financial Regulator

- Principles-based regulation focuses on outcomes not processes

- Simplification and improved accessibility of the legislative framework should be one of the major benefits of the project.

- Consideration should be given to the use of preambles to the proposed legislation similar to how such preambles are used in EU Directives. It may be helpful to include principles or other interpretative aids in this form.

- A risk-based approach should be integral. The Regulator at present has discretion to apply a risk-based approach to how legislation is implemented and this is an important flexibility and enables a responsive approach to new and unexpected developments. Accountability mechanisms overseeing this approach are important. The flexibility which a risk-based approach offers could be adversely affected by a legislative approach that strives for a high-degree of specificity in relation to regulatory principles.

- The group addressed the proposed 3 tier structure and drew the following conclusions:

– cross-sectoral harmonisation is desirable as far as possible

- the output must be a pragmatic and flexible system which both works now and provides the infrastructure for evolving regulatory and market needs

- the legislation must be legally robust should try to minimise opportunity for legal disputation and challenge

- secondary legislation cannot be made without the proper enabling powers in the primary legislation (i.e. 'policies and principles')

- it will be difficult at the outset of the project to draw a clear line between the level one (primary) and level two (secondary) provisions in the new framework

* It would be desirable for the proposed legislation to provide a robust structure for the implementation of further EU financial services legislation to the extent possible without the need for amending primary legislation

* A deliverable of this project could be an ongoing process for consultation underpinning development of further legislation at all levels.

* It is essential that a process supporting ongoing review and reform of financial services legislation is put in place so that the value from the consolidation and modernisation project is maximised.

* A practical benefit of the project could be a regular financial services bill.

Appendix III - Summary of main strands of the discussion on the Working Methods

Role of the drafting groups:

- The mandate of the groups is to draft the consolidated legislation. This needs to be done by specialists in the various areas.
- The cross-sectoral drafting group will pull together all the cross-sectoral issues for the Bill.
- The sectoral drafting groups – banking, insurance and securities subgroups will extract from the legislation what can be consolidated in each sectoral area
- The steering drafting group will co-ordinate the work of the sub-groups. It will be chaired by the Forum Chair, and will be made up of the coordinators of each sectoral group.
- Consumers will be represented on each subgroup by the Department and the Regulator.
- The appropriate group for non-deposit taking lenders legislation will require further consideration.

Composition of the drafting groups:

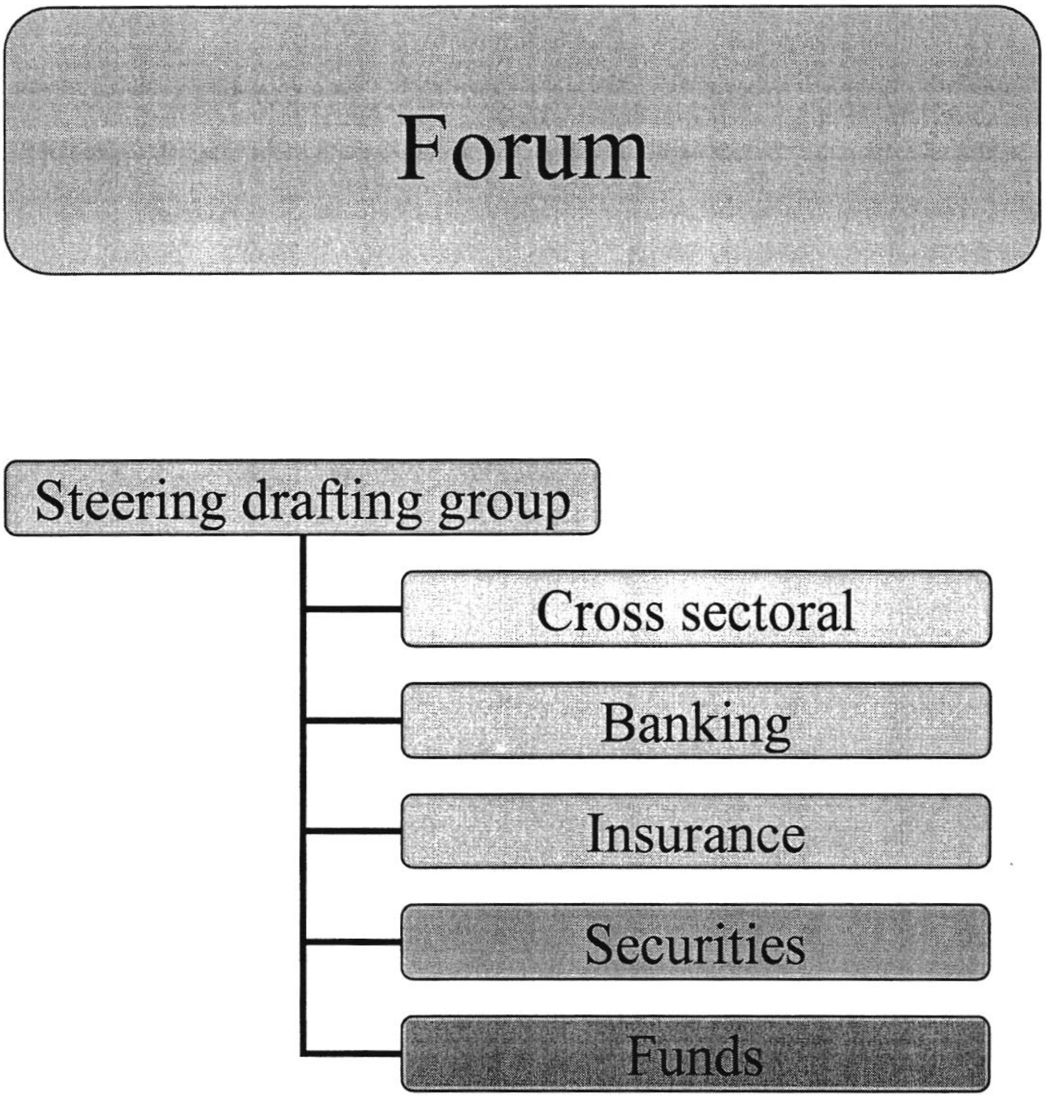
See Appendix IV below for proposed Group structure.

- 6-7 people on each group including in addition to the co-ordinator (senior, capable figure): Groups may differ depending on the extent of the work and skills they require but, in outline, may include a representative of the department and of the regulator, an in-house lawyer and an independent lawyer.
- Chair to approach potential co-ordinators before the next meeting. The participants in the subgroups should be technical experts in their area. The drafting work is completely voluntary and is expected to be very onerous.

At a later stage sub-groups of the Forum or of any of the drafting groups can be formed if the work requires. .

Appendix IV

Drafting Group Structure



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ADVISORY FORUM ON FINANCIAL LEGISLATION
Report of meeting 23 September 2008

Attendance
Attendance list attached at Appendix I.

Introduction
The Chair welcomed members. The Forum approved the minutes of the previous meeting. The Chair addressed the current dislocation in global financial systems. He pointed out that when the current phase of work (i.e. building the architecture of the Bill) is complete, the Forum may need to reflect on any changes in international thinking on the topics of regulation and principles-based regulation that have resulted from the current turmoil. Forum members should note that the current developments underscore the importance of the work of the Forum in producing a robust legal framework for today's financial sector.

Update from the Cross-Sectoral Drafting Group
The Chair then introduced Colm Kincaid, the co-ordinator of the cross-sectoral drafting group, who presented a detailed review of the work done to date by that drafting group. The presentation made, and all documents referred to, are attached. At the conclusion of the presentation the Chair highlighted two very important points:

- we now have clear guidance about what will go in the Bill;
- the methodology which has been developed will be very useful and there is now an excellent roadmap to ensure a robust framework.

Review of Progress
The Chair then outlined how the work done to date has demonstrated the benefit of the project:

- Firstly, and critically, this work will produce a hugely simplified, transparent, easier to understand, regulatory system.
- Secondly, as we progress we will draw out many historical differences between sectors that are just anomalies.
- Finally, we should be able to garner a lot of efficiencies – our new consolidated legislation will be easier to use than the existing body of legislation

The Chair also pointed out that the project is still at the big picture stage – more benefits will be apparent as work progress into the body of the S.I.s.
The project should progress more quickly now that the architecture is in place. However, there is no substitute for detailed reading of the existing legislation. It might be appropriate to consider adding more resources at this point in the project.

Progress Report from Other Drafting Groups
The Chair gave a brief update on the progress of the other drafting groups. The work of the Banking Group is progressing well. The group has made good progress in compiling an arrangement of sections, and has begun drafting work. Likewise, the Securities Group has completed much of the necessary preparatory work. The Insurance Group are now up and running and have familiarised themselves with the work methodology of the other groups. They are now beginning the process of consolidation. Discussions are ongoing on the issue of whether funds will be included in the scope of the project.

07/02.

Tánaiste's Request to Forum – [redacted] Judgement
Aidan Carrigan of the Department gave an update on this. [redacted]

Report to Minister
The Chair then addressed the Report which the Forum must make to the Minister in Q1 2009. The goal of the Forum is to produce a substantive document for the Minister in January, comprising a complete scheme for the Bill, together with some worked examples in terms of draft heads. The report to the Minister must also address how the project will be completed. It is critical to keep this in mind when drawing up work plans.

Work plans
The Department takes the view that the report from the cross-sectoral group is a good starting point for a work plan and will liaise with drafting groups regarding work plans.

Dates of Future Meetings
The next meeting will be held in a month or so.

Appendix I - Attendance at Meeting 23 September 2008

Forum

Pádraig Ó Ríordáin	Chair of Forum
William Beausang	Department of Finance
Kieran Crowley	Small Firms Association
Gwen Harris	Society of St Vincent de Paul
Brendan Kelly	Financial Services Ireland
Diarmuid Kelly	Professional Insurance Brokers Association
Vincent Madigan	Department of Enterprise, Trade & Employment
Brian McNelis	Irish Brokers Association
Damien Moloney	Office of the Attorney General
Frank O'Dwyer	Irish Association of Investment Managers
Muireann O' Neill	Nominee of the Minister for Enterprise, Trade & Employment
Gary Palmer	Irish Funds Industry Association
Alex Schuster	National Consumer Agency
Deirdre Somers	Irish Stock Exchange

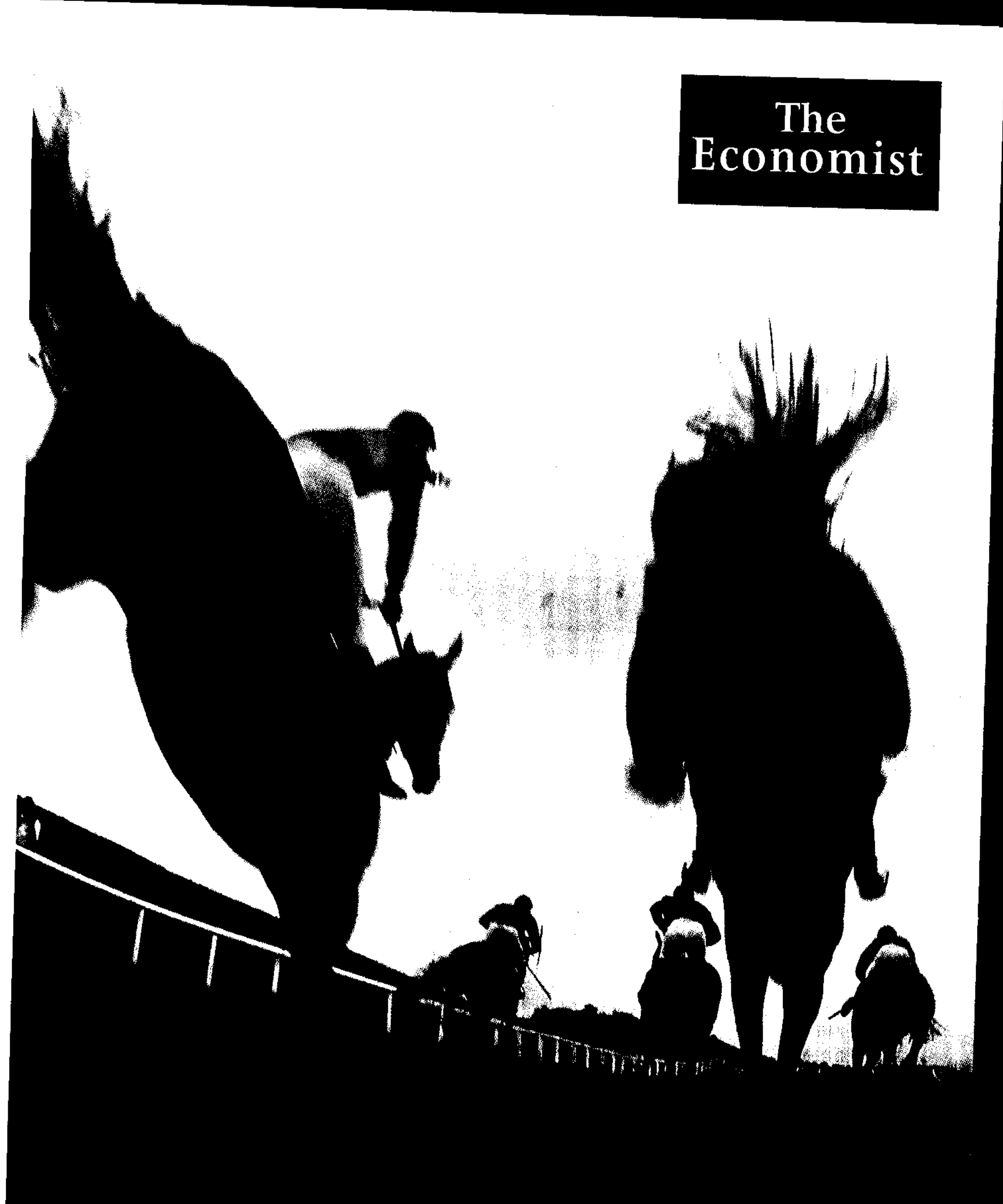
Apologies		**Alternate attendees**
Larry Broderick	Irish Bank Officials Association	-
Fiona Cullen	Irish League of Credit Unions	-
Joe Doherty	Central Bank and Financial Services Authority of Ireland	Shane Connolly
Pat Farrell	Irish Banking Federation	Eimer O'Rourke
Dermott Jewell	Consumers' Association of Ireland	
Mike Kemp	Irish Insurance Federation	Paul MacDonnell
Paul Kierans	Dublin International Insurance & Management Association	-
Bernard Sheridan	Financial Regulator	Donnie Kennedy
George Treacy	Financial Regulator	Grace O' Mahony

Project Team

Michael Manley	Project Manager
Karen Cullen	Project Team Member
Jean Carberry	Project Team Member

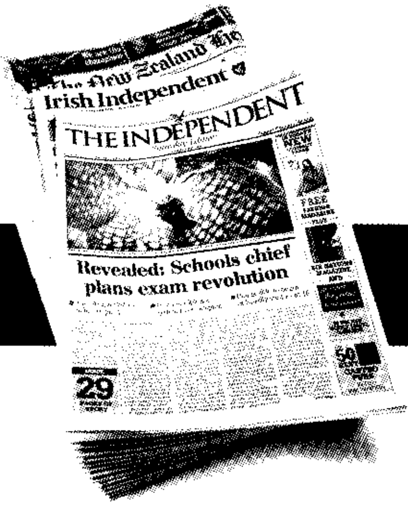
Also, from the Department: Aidan Carrigan.

The Economist



The luck of the Irish

A survey of Ireland | October 16th 2004



INDEPENDENT NEWS & MEDIA PLC

30 YEARS OF GLOBAL SUCCESS

"Thanks to *The Independent*, the face of British national newspapers has been changed forever." British Press Awards 2004

The Irish always did travel well...

Thirty years ago – under the leadership of Sir Anthony O'Reilly – Independent News & Media PLC [INWS.I; INWS.L] commenced international operations from its base in Dublin, Ireland.

Sir Anthony O'Reilly
Chief Executive Officer
Independent News & Media PLC

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The ability to always 'think globally and act locally' has seen Independent become the industry standard for innovation. Commenting on the successful launch of its 'compact' edition, the judges at the British Press Awards 2004 said – "Thanks to *The Independent*, the face of British national newspapers has been changed forever". In addition to the launch of compact editions in Ireland and the UK, Independent continues to deliver more new products and advertising platforms than at any time in the Group's history.

The result – continued and sustainable growth – delivering quality to readers, listeners, advertisers and shareholders.

	1994 US$M	2003 US$M	CAGR %
Revenues	406	1,573	16
Op. Profit	65	270	17

GLOBAL REACH

Today, Independent News & Media PLC manages newspaper, radio and outdoor advertising assets of over US$4.2 billion and has a stable of number one, market-leading newspaper brands in Ireland, the United Kingdom, South Africa, Australia and New Zealand. Publishing over 165 individual newspaper and magazine titles, the Group enjoys a weekly circulation figure of 13.5 million copies.

BRAND DIVERSITY & VITALITY

Independent's strong brands, leading market positions, geographic diversity and strong balance sheet leave the Group and its shareholders uniquely well positioned to benefit from the improving economic cycle and will guarantee the organic growth of the Group for the next five years.

For further information, please visit our web site: www.independentnewsmedia.com or e-mail info@inplc.com

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The luck of the Irish

The economic boom that spawned the "Celtic Tiger" has transformed Ireland. But, asks John Peet, can it last?

SURELY no other country in the rich world has seen its image change so fast. Fifteen years ago Ireland was deemed an economic failure, a country that after years of mismanagement was suffering from an awful cocktail of high unemployment, slow growth, high inflation, heavy taxation and towering public debts. Yet within a few years it had become the "Celtic Tiger", a rare example of a developed country with a growth record to match East Asia's, as well as enviably low unemployment and inflation, a low tax burden and a tiny public debt.

The Economist proved no better than anyone else at predicting this turnaround. Our most recent previous survey of Ireland, "The poorest of the rich", published in 1988, concluded that the country was heading for catastrophe, mainly because it had tried to erect a welfare state on continental European lines in an economy that was too poor to support one. Yet only nine years later, in 1997, Ireland featured on *The Economist*'s cover as "Europe's shining light". It goes to show how remarkable has been the transformation of a sleepy European backwater into a vibrant economy that in some years grew by as much as 10%.

That transformation has made the Irish republic, with just over 4m people, a place of great interest around the globe. Many rich countries, not least Ireland's sclerotic neighbours in western Europe, would love to achieve a similar change of image. The eight central European countries that joined the European Union in May seem fascinated by Ireland. Civil servants and businessmen in Dublin talk wearily of a procession of visitors from such places as Vilnius and Bratislava, anxious to emulate Ireland's leap from one of the EU's poorest members in the 1980s into one of its richest (see chart 1, next page). They all promise that they will make good use of EU money, as Ireland did, and avoid the fate of Greece, which in the 1980s was not far behind Ireland but has since been left standing.

Punching above its weight

The world's interest in Ireland is not confined to its rags-to-riches story. Thanks partly to the Irish diaspora, created by a century and a half of emigration, the country has far more clout than its small population might suggest. It had a notable stint on the United Nations Security Council in 2001-02. And Europeans were impressed by the Irish presidency of the European Union in the first half of this year, which took in not only the eastward expansion of the EU and the choice of a new commission president, but also a deal on a new EU constitutional treaty, brokered by the Irish taoiseach (prime minister), Bertie Ahern. On a less elevated level, the main streets of cities the world over feature "Irish pubs" serving draught Guinness.

Over the border, Northern Ireland, which has a population of 1.7m, offers a valuable case-study in how to resolve an entrenched terrorist problem. The peace ▸▸

Acknowledgments
As befits a literary nation, there is a vast literature on Ireland. This survey draws especially on "Modern Ireland 1600-1972" by R. F. Foster (Penguin), "The Transformation of Ireland 1900-2000" by Diarmaid Ferriter (Profile Books), "Reflections on the Irish State" by Garret FitzGerald (Irish Academic Press), "The Making of the Celtic Tiger" by Ray MacSharry and Padraic White (Mercier Press), "Breaking the Bonds: Making Peace in Northern Ireland" by Fionnuala O'Connor (Mainstream), the OECD's July 2003 survey of Ireland and "Catching Up With The Leaders" by Patrick Honohan and Brendan Walsh (Brookings Papers on Economic Activity, 2002). The author would like to thank all those who generously made themselves available for interview, not all of whom are cited in the text.

An audio interview with the author is at **www.economist.com/audio**

A country briefing on Ireland is at **www.economist.com/Ireland**

process in the province remains partial, bumpy and incomplete (only last month British, Irish and Northern Irish leaders failed yet again to agree on a precise formula for the revival of devolved government in Belfast). Yet ten years of painstaking diplomacy, by both the British and the Irish governments and by politicians and paramilitary leaders on both sides of the sectarian divide in the north, have largely put an end to the violence that for two decades disfigured Northern Ireland. Other countries with intractable terrorist problems might take note.

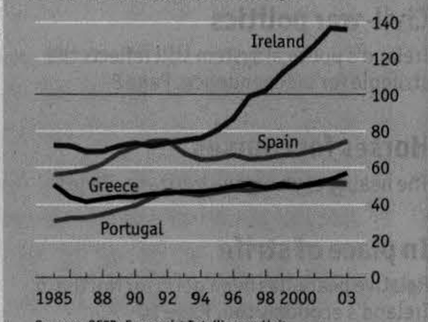
Peace in Northern Ireland has helped to boost the economy of the whole island. A visitor to Dublin, so lively and cosmopolitan today, would find it hard to believe that only a few decades ago it was gloomy and depressed. In the 1960s Ireland's heavily agricultural economy, almost wholly dependent on exports to Britain, was only just emerging from the misguided protectionism that since the 1930s had been the main plank of Eamon De Valera's ill-advised economic policy. Ireland had missed out almost entirely on Europe's post-war boom; living standards were stagnating and emigration was in full flow. In 1960 the republic's population was down to around 2.8m, the lowest in two centuries and a pale shadow of the 8m (for the whole island) in 1840, when this was one of the most densely populated countries in Europe. Many wondered if Ireland had a future.

In fact, the 1960s proved something of a turning-point. Corporate tax on foreign multinational companies investing in Ireland was cut to zero in 1957. Belatedly, the country embraced free trade with Britain and, by joining the European Economic Community in 1973, with much of the rest of Europe. The combination of zero corporate taxes, a low-wage economy inside the EEC and a shared language proved a strong lure for American manufacturers. Ireland's long love affair with foreign direct investment (FDI) began in the 1960s. Free secondary education for all arrived in 1967, and after 1973 Irish farmers benefited from Europe's munificent farm subsidies.

This promising start, however, was kyboshed by the two oil shocks of the 1970s, and even more by a knuckle-headed policy response. Successive Irish governments sought to offset the cut in living standards imposed by higher oil prices through fiscal and monetary expansion. The result, ultimately, was the high inflation, high unemployment, slow growth and even electoral instability that marred the 1980s. Emigration, especially of graduates, hit new highs. At the start of the third Haughey government in 1987, a grim joke made the rounds: would the last Irishman to leave please turn out the lights? Yet only a few years later the Irish miracle had arrived. What caused it? Can it be replicated? And can it last? ■

Leader of the pack 1

GDP per head as % of EU15 average



Sources: OECD; Economist Intelligence Unit

Tiger, tiger, burning bright

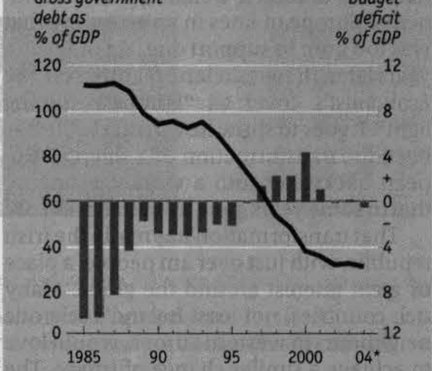
An economic miracle with many causes

THE figures recording Ireland's transition from Europe's worst- to its best-performing economy are remarkable. In 1987 Irish GDP per person was 69% of the EU average (adjusted to EU 15); by 2003, it had reached 136%. Unemployment fell from 17% in 1987 to 4% in 2003; and government debt shrank from 112% of GDP to 33% (see chart 2). Annual GDP growth in the decade of the 1990s averaged a tigerish 6.9%; GNP growth, usually a more appropriate measure for Ireland (see box, next page), only slightly less. Perhaps even more impressive, after a downward blip coinciding with the American and, especially, the information-technology (IT) slowdowns in 2001-02, the economy is bouncing back: growth both this year and next is expected to be around 4-5%.

Not surprisingly, this Celtic miracle has been carefully analysed. Many different, and sometimes contradictory, explanations have been proposed, but as usual there is no single cause: it was a combination of different factors at different times.

To get a more complete answer, it also helps to ask a different question altogether. Seen in a historical context, what is striking about Ireland is not that it grew so spectacularly in the 1990s, but that it did so badly in the 1980s, and indeed for a long time before then. At independence in 1922, Ireland was as rich as most European countries, and only a bit poorer than Britain. But by 1960 it had fallen far behind, and continued to lag the rest of Europe until the late 1980s. On this reading, the emergence of the Celtic Tiger was a belated catch-up after years of underperformance.

Payback 2



Source: OECD *Forecast

There were, nevertheless, a number of special factors that changed Ireland's fortunes after 1987. Here are some, in ascending order of importance:

- **Fiscal and monetary consolidation.** Charles Haughey's Fianna Fail government, crucially supported by the opposition Fine Gael, started to cut spending, taxes and borrowing. Falling interest rates helped to stimulate the economy, and so did a currency devaluation in 1993. The launch of the euro in 1999 gave Ireland, a founder member, the benefit of lower—perhaps unduly low—interest rates.

• The tax cuts were also a critical component of a new **social partnership.** Unlike Britain, where the Thatcher government shifted decisively against corporatism, the Irish resuscitated social dialogue in 1987, with trade unions accepting wage restraint in exchange for more policy influence and tax cuts. Seventeen years on, unions and employers still talk up the advantages of social partnership. Even the tanaiste (deputy prime minister) and leader of the free-market Progressive Democrats, Mary Harney, considers this an important part of Ireland's success.

• **European Union subsidies.** Countries such as Germany, the chief EU paymaster, like to argue that Ireland's miracle was due to huge transfers from Brussels. Yet European money had been pouring into Ireland since 1973, at first to little obvious effect. The expansion of the EU's structural funds after the Maastricht treaty of 1992 was helpful, but even then transfers never exceeded 5% of Irish GDP, a far smaller proportion than, say, west German transfers to east Germany. The most authoritative studies suggest that EU subsidies may have added around 0.5% a year to growth during the 1990s—useful, but modest in the context of average growth of 6.9%.

• More important than EU money may have been the 1992 programme to create a **European single market.** As a big low-cost exporter to Britain and the rest of Europe, Ireland benefited from more open access. EU subsidies also played another indirect part: by requiring a planned capital programme some years ahead, they helped to protect badly needed infrastructure projects from the cuts imposed in response to the fiscal pressures of the 1980s.

• **Ireland's FDI boom.** A number of foreign manufacturers invested during the 1960s, lured by the country's low costs and zero corporate-tax rates. Among them were such high-tech companies as Polaroid and Digital Equipment. But by the 1990s they had pulled out, as did Gateway, a PC-maker. By then, after complaints from the EU, the corporate-tax breaks had become less generous (from this year the rate for all companies is 12.5%). But Ireland's Industrial Development Authority (IDA) had become good at attracting desirable companies, and it proceeded to win big FDI projects in such businesses as software, semiconductors, personal computers, pharmaceuticals and medical devices.

• **Education.** One of Ireland's bigger attractions was a ready supply of skilled workers, including scientists, engineers and business-school graduates. As far back as the 1960s, the country had been investing heavily in both secondary and higher education. Dublin's two main universities, but also those at Cork and Galway, and a new one at Limerick, became crucial to the IT, pharmaceutical and health-care companies that invested in those regions.

• **Low personal taxes.** In the 1960s and 1970s, high income-tax rates, and a high tax burden in general, discouraged domestic growth, but from the early 1990s taxes started to come down sharply, giving a big boost to home-grown enterprise. Des

Measure for measure

The tangled tale of GDP and GNP

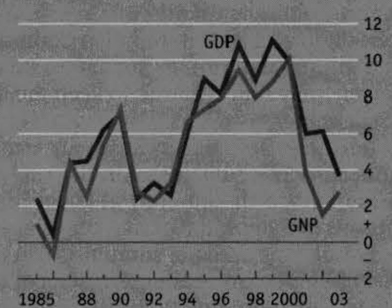
Any first-year economics student knows that national-income figures can be collected in three different ways, using income, output or expenditure numbers. Although the three are supposed to produce the same result, they rarely do. But the differences are tiny compared with a more obscure oddity that affects the Irish economy: the huge gap between gross domestic product (GDP) and gross national product (GNP).

GDP is the more common measure of national income, to which GNP adds an item known as net transfers of factor incomes. This means adding the overseas profits of Irish companies that are repatriated to Ireland, and subtracting the profits of foreign multinationals operating in Ireland that are sent abroad. In most countries the two numbers will be small, and may also broadly balance out. But because of Ireland's large FDI base, coupled with its enticingly low corporate taxes, lots of big foreign companies make (or at least report) big profits in Ireland which they transfer back to their head offices. As a result, Ireland's GNP is as much as 25% smaller than its GDP.

What this means in practice is that GDP figures overstate the national income available to Irish people to spend. Ireland's diplomats in Brussels wised up to this long ago. When they want to crow about the brilliant economic policies that created the Celtic Tiger, they use the GDP figures, noting proudly that Irish GDP per person is now the third-highest in the EU,

Widening gap 3

% change on a year earlier



Source: National accounts

well above Britain's. However, when the talk turns to EU regional subsidies, the diplomats switch to the "more appropriate" GNP measure, which puts Ireland close to the EU average, and mutter about the country's huge infrastructure backlog.

As the Irish economy develops, GDP and GNP might be expected to converge, but instead the gap seems to have widened recently (see chart 3). That is largely because American multinationals have been racking up (or at least recording) such big profits in Ireland. In some ways, this is a mark of the country's economic immaturity, and its failure to nurture indigenous industry. Chris Coughlan, a vice-president of HP Compaq and chairman of the Galway Chamber of Commerce, suggests that Ireland's future success could be measured in part by whether GDP and GNP converge, which would indicate that home-grown industry has matured. That might, sadly, put an end to another splendid quirk with which to confuse those first-year students: that Ireland's total exports exceed the country's national income.

Enjoying the boom while it lasts

O'Malley, who quit Mr Haughey's Fianna Fail party to found the Progressive Democrats in 1985, says that lower income-tax rates were key to the Irish miracle.

• **Demographics**. The baby boom in Ireland lasted longer than in the rest of Europe, and there were fewer elderly pensioners because emigration in the 1950s and 1960s had been so heavy. Where other European economies were facing a rapidly ageing population, Ireland has been boosted by its youthfulness. Ireland's population has been growing strongly for 13 years now, helped also by an end to the net outflow of people and the start of an inflow.

• The biggest contribution to the Irish miracle, however, came from **more people working**. Until the 1980s, women's participation in the workforce was low by international standards; today it is above average. Conversely, Irish unemployment was high, at around 17% in 1987; today it is 4%. All in all, the labour-force participation rate in Ireland has risen from around 60% in the 1980s to almost 70%. The absolute numbers of those in work rose from 1.2m in 1993 to over 1.8m ten years later. On some estimates, this accounts for half of Ireland's growth in the 1990s.

Unrepeatable

Does it matter which of these explanations for Ireland's success counts for most? Yes, for two reasons. The first is that many of them were one-offs. European subsidies, for example, are a thing of the past now that Ireland has become one of the EU's richest countries. Likewise, the stimulus to growth from the lower interest rates that came with the European single currency will not be repeated. And the sharp rise in labour-force participation is over and done with. Although the Irish population remains relatively young, it is beginning to look a lot more like that of the rest of Europe, with a falling birth rate and a rising proportion of old people.

The conclusion is stark: much of the Irish miracle (ie, higher output) was attributable to one-off changes (ie, greater input) and not to productivity growth (ie, more efficient use of that input). In effect, an economy that was suffering from 50 years of inefficiency, poor organisation and under-use of inputs (especially female workers) has spent the past 15 years catching up with more efficient, better-organised neighbours. Now it needs to find ways to keep the momentum going.

The second reason why there is so much interest in the secret of Ireland's success is that many countries in central and eastern Europe want to emulate it. This will not be easy. Some may be able to increase their female labour-force participation, but most will find their demographics a hindrance rather than a help. They can aim for better education, more foreign direct investment and fiscal and monetary consolidation, but such measures take years to produce results.

The new EU members will also discover, as Ireland has already done, that the world has become a lot more competitive. Ireland has some useful advantages to help it stay ahead, but it also faces serious short-term problems, such as the state of some public services and a dangerous obsession with property. ■

Why worry?

The economy has some weaknesses—but several strengths too

IF THE Irish miracle materialised so quickly, might it as suddenly vanish again? The country faces more intense competition than it did, often from lower-cost rivals that are becoming equally adept at attracting FDI, investing in education and encouraging indigenous industries. But there are also more specific concerns.

Some of the biggest are macroeconomic. Ireland's fiscal position, which in the 1980s put the country in danger of default, is today enviably healthy. But a pre-election spending splurge in 2001-02 has had to be sharply cut back; and the country still needs to spend a lot more on infrastructure. The long-serving, tough-minded finance minister, Charlie McCreevy, has gone off to a job in the European Commission in Brussels, and his successor, Brian Cowen, may find it harder to keep the lid on spending.

Ireland also suffers from an acute monetary-policy dilemma. In the run-up to the launch of the euro in 1999, Irish short-term interest rates were cut sharply. The result was an extra stimulus to an already fast-growing economy, a burst of renewed inflation and a further ratcheting-up of property prices, especially in the Dublin area. The subsequent depreciation of the euro made matters worse. Fortunately, a sclerotic European (and, by 2001, world) economy held prices down, so that inflation has remained relatively low, although higher than elsewhere in Europe. But interest rates, set in Frankfurt by the European Central Bank, are still far lower than Ireland would choose for itself.

Higher inflation than in rival countries means that Irish competitiveness is being steadily eroded. Moreover, if the euro appreciates further against the currencies of Ireland's two biggest trading partners, America and Britain, Irish exports will be hurt. Even more serious, low interest rates ▸

have helped to cause a property frenzy, particularly in the greater Dublin area, in which average house prices have quadrupled over the past decade, with household debt expanding to match.

Ireland is not the only country to have experienced a housing bubble in recent years. But it may be peculiarly vulnerable, because as a member of the euro area it cannot raise interest rates in order to prick the bubble. Moreover, in the past decade or so property and construction have become unduly dominant in the economy (and in politics too, see next article). This year, for example, Ireland is on course to build almost 80,000 new houses. Britain, which has 15 times as many people, builds only twice as many. Employment in construction has almost doubled in the past decade, and the sector accounts for some 15% of national income—over twice as much as in Britain.

Ireland is also exposed to property prices abroad. The Irish, like the British, have always liked property portfolios. Various London landmarks, such as Claridge's, the Connaught hotel and the Unilever building, are Irish-owned. The banking system is heavily exposed: the big Irish banks, such as Bank of Ireland and Allied Irish, are in effect mortgage banks, observes Colm McCarthy of DKM Economic Consultants. A property crash would badly hit their balance sheets.

The dominance of Dublin is another risk factor. The city and its region contain almost a third of the Irish population and generate close to 40% of GDP. Dublin is also a surprisingly spread-out city, with low-density Georgian streets at its heart, big parks and almost no high-rise buildings. Two consequences are giddy house prices and long commutes for those who cannot afford to pay them.

Clearly there are big risks ahead, with a property crash perhaps the most threatening. But the gloom can be overdone. Ireland also has a number of plus points that should help it grow rapidly.

The big magnet

For a start, there is an impressive FDI machine, led by the IDA but with help also from Science Foundation Ireland, Forfas and Enterprise Ireland, which fosters indigenous industry. The IDA is a world-class agency, able to compete not just with the rest of Europe but with places such as Singapore and Taiwan for valuable projects in pharmaceuticals, biochemistry, IT and medical devices. Its roster of satisfied investors, mostly but not exclusively from America, remains impressive.

Ireland takes roughly one-quarter of all American FDI in Europe. It now has over 1,100 multinational companies, which export goods worth some $60 billion a year. In certain sectors it is pre-eminent; for example, it takes almost one-third of all FDI in Europe in pharmaceuticals and health care. Nine of the world's top ten drug companies are present (the republic produces most of Europe's supply of the drugs Viagra and Botox). One-third of all personal computers sold in Europe are manufactured in Ireland. The country is the world's biggest software exporter, ahead of America. And Dublin's International Financial Services Centre, about which many were once sceptical, has become a big success, employing some 16,000 people.

The companies that have come to the emerald isle seem delighted with it. At Leixlip, west of Dublin, Intel has invested some $5 billion in its biggest semiconductor plant outside America; it has just started operating Fab 24, the most advanced chip-making facility in the world. Wyeth has chosen Dublin as the site for one of the world's biggest bio-pharmaceutical centres. Dell's personal-computer plant in Limerick is one of the company's most productive. HP Compaq is the biggest employer in Galway, with its main plant on the site of the Digital Equipment venture that went wrong in the 1990s. Apple has chosen Cork for its chief European software-development and support centre, although it has shifted most manufacturing to the Czech Republic and Taiwan.

The Apple story is a symbol of a broad change. As Joe Gantly, its outgoing vice-president, notes, in 1997 the company employed 1,800 people in Cork, 90% of them in manufacturing. But as Ireland saw its low-cost advantage erode over the next few years, most of those jobs were lost. Instead, Mr Gantly persuaded the firm to move into higher-value-added operations, concentrating most European support services and research in Cork. Today it employs just over 1,400 people there, most of them skilled graduates; only 15% of them are in manufacturing.

Brains in clover

That, writ large, is what the country now has to do. At Science Foundation Ireland, Bill Harris uses public money to lure top scientists and researchers to Ireland. His goal, he says, is to make Ireland "science-friendly and friendly to scientists". Many of his targets are Americans with Irish roots, rather like himself. He trumpets the recent investment by Bell Labs in top-end research, and he works closely with universities. University heads such as John Hegarty at Trinity College, Dublin, and Hugh Brady at University College, Dublin, have spent time in America and brought back an American fervour for links between universities and high-tech industry.

Gerry Wrixon, president of University College, Cork, is typical of the breed. After graduate work and an academic career in America, he came back home to run Ireland's National Microelectronics Research Centre before moving on to UCC, where he seems to spend as much time on links with business and industry as on students. He sees Stanford University and its relationship with Silicon Valley as a model to aspire to, and unabashedly proclaims that, if a university is to thrive, it must be a research-based, elite institution. It is a far cry from the mass universities, with poor links to local industry, that are the norm in continental Europe.

The universities are also integral to another big challenge for Ireland, which is to foster home-grown industry. There are few well-known big Irish companies beyond the Kerry Group (foods), CRH (building materials), Jefferson Smurfit (paper and packaging) and Ryanair. And none is in the booming sectors that dominate FDI in Ireland, notably IT, health care and pharmaceuticals. Such firms as Elan (drugs) or IONA Technologies are successful but small (and Elan has had a big accounting scandal). Yet a growing venture-capital industry is spawning new companies. One example is Multis in Galway, a "re-manufacturer" of computer parts for HP Compaq and Sun Microsystems. The ▸▸

country needs more firms of this sort if it is to stay ahead.

It also needs a strongly pro-business government. The 1980s taught politicians from all sides the folly of high taxes, extravagant spending and other anti-business policies. The present Fianna Fail-Progressive Democrat coalition, led by FF's Bertie Ahern as taoiseach, but with the formidable Mary Harney as tanaiste in charge of industry and enterprise, and Charlie McCreevy as finance minister, has won plaudits from Irish and overseas businessmen alike. In EU meetings, Ms Harney and Mr McCreevy have become renowned for fighting for economic reform and against tax harmonisation—their keenest allies being the British.

Ms Harney recently took delivery of a new report on enterprise strategy by a committee chaired by Eoin O'Driscoll, managing director of Aderra, which argues not only for more emphasis on high-value-added sectors and scientific research but also for greater efforts in keting and promotion, in which Ir has been weak. She wants to push thr the report's recommendations, and t Ireland needs the spur of more co tition if its domestic industry is to pro

But Mr McCreevy has gone to Bru Ms Harney has now taken the health folio, and Mr Ahern's low popularit put him under pressure to shift leftv Suddenly Irish politics has become important for the country's economy

Civil-war politics

Ireland's political system still reflects the struggle for independence

ALL countries are shaped by their history, but in Ireland, south and north, history is ever-present and inescapable. Other things being equal, knowledge of the past is surely a plus. But other things are not always equal, and the trouble in the north caused by commemorations of battles fought several centuries ago invites the question whether a country can have too much history. Certainly, history has shaped Ireland's main political parties.

Most European countries have a centre-left (broadly socialist) party and a centre-right (broadly conservative or Christian Democrat) one, perhaps with some liberals in the middle, plus a green party and a few regional or fringe ones thrown in for a dash of colour. Ireland's parties do not conform to this model (nor do Northern Ireland's, see next article). The political differences between the two main parties, Fianna Fail and Fine Gael, can be hard to detect. As a telling piece of evidence, try asking a political insider in Dublin where the parties sit in the European Parliament: the odds are that he will not know. (Answer: Fine Gael is part of the centre-right European People's Party, and Fianna Fail sits, bizarrely, in the Europe of Nations group, with Italy's former fascists and the anti-EU League of Polish Families.)

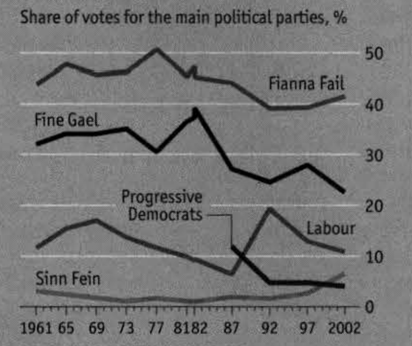
The main point about the two parties is not what they stand for now, but that their forebears fought each other in the civil war of 1922-23. Fianna Fail was founded by De Valera, who opposed the treaty of independence, whereas Fine Gael emerged from the party that supported it. If Ireland has a natural party of government, it is Fianna Fail. It has been in government for 54 of Ireland's 82 years of existence and has long had the biggest share of the vote (see chart 4). It touched a moral low under Charles Haughey in 1987-92, when ministers were taking cash from property and construction interests. That period is now under minute scrutiny in a string of official tribunals.

The tribunals are likely to produce further embarrassing revelations, mostly about Fianna Fail politicians. And yet the party seems to have escaped the worst of the fallout. Indeed, it is in government again, under Bertie Ahern, who has been taoiseach since 1997. This time, shrewdly, he has formed a coalition with the Progressive Democrats, a free-market liberal party led by Mary Harney.

To an outside observer, Mr Ahern personifies the Irish politician. He is a cheerful, ruddy-cheeked man with the gift of the gab, a ready handshake for potential voters and a big smile at such exuberant events as the Galway races (see box, next page). So far his government has proved

Civil-war relics 4

Share of votes for the main political parties, %



Source: Parties and Elections in Europe

surprisingly robust, serving out a full in 1997-2002 and on course to serve o other before the election due in 200 Ahern has become a close friend an of Tony Blair, Britain's prime ministe two have devoted much time to tryi a peaceful settlement in Northern Ir Mr Ahern's government has also cut and, except in 2001-02, held down p spending. Ms Harney is a doughty pion of tax cuts, who claims that tions in corporate and capital-gains have actually produced higher rever

Unloved

Unfortunately the Ahern governm now having to cope with an acute at mid-term blues. The fear is that Mr will try to make himself more popu shifting leftwards and letting spending rip, yet the taoiseach insis he is not changing course. He point government's tough action in 2002 public spending, which has be warded with renewed growth. He about to change tack and jeopard government's economic record maybe risk losing the Progressive crats from his coalition as well).

Instead, he talks of two big cha ahead. The first is the need for an that has shed much of its cost advan shift further towards services an tech industry. The second may b tougher: to reform public services. in part to its inheritance from Brit Irish civil service is efficient and, l standards, free of corruption. But, where, public services are insuffici sponsive to customers and often fa liver value for money.

The boom years of the Celtic Tiger allowed the country to pour money into education and health care. Mr Ahern points out that annual public spending on health, education and welfare combined has risen from €9 billion in 1997 to €26 billion ($32 billion) now. Public-service workers have also benefited from a "benchmarking" exercise that, under the guise of keeping public-sector pay competitive, has made it harder to control spending.

Mr McCreevy notes that health spending alone has tripled during his time as finance minister, from €3.5 billion to over €10 billion, with the numbers of front-line staff rising from 58,000 to 96,000. Yet as other countries are finding, what matters in health care is not necessarily spending more money, but getting a more efficient service. And here Ireland is behind the rest of Europe: doctors remain unaccountable, patients are not treated as consumers, choice is limited, and many hospitals are too small to be effective. Reform will be a challenge even for the tough Ms Harney to deliver, not least because Ireland's multi-member constituencies, combined with its peculiar system of proportional representation, give local issues (such as closing hospitals) undue political weight.

Mr Ahern has also made enemies in the civil service by proposing to move entire departments out of Dublin. This attempt at decentralisation has run into fierce opposition, and not just from senior officials who have no desire to go. Ed Walsh, who established the University of Limerick, has become a vocal critic, arguing that intelligent policymaking across departments becomes impossible if they are physically far apart. A better idea might have been to put the capital in another place, but that would be unpopular with the politicians. Mr Ahern insists that he will stick to his decentralisation plans, though he is willing to negotiate over details and timing.

What of the opposition parties? Fine Gael has changed leaders repeatedly since Garret FitzGerald was taoiseach in the 1980s. The current incumbent, Enda Kenny, has yet to make a big impression, but the party did well in June's European and local elections, when Fianna Fail got its lowest share of the vote since the 1930s. When Fine Gael was in office in 1994-97, under John Bruton, it was in a "rainbow" coalition with Dick Spring's Labour Party; the two parties now talk openly about roping the Greens into a future coalition.

Even so, no opposition party finds it easy to attack the Ahern government. Labour's leader, Pat Rabbitte, admits that Fianna Fail has reinvented itself as a modern progressive party since Mr Haughey's day, but he hopes that revelations from the tribunals may dent the party's support.

Eyes right for Ahern

All parties are, however, worried by a new factor in Irish politics: the rise of Sinn Fein, the political wing of the Irish Republican Army (IRA). As the main pro-independence group, Sinn Fein set up Dail Ei- ▸▸

Horses for courses

The beauty of an equine heritage

IT IS late July in Galway, and there is not an empty hotel room or bar stool in sight. The annual Galway races, one of the top spots in the Irish social calendar, are also a big political occasion: the Fianna Fail tent at the races heaves with property developers and other campaign contributors. The races themselves often seem less important than the champagne (this is not the place for Guinness), the talk and the wheeling and dealing. Senior Fianna Fail ministers, among them Bertie Ahern, the taoiseach, spend whole days at the Galway races.

The presence of Fianna Fail's top brass reflects the party's populist roots as well as its need for money, but also something else: the importance of the horse in Ireland. The whole island stages over 300 race meetings a year, a 20% rise on a decade ago. Attendances have also gone up, by over 25% to some 1.4m. The green countryside of Ireland is now pleasantly pockmarked not just with racetracks but also with smart-looking stud farms.

But the business may not be quite as clean as it looks. There have been betting and race-fixing scandals over the years. Last November, Ireland's biggest stud-farm owner, John Magnier, hit the headlines when the manager of Manchester United football club, Sir Alex Ferguson, sued him over the stud earnings of a racehorse called "Rock of Gibraltar" in which he had been given a half-share. What made the case awkward was that Mr Magnier, with another rich Irishman, has a 29% stake in Manchester United.

But the biggest scandal is that super-rich stud-farm owners benefit shamelessly from an exemption from both income and corporate taxes. Ireland openly uses this exemption as an enticement to outsiders. Its share of Europe's thoroughbred stud industry has risen to over 40%, whereas Britain's has fallen sharply. The industry pleads that it contributes more to the Irish exchequer than the value of taxes forgone because it generates employment and wealth. But the European Commission is now investigating whether the tax exemption constitutes a form of illegal state aid.

Observers note two delicious ironies. One is that the EU single-market commissioner in charge of the investigation will be none other than the ex-finance minister, Charlie McCreevy, who is not only a dedicated race-goer but also gained notoriety for pouring public money into the struggling Punchestown racecourse, which happened to be in his constituency. The other is that Ireland's biggest foreign high-tech investment, the Intel plant at Leixlip near Dublin, was built on the site of a bankrupt stud farm.

reann, the Irish parliament, in 1919. But after the civil war and the establishment of Fianna Fail and Fine Gael, it was eclipsed, even though the IRA remained active. Now, however, Sinn Fein has grown to become the biggest nationalist party in the north, where it confronts Ian Paisley's Democratic Unionists. Less noticed overseas, Sinn Fein has also garnered support south of the border, where it now commands getting on for 10% in opinion polls.

From which party is Sinn Fein drawing its support? Most of its followers are urban and relatively poor, so they have probably come partly from Labour and partly from Fianna Fail. The leaders of these two parties say that Sinn Fein will hit a natural ceiling of a bit less than 15%. That may seem small; yet as Michael McDowell, the (Progressive Democrat) justice minister, observes, Sinn Fein's platform is essentially a Marxist one. Besides, it still has an armed wing, in the shape of the IRA. Both Mr Ahern and Mr McDowell pointedly note that Sinn Fein is surprisingly well-organised and financed, and Mr McDowell openly questions the source of the party's money. Asked what single action might do most to reduce its income, he suggests that equalising diesel taxes on both sides of the border would have a salutary effect because it would cut smuggling.

It is possible that Sinn Fein might mature into a legitimate nationalist party: were it ever to be considered as a potential partner in a coalition government, it would have to. But even in its present guise, as a neo-Marxist party with guns, it will not disappear. Its new-found respectability has become part of the price that both parts of the island have had to pay for ten years of peace in Northern Ireland. ■

In place of strife

Relative peace has been good for Northern Ireland's economy too

BELFAST, like Dublin, has been transformed over the past 15 years. It used to be a bleak, partly bombed-out shell of a Victorian city, festooned with barbed wire and full of nervous soldiers in armoured vehicles. Now its centre is a bustling, lively place full of shops, offices, restaurants and theatres. Beyond the centre, admittedly, lie stark reminders of the province's sectarian tensions, most obviously the ugly graffiti-strewn walls that physically keep apart the divided Protestant and Catholic communities in the west and north. But overall Northern Ireland has changed sharply for the better—just like the republic.

The big difference is that the primary agent of change in Northern Ireland has been not economics but peace. The Irish Republican Army declared a ceasefire in 1994, after a 25-year campaign in which some 3,000 people were killed. That ceasefire has been mostly stuck to. The Good Friday agreement of April 1998 was later approved by referendums in both parts of the island. It led not only to the republic amending its constitution to drop its territorial claims on Northern Ireland but also to the restoration of devolved government at Belfast's Stormont. Sinn Fein, the IRA's political wing, joined in for the first time, with its former chief of staff, Martin McGuinness, somewhat incongruously serving as education minister.

Northern Ireland's devolved government has since been suspended several times, usually because Unionist parties wanted more progress in decommissioning IRA weapons. The most recent suspension, in October 2002, came after a scandal when Sinn Fein was found spying on Northern Ireland Office ministers and other parties at Stormont. Since then, attitudes across the divide have hardened.

In elections in 2003, the Catholic, nationalist vote shifted from the moderate Social and Democratic Labour Party (SDLP) to Sinn Fein, led by Gerry Adams. The Protestant, Unionist vote also moved, from the Ulster Unionists to the harder-line, anti-agreement, Democratic Unionist Party (DUP), led by Ian Paisley. The two (moderate) Nobel peace-prize winners, John Hume of the SDLP and David Trimble of the Ulster Unionists, have been sidelined (and Mr Hume has stood down).

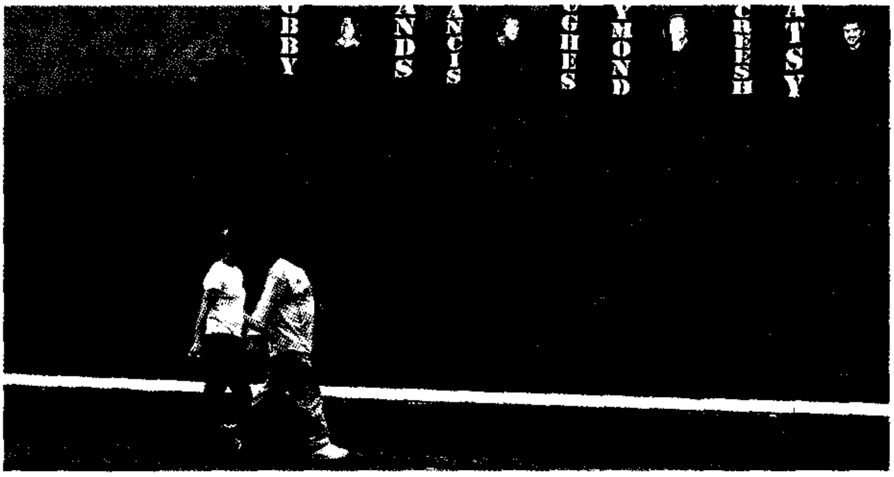
This polarisation towards the extremes helps to explain the failure of the latest attempt to reach agreement on restoration of devolved government, at a summit meeting of the British and Irish governments and Northern Irish political leaders at Leeds Castle last month. But there are grounds for optimism, even for hoping for a total disarmament of the IRA. Nobody involved wants to go backwards to the years of the Troubles, when the IRA (and loyalist paramilitaries) were bombing and killing in both province and mainland. Moreover, it may, oddly, be easier to forge peace in Northern Ireland if the two main protagonists represent the extremes of the sectarian divide.

Economics follows the peace

The unsung hero of the past decade in Northern Ireland has been the economy. Its performance has been a lot less spectacular than that of the Celtic Tiger next door, but Northern Ireland in the 1990s still grew faster than any other region in Britain. Growth has slowed in recent years, but unemployment is down to just over 5%, which puts it in the middle ground among British regions. Few would have predicted a decade ago that what was then the basket-case of the British economy would soon have lower unemployment than London, the west Midlands, the north-east and Scotland.

Yet there are also economic clouds hanging over Northern Ireland. Its manufacturing base continues to shrink, a change that matters more than in the republic because the six counties were always the most heavily industrialised part of the island. The linen, textile and shipbuilding industries are a shadow of their former selves (the cranes at Harland & Wolff, where the *Titanic* was built, now look down on a science park). Employment in manufacturing has fallen from almost 200,000 two decades ago to under 100,000 now.

Even more serious is the economy's dependence on the public sector. Philip McDonagh, chief economist at PricewaterhouseCoopers in Belfast, reckons that the public sector accounts for some 65% of GDP in Northern Ireland. That share has remained steady even as security and police spending has fallen, because public spending elsewhere has been expanding so fast. But that is unlikely to continue. In any case, the economy needs more private enterprise, and especially more high-technology, high-value-added businesses and, above all, services. Tourism, for instance, is ▸▸



In the bad old days

feeble, contributing less than 4% of GDP, compared with about 6% in the republic and 7% in mainland Britain.

Partly because it is so big, the public sector is also inefficient. Schools do better than in mainland Britain, but health care needs rationalising. There are 26 district councils for a population of only 1.7m. Insiders reckon that the number could be shrunk to four or five, though that might be politically tricky. All efforts to trim employment in the civil or public services tend to generate fierce resistance.

Is an all-island economy in the making? One answer is that trade across the border remains underdeveloped. InterTrade Ireland, one of the six cross-border bodies set up after the Good Friday agreement, is trying to foster more. Over the past five years, the value of cross-border trade has doubled in real terms, says Liam Nellis, its chief executive. But one-third of it consists of food and live animals. Obstacles to greater all-island trade include currency, tax and infrastructure differences. Were Britain to join the euro, trade across the border might rise sharply. Yet the biggest problem, says Mr Nellis, is lack of knowledge and of personal contacts.

In the end, though, the fortunes of Northern Ireland depend most of all on a continuation of the peace process. Business surveys since the suspension of Stormont in October 2002 have been getting gloomier. For the most part, government and business are able to work quite happily without the assembly and devolved government. But so long as there is a question-mark over peace, some businessmen and foreign investors will hold back. ■

A European country like any other

Ireland's economic success has helped its society to grow up

THE stereotype of Irish backwardness 30 or 40 years ago had much truth in it. The influence of the land was strong in a country where as late as 1973 one-quarter of the population was engaged in farming. In De Valera's time the Catholic Church's power was vast, and it lingered on into the 1980s. No politician could contemplate proposing a law without winning the approval of the Catholic hierarchy. Divorce, abortion and most forms of birth control were in effect illegal. Education was patchy at best: even into the 1960s, people had to pay for secondary schooling.

Irish society was also deeply patriarchal. Women were second-class citizens who were expected to stay at home and have babies. Many husbands would go abroad for long periods to work, and immigration was almost unknown. Ireland continued to define itself largely against Britain, by far its biggest trading partner and the recipient of most of its emigrants. The great famine of the 1840s proved an enduring influence.

But as the country has become richer over the past two decades, all this has changed. Divorce was legalised only in 1995 and abortion remains illegal in most circumstances, but Irish family life has evolved to look more like the rest of Europe's. The birth rate has tumbled, and many more married women are at work. The abortion rate is estimated to have risen from around 4.5% of pregnancies in 1980 to over 10% in 2002 (mostly carried out in Britain); over the same period, births out of wedlock have soared from 5% to 31% of the total. The divorce rate is creeping up.

Crime and violence are on the rise. Ireland has turned from a country of emigration into one of immigration, and although as many as one-third of the immigrants have Irish roots (or are former emigrants returning home), many now come from farther afield and look recognisably foreign in Dublin's streets. The country has also had a big influx of people from central and eastern Europe. In restaurants and bars, even in cities such as Cork and Galway, the staff often hail from such countries as Slovakia or (non-EU) Croatia.

As for religion, although almost 90% of the population still claim that they are Catholic, the Catholic Church is not the force it was. It fought hard against the legalisation of divorce, but lost decisively. It is hard to imagine the church in its heyday tolerating a taoiseach living with a woman who was not his wife, as Mr Ahern did for many years.

Like its counterpart in America, the Catholic Church in Ireland through the 1990s was beset by a series of sex scandals involving priests and boys, or children's homes run by religious orders. One bishop had to resign after seeming to cover up for abusive priests. Some 18 religious orders were landed with compensation bills that may reach €128m (though the state helped by taking on all additional liabilities).

The new Archbishop of Dublin, Diarmuid Martin, who recently returned to Ireland after long service abroad, concedes that the church has gone through difficult times, but insists that it is still one of the strongest in Europe. In many ways he welcomes "modernisation": in particular, the ending of the church's long entanglement with politics. The archbishop sees a big role for the church in tackling Ireland's growing social problems: he notes more violence, more drug and alcohol abuse, and greater selfishness than before he went abroad.

Yet the church suffers from long-term weaknesses. As with the Protestant Church of Ireland, which claims about 5% of the population, congregations and priests alike are ageing. Archbishop Martin recalls that when he was ordained in the diocese of Dublin in 1969, there were 13 other ordinands. Last year there was one. ▸▸

Next year, there will be none. The archbishop says he does not want to preside over a dying church; he talks ruefully of Catholicism becoming a "minority culture" in Ireland. In many ways, after years of sectarian conflict, religion now plays a bigger role north of the border.

It is not only churchmen who regret Ireland's growing secularism. David Quinn, a journalist at the daily *Irish Independent*, points to rising drug and alcohol consumption, a sharp increase in suicides, a greater incidence of sexually transmitted diseases and a growing "yob culture". He suggests that with the decline of religion, society has lost a moral compass.

Yet Michael McDowell, the thoughtful Progressive Democrat justice minister, says it would be wrong to hanker after the good old days: "They weren't that good." The social changes that attract criticism are common across Europe, he suggests. And curtailing people's liberties would be the wrong response. Admittedly, Ireland earlier this year became the first EU country to ban smoking in pubs and restaurants, but the government sees that as a health issue, not a matter of civil liberties.

Left-leaning commentators criticise the government for presiding over rising poverty and inequality. Much fuss was made over a recent UN report suggesting that Ireland had become more unequal during its tiger years, and was now one of the most unequal countries in Europe. The figures are a matter of dispute, but in any event Mr McDowell offers a robust defence. Fifteen years ago, he says, political conversation was about economic failure and poverty. Since then, absolute poverty has fallen sharply. He sees inequality as an inevitable part of the society of incentives that Ireland has, thankfully, become.

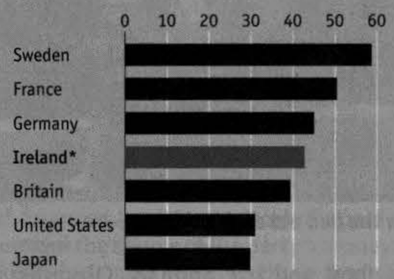
His party leader, Mary Harney, puts the emphasis on equality of opportunity, not equality per se. She also symbolises another huge change for the better in Ireland: its treatment of women. A generation ago they were second-class citizens. Now not only is the tanaiste female, but so is the president, Mary McAleese—as was her immediate predecessor, Mary Robinson. Far more women are working, and some are starting to rise to the top in business.

Looking which way?

What do all these social changes add up to? A few years ago, Ms Harney caused a stir with an address that became known as her Boston v Berlin speech. In it she claimed that, because its success was rooted in lower taxes and other free-market policies, Ireland, though geographically closer to Berlin, was spiritually closer to Boston. It is an appealing thesis.

A middle European 5

Tax receipts, % of GDP, 2003



Source: OECD *as % of GNP

Yet in social terms, the Boston v Berlin thesis looks wrong. In every area where Ireland has seen social change—secularisation, the growth of public health and welfare systems, trends in crime, drug and alcohol abuse, changing family patterns, increased migration—the shift has brought it closer to Europe than to America. By European standards the Irish tax burden is low, but it is still well above America's (see chart 5). Thanks to cheap flights (notably through Ryanair, a young airline that has made a big contribution to social change in Ireland), many more people travel from Ireland to Britain and continental Europe than go to America.

Indeed, in many ways the place that Ireland most resembles now is not America; it is Britain—but with a pro-European stance. Many British politicians think their country should become more detached from Europe, or even become more firmly attached to America. Yet in Ireland, despite Ms Harney's Boston v Berlin thesis, nobody would dream of suggesting such a move. Which is not to say that nationalist feeling is weaker than in Britain. The country's efforts to promote the Gaelic language belie that. Yet in practice as opposed to sentiment, Gaelic is still declining. When one minister was confronted by protesters demanding that Gaelic be made an official EU language, he went to talk to them—only to discover that they themselves did not speak the language.

As if to demonstrate its European credentials, Ireland is even metricating its road signs. Driving west of Cork, your correspondent spotted a sign reading: "Speed limit: 60km per hour for the next five miles." Naturally, nobody took much notice. Ireland will surely retain its charms and foibles, though its growing tourist industry will not be helped by the ugly houses sprouting across open countryside or the salmon farms that jeopardise its glorious wild salmon and salmon-trout runs.

The point about Ireland is not that people have become rich, though many have. Nor is it that, in just ten years, it has undergone a modernisation and secularisation that took other countries several times as long, though it has. No, the really big thing is that, 30 years after joining Europe, Ireland has grown up. No longer does it suffer from a lack of confidence or excessive touchiness about Britain. Instead, it has become like any other well-off European country, with reasonable if not outstanding growth prospects and a recognisably European social mix. On the whole, this is a vast change for the better—even if some traditionalists may mourn it. ■

Future surveys

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Key statistics for the construction industry

	2006	2007	2008	2009	2010E
GNP (constant 2008 prices, €m.)	153,398	160,299	154,672	138,161	136,089
% volume change in GNP	+6.5	+4.5	-3.5	-10.7	-1.5
Gross domestic fixed capital formation (GDFCF) (Constant 2008 prices, €m.)	45,193	46,456	39,806	27,482	21,106
Volume Change in GDFCF (%)	+4.6	+2.8	-14.3	-31.0	-23.2
Total construction output					
Value output (current prices €m.)	38,631	38,601	32,593	18,048	11,733
Change in value of construction output (%)	+14	+0	-16	-45	-35
Value output (constant 2008 prices €m.)	34,838	35,057	32,593	20,646	14,540
Change in volume of construction output (%)	+10	+1	-7	-37	-30
Construction output as % of GNP *	25.1	23.7	21.1	13.8	9.2
New construction output **					
Public sector new construction output ***					
Value of output (constant 2008 prices, €m.)	6,375	7,008	8,564	8,025	7,045
Change in volume of construction output (%)	+0	+10	+22	-6	-12
As % of total construction output *	17	19.6	26	40	50
Private sector new construction output **					
Value of output (constant 2008 prices, €m.)	21,324	20,356	16,040	6,379	2,270
Change in volume of construction output (%)	+13	-5	-21	-60	-64
As % of total construction output *	64	60	49	28	13

	2006	2007	2008	2009	2010E
Direct employment in construction (000s Q4)	268	264	216	137	110
Direct plus indirect employment (000s Q4, est.)	376	369	303	191	154
Change in capital goods price index for building and construction (materials and wages) (%)	+6	+5	+3	-2	+1
Change in building and construction price index for all materials (%)	+8	+5	+3	-3	+3
Change in tender prices (est) (%)					
- New housing	+4	-2	-12	-22	-12
- New general contracting	+4	-1	-11	-17	-10
- New civil engineering	+4	+4	-6	-7	-7
Change in total construction price inflation	+4	-1	-9	-13	-8

Notes:
* Percentages derived using output measured in current prices.
** The balance, not shown in the table, is repair and maintenance output (32% of total output in 2009 and 37% in 2010).
*** The estimate for new public sector construction includes an estimate for private sector investment under education, energy and telecommunications (estimated at €0.9bn in 2009 and €0.6bn in 2010).

Ireland: Housing loans

2.20 Ireland: Housing loans[1], 2004-2013

Year	New Houses	Other houses	Total Number	Total value (€m)	Average value of mortgage (€000)	Representative mortgage interest rate (%)[2]
2004	44,231	54,478	98,709	16,933	171.5	3.48
2005	53,758	53,922	107,680	21,536	200.0	3.49
2006	55,737	55,516	111,253	25,495	229.2	4.20
2007	46,588	37,698	84,286	22,457	266.4	5.25
2008	24,467	29,224	53,691	14,508	270.2	5.51
2009	9,832	15,340	25,172	5,831	231.6	3.46
2010	6,923	11,459	18,382	3,799	206.7	3.66
2011	3,033	8,204	11,237	2,105	187.3	4.18
2012	3,229	11,080	14,309	2,484	173.6	4.24
2013	2,522	11,093	13,615	2,368	174.0	4.36

Source: Department of the Environment, Community and Local Government

[1] These data contain an unquantified element of refinancing of existing mortgages.

[2] See Appendix 1 for more details.

Open in Excel: Measuring Ireland's Progress, 2013 Table 2.20 (XLS 19KB)

- The average value of a housing loan in Ireland increased strongly from €171,500 in 2004 to €270,200 in 2008 before falling sharply over the following five years to €174,000 in 2013.
- The mortgage interest rate rose from 3.48% in 2004 to 5.51% by 2008. The rate then dropped sharply to 3.46% in 2009 and has gradually increased each year since then to stand at 4.36% in 2013.

Central Statistics Office, Skehard Road, Cork, Ireland
Tel: 353-21-4535000 | Fax: 353-21-4535555 | email: information@cso.ie
Contact Census: Tel: 353-1-8951460 | email: census@cso.ie

Distribution of largest debtors

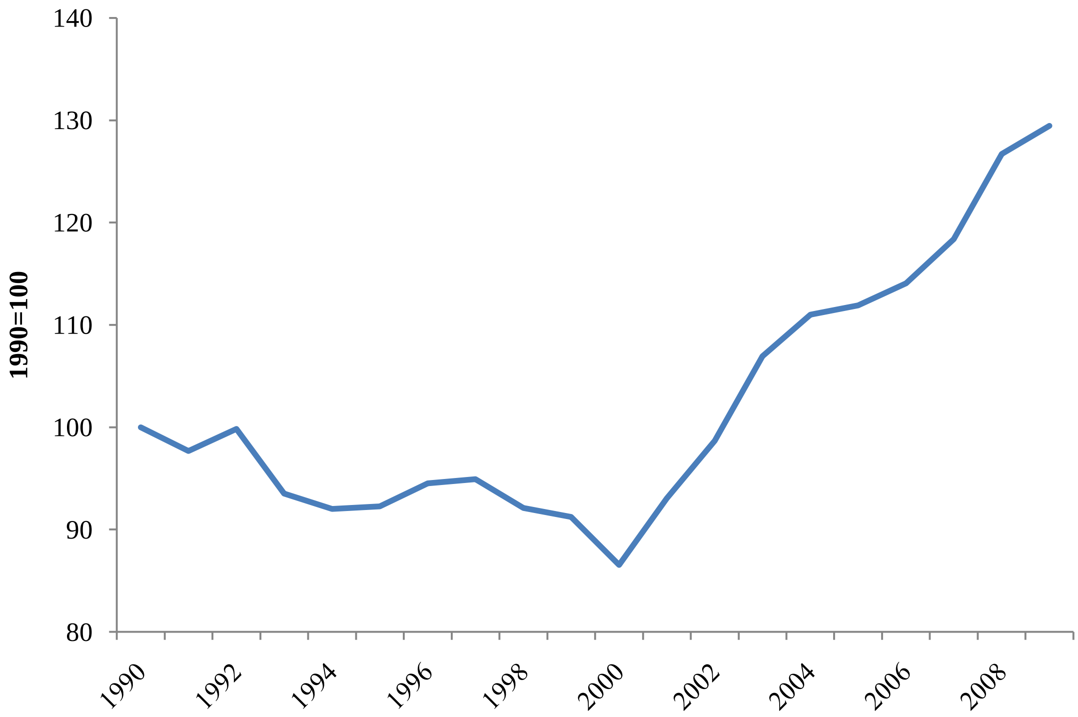
Distribution of largest debtors

Table 2 provides a breakdown of all debtor connections by size of nominal debt exposure. It should be noted that many of the debtors are also indebted to financial institutions which are not part of the NAMA scheme.

Nominal Debt	Number of debtor connections	Average nominal debt per connection €m	Total nominal debt in this category €m
In excess of €2000m	3	2,758	8,275
Between €1000m and €2000m	9	1,549	13,945
Between €500m and €999m	17	674	11,454
Between €250m and €499m	34	347	11,796
Between €100m and €249m	82	152	12,496
Between €50m and €99m	99	68	6,752
Between €20m and €49m	226	32	7,180
Less than €20m	302	7	2,117
Total	772	96	74,015

Table 2: Distribution of NAMA debtor connections by size of nominal debt

Chart 2.7: Relative Hourly Earnings (Manufacturing) Ireland -v- Main Trading Partners, 1990-2010



Source: CBFSAI

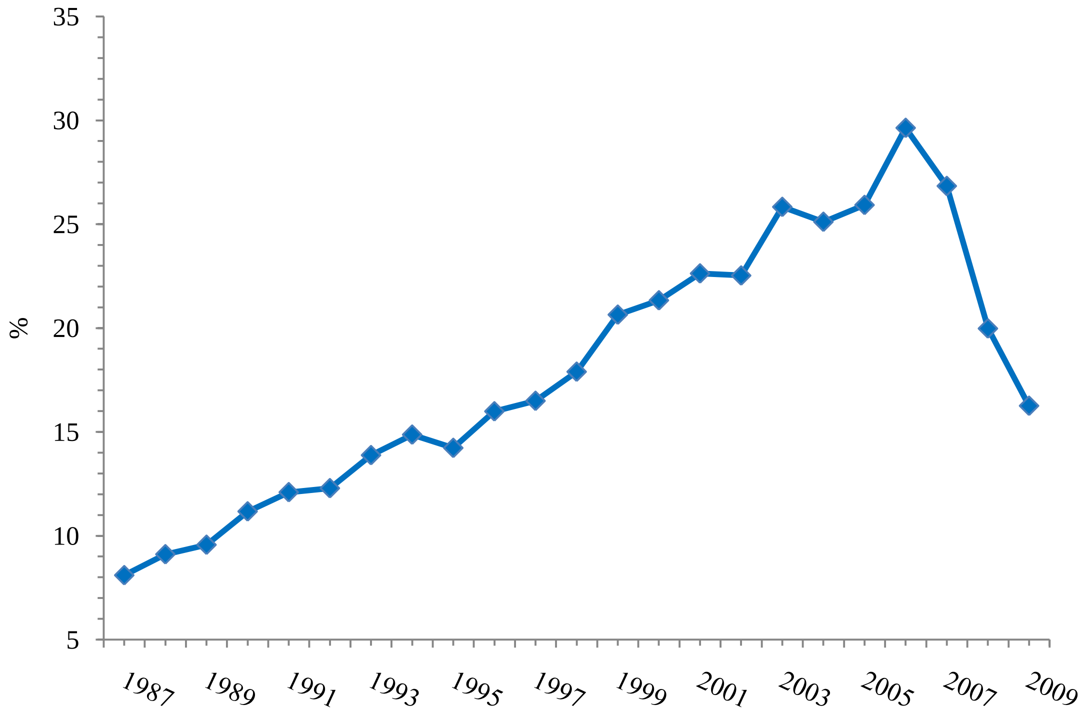
trading partner countries. Masked by the construction boom, this loss of wage competitiveness was certain to affect employment expansion sooner or later.[20]

2.23 Although Ireland's public debt level immediately prior to the crisis was low, the **fiscal deficit and public sector borrowing** surged quickly with the onset of the crisis. This was partly attributable to a rise in Government spending in GDP (after 2004) which became embedded in the system. The expenditure boost came at a period when elements such as the cost of unemployment payments was driving other cyclically-related spending down. However, in light of soaring tax revenues at the time, Government decided to increase autonomous spending particularly on public sector pay. But the main cause of the borrowing surge was the collapse in tax revenues in 2008-09 which appears to have been the most pronounced of virtually any country during the current downturn.

[20] Public sector workers, who had on average maintained a significant average wage premium relative to private sector workers during the Celtic Tiger period, seem to have stretched that premium in the years after 2003 (cf. Boyle et al., 2004; Kelly et al., 2008).

2.24 Much of the reason for the revenue collapse lies in the systematic shift over the previous two decades away from stable and reliable sources such as personal income tax, VAT and excises towards cyclically sensitive taxes. Revenue became increasingly dependent on corporation tax, stamp duties and capital gains tax (in that order); the contribution of these taxes to total tax revenues rose steadily from about 8 per cent in 1987 to 30 per cent in 2006 before falling to 27 per cent in 2007 and just 20 per cent in 2008 (Chart 2.8).

Chart 2.8: Cyclical Taxes as % of Total 1987 to 2009
(Corporation Tax, Capital Gains Tax and Stamp Duties)

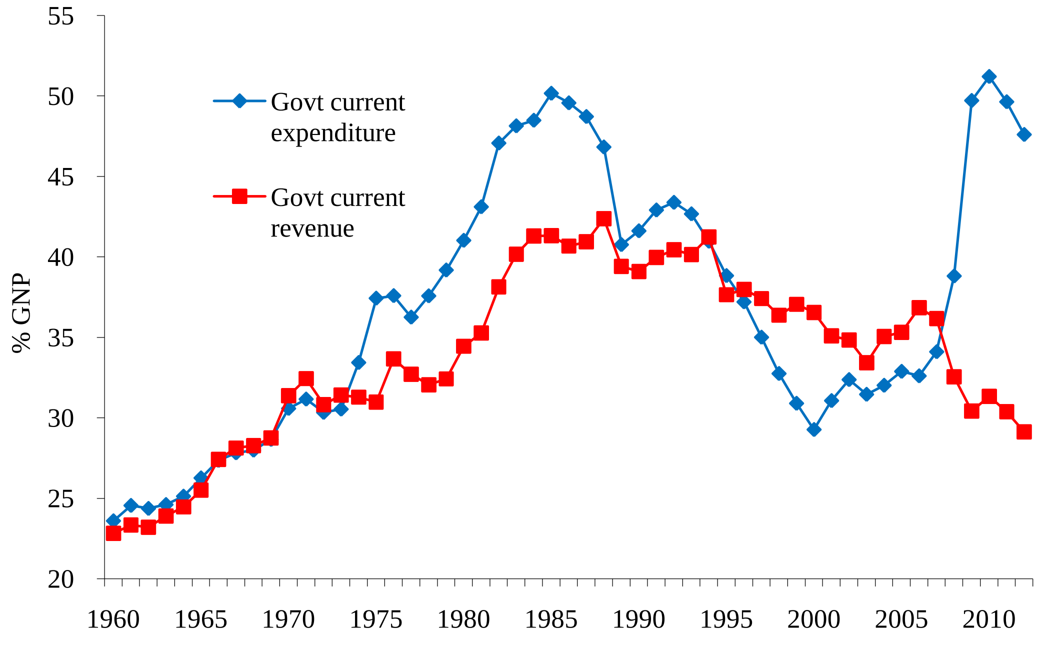


Source: Department of Finance, CBFSAI Calculations.

2.25 The steady growth in revenue from the above "fair weather" taxes during the two decades from 1988 – with only two brief hesitations in 1993 and 2001-02 – created a false sense of security as to their sustainability and induced policy makers to take advantage by narrowing the base of the personal income tax and lowering rates. The latter did help buy wage restraint but left the budget seriously exposed to a downturn. Had the tax structure been less cyclically sensitive, the fall in revenue in 2008 would have been much lower.

2.26 Government spending doubled in real terms between 1995 and 2007, rising at an annual average rate of 6 per cent. With the economy growing at an even faster rate, this implied a generally falling or stable expenditure ratio of expenditure to GNP until 2003. But thereafter the ratio rose, especially after output growth began to slow in 2007. And, in a final twist, real expenditure rose by over 11 per cent in both 2007 and 2008, an unfortunate late burst of spending which boosted the underlying deficit at almost the worst possible time.

Chart 2.9: Current Government Expenditure and Revenue, 1960-2010



Source: Department of Finance, CBFSAI calculations.

2.27 Throughout this period, the Government made extensive use of taxation incentives aimed at the construction sector.[21] The rates of stamp duties, which were high, were lowered several times in recent years (in 2001, 2002, 2003, 2005, and 2007), sometimes with the aim of improving the affordability of housing to first time buyers (as was the case with the Bacon initiatives 1998-2000). In addition, different classes of construction investment have attracted sizeable income tax concessions extending over long periods. At the height of the boom, in 2004-06, schemes existed for urban renewal, multi-storey car parks, student accommodation, buildings used for third level

[21] The effect of taxation on investment in construction is a complex subject [see studies by Barham (2004) Indecon (2006), Goodbody (2005), Van den Noord (2005) and Rae and van den Noord (2006)].

educational purposes, hotels and holiday camps, holiday cottages, rural and urban renewal, park and ride facilities, "living over the shop", nursing homes, private hospitals and convalescent facilities, sports injury clinics and childcare facilities. After some transitional arrangements, most of these incentives were abolished by 31 July 2008, after the expiration date of the schemes had earlier been extended on several occasions during 2000-08.[22,23]

2.28 The ceiling on the income tax deductibility of mortgage interest for owner-occupiers was increased in 2000, 2003, 2007 and 2008. By 2006 Ireland was one of only four OECD countries which allowed income tax deductibility while not taxing imputed rental income or capital gains for owner-occupiers. Furthermore, no residential property tax existed. Still, the estimated tax bias in favour of owner-occupation was only the fifth highest in the EU15 countries (Rae and Van den Noord, 2006). For investors, after 2001 deductibility was limited only by the investor's rental income.

2.29 The above tax policy elements of the tax code certainly influenced the extent of construction activity and the level of land and property prices. In theory they might just have shifted the composition of Irish wealth in favour of construction and not necessarily have caused in themselves unsound borrowing or lending and defaults. However, studies of some of the schemes suggest that they became associated with over-building and high vacancy rates – phenomenon which are very evident today.

Section 6: Disentangling the Effect of Lehman Brothers

2.30 It would be a significant mistake to suppose that the steep economic downturn that has been experienced since 2007 is wholly due to the working out and correction of underlying domestic imbalances that have been described. After all, there has been a severe world-wide recession, the causes of which involve the correction of imbalances in the US, UK and elsewhere – excesses which have their own complexities not shared in the Irish case.

2.31 It is useful to consider more specifically what might have been the relative contribution of local factors to the Irish output loss. As a first approximation, Chart 2.10 compares

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[22] Tax incentive schemes in the health sector were not abolished in 2008. However, these were later abolished in the Supplementary Budget 2009.

[23] For example, in the case of the Urban and Town Renewal Schemes, end-dates of 31 December 2002, 31 December 2004 and 31 July 2006, had previously been specified.

conducive to promoting the IFSC was considered important by Government.[136] The Department of the Taoiseach took a lead role in coordinating support and the development of the international financial services industry. Partly, this was done through a consultation mechanism, the Clearing House Group at which senior FR representatives as well as industry personnel were present to identify issues of major concern to the development of the sector. The Chair and CEO of the FR participated in several roadshows to promote the IFSC (e.g., Patterson 2007).

7.28 The FR and the CB were mandated by legislation to pursue two goals – financial stability and promotion of the financial sector – which may well have been in conflict. The FR was in a difficult position as the possible adverse effects on discouraging inward investment in the IFSC were more immediate and real than what were perceived as more distant concerns about financial stability. While the stability goal was given explicit priority, the potential conflict between the two goals complicated policy choice.

7.29 A **third** concern was that more aggressive use of some of the instruments discussed above could have been criticised as running contrary to the spirit of principles-based regulation. The latter assumed that financial institutions would at the end of the day operate in their enlightened self interest and that by and large they should be left to so unencumbered by unnecessary, and especially, heavy handed, regulatory intervention. However, such an argument is based on an insufficient appreciation of the risk that poor judgements by decision makers in institutions will lead not only to costs for themselves but also for the wider public given, in many cases, the institutions' systemic importance and the consequent pressures to " bail them out" to a greater or lesser extent during a crisis.

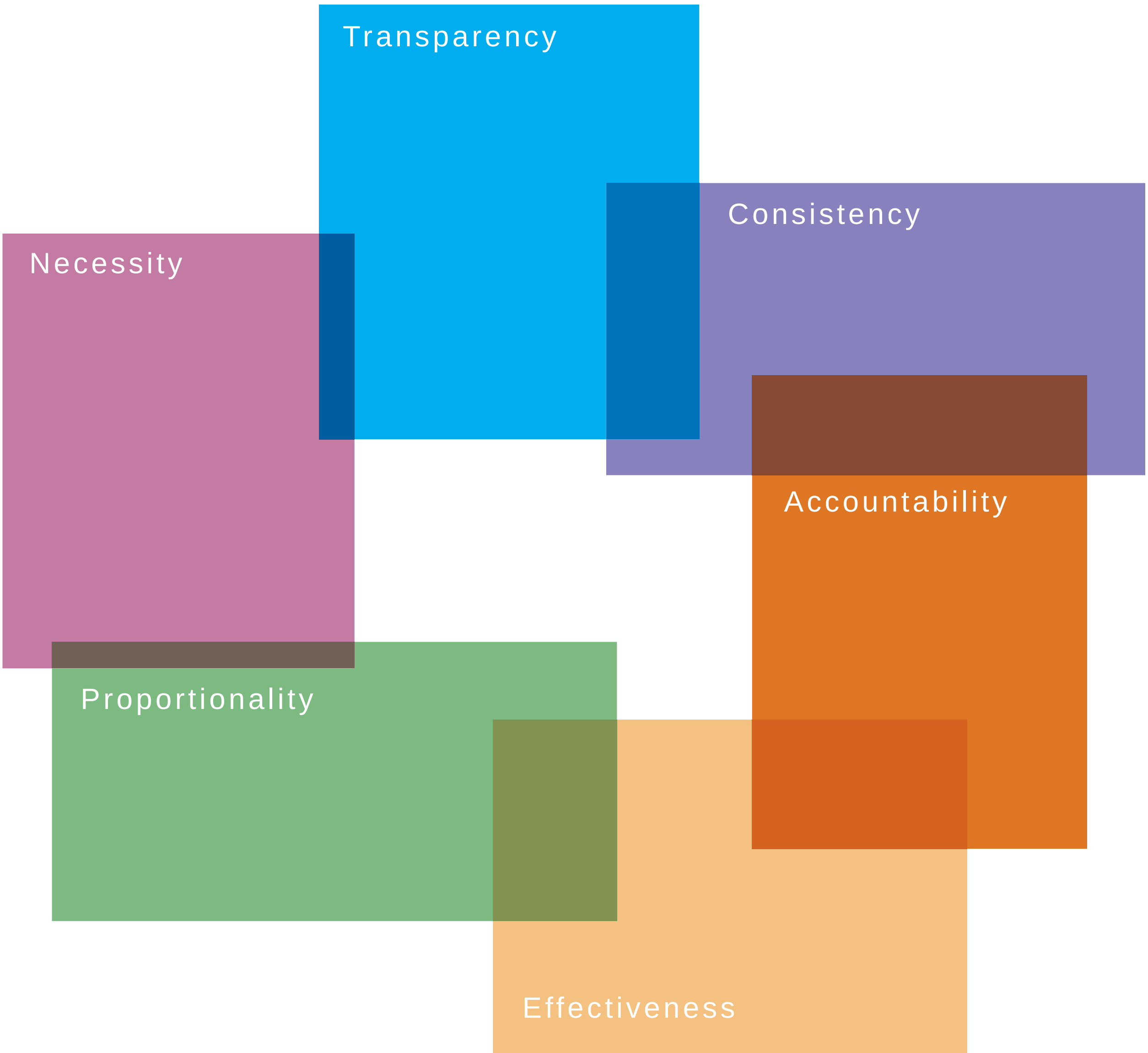
7.30 As noted in Chapter 4, several key architectural aspects of the principles-based approach had not been applied, or applied only partially, in Ireland since 2003. But even if these elements had been fully in place it would not have protected the financial system from the potential for misjudgement that led to the financial crisis. These misjudgements – in the form of excessive reliance on a massive expansion in property-related lending – were probably facilitated by an incentive structure which, to varying extents, in the face of aggressive competition, tended to reward volume at the expense

[136] For example, "A number of factors have underpinned our attractiveness as a location for international financial services, including an attractive fiscal and regulatory environment ..." (Department of the Taoiseach, 2006, p. 8). See also *ibid*, (pp. 12-13).

Roinn an Taoisigh
Department of the Taoiseach

Regulating Better

A Government White Paper setting out six principles of Better Regulation



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Department of the Taoiseach

Regulating Better

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Taoiseach's Foreword

Enhanced competitiveness is a key part of the Government's strategy to achieve social progress, better living standards and a steadily improving quality of life. I am absolutely committed to ensuring that Ireland continues to be a competitive and open economy and that we do not erode the social and economic progress we have made as a country over recent years. This White Paper deals with good quality regulation, which has an essential role in achieving these objectives. It sets out core principles that the Government will adhere to in regulating and outlines a number of steps that will be taken to put the principles into practice.

Our exceptional economic growth in recent years has enabled Ireland to make significant gains on a number of fronts. Employment expanded, the unemployment rate fell rapidly, much-needed infrastructural projects were put in place or initiated, and living standards rose significantly. However, in the current, more uncertain global economic environment we need new avenues through which we can maintain and enhance our competitiveness. We also need to ensure that the benefits of greater competitiveness and of heightened domestic competition are transferred to citizens and businesses. Better Regulation is one of the instruments available to achieve this.

Historically, much Government attention has been focused on the traditional instruments of Government, such as current expenditure, taxation and investment. Little importance has been given to regulatory policy. However, increasingly in OECD countries, greater attention is being paid to choosing the most appropriate regulatory framework. The coming years are likely to be crucial, domestically and internationally, in establishing the right mix of regulatory policies, tools and institutions. This White Paper establishes core principles to guide these choices and, in doing so, provides for greater participation and transparency in policy-making and contributes to a better environment for the individual, the community and for business.

While many countries now recognise that Better Regulation is vitally important for competitiveness and economic growth, Better Regulation also has a role to play in promoting inclusiveness and good government for all citizens. Thus, the core principles set out in this White Paper also relate to the quality of governance and the efficiency and effectiveness of the public service.

It is widely accepted that, as well as providing predictability and certainty in the business world, good quality regulation contributes to establishing and maintaining individual freedom and social cohesion, not least through articulation and protection of citizens' and consumers' rights. However, the reverse is also true. Bad or cumbersome regulation not only creates barriers to efficient markets, thereby discouraging competition and innovation, but also alienates citizens from government and can contribute to unfair income and wealth distribution.

Reflecting the importance of regulation in many areas of economic and social policy, the latest social partnership agreement, *"Sustaining Progress"*, contains commitments to publish a White Paper on Regulation and introduce Regulatory Impact Analysis (RIA). At EU level, the Better Regulation agenda has been gaining momentum in recent years, particularly in terms of the stated need, in the Lisbon objectives, to pursue a simpler regulatory environment. The European Commission is implementing an action plan on simplifying and improving the regulatory environment which Ireland is actively supporting.

This White Paper sets out core principles of good regulation. It also goes further: it sets out a programme of actions to give effect to these principles. I look forward to seeing these actions being implemented and to a new drive for economic competitiveness, social progress and better Government.

BERTIE AHERN, T.D.
Taoiseach

Executive Summary

Introduction

The Government has prepared *"Regulating Better"*, a Government White Paper that will contribute to improving national competitiveness and better Government by ensuring that new regulations – Acts and Statutory Instruments (Orders) – are more rigorously assessed in terms of their impacts, more accessible to all and better understood. Existing regulations will be streamlined and revised, where possible, through a process of systematic review and by repealing, restating and consolidating them as appropriate. This White Paper will also contribute to better regulatory processes and institutions, including a more consistent approach to the establishment and design of independent sectoral regulatory authorities.

Principles

This White Paper identifies what the Government sees as the principles of good regulation:

NECESSITY – is the regulation necessary? Can we reduce red tape in this area? Are the rules and structures that govern this area still valid?

EFFECTIVENESS – is the regulation properly targeted? Is it going to be properly complied with and enforced?

PROPORTIONALITY – are we satisfied that the advantages outweigh the disadvantages of the regulation? Is there a smarter way of achieving the same goal?

TRANSPARENCY – have we consulted with stakeholders prior to regulating? Is the regulation in this area clear and accessible to all? Is there good back-up explanatory material?

ACCOUNTABILITY – is it clear under the regulation precisely who is responsible to whom and for what? Is there an effective appeals process?

CONSISTENCY – will the regulation give rise to anomalies and inconsistencies given the other regulations that are already in place in this area? Are we applying best practice developed in one area when regulating other areas?

Approach taken

The approach of this White Paper is both practical, in that it is action-oriented, and pragmatic in that the Government is not "for or against" regulation. Rather, the Government favours Better Regulation. Regulation is an integral part of the process of governing and it will continue to be so. Legislation and subsidiary regulations have a critical role to play in key areas of economic and social life. The recommendations and actions in this White Paper are best seen in the context of the continuing drive for competitiveness and people's expectations of high quality public services. Many of the principles and commitments reflect good practice and developments regarding regulation internationally. For example, many of our European Union (EU) partners and the EU institutions themselves are developing similar principles and actions.

Overview of Actions

The Government will make better use of evidence-based policy-making. This means making better use of research and analysis in both policy-making and policy implementation. Regulation is an expression of policy and **Regulatory Impact Analysis (RIA)** is an evidence-based approach that allows for the systematic consideration of the benefits and costs of a regulatory proposal to the economy and society. The Government will pilot a system of RIA in a small number of Departments and, following the pilot phase, RIA will be integrated with existing procedures. RIA will give special consideration to business impacts, especially in respect of Small and Medium Enterprises (SMEs). RIA will be integrated with developments under the e-Cabinet project and will be supported through training, guidelines and promotion.

Systematic reviews of the regulation of key areas and sectors will be carried out which will involve reviewing the regulatory institutions in place, as well as the body of regulation governing particular areas.

To improve the internal consistency of regulation in particular areas, the Government will implement a programme of **Statute Law Revision**, including a major project to update pre-1922 legislation. The Government will also use RIA to ensure the effectiveness of new regulations, taking account of the existing body of regulation.

Emphasis will be placed on developing proposals for improvements to the procedures for **appealing regulatory decisions**. For example, consideration will be given to establishing expert panels of judges to deal with specific competition and sectoral regulation cases.

In considering the burden of complying with regulations, the Government will review:

i) compliance and the question of linking penalties and fines to income and ability to pay; and

ii) the extent to which the criminal justice system is capable of efficiently dealing with the complexities of modern regulatory issues.

The Government will also monitor the cumulative burden of **compliance** on business and SMEs to ensure that compliance costs are fair and proportionate with the benefit the regulation brings.

The Government will ensure that new regulations are better understood, by publishing **explanatory guides** alongside primary legislation with significant impacts, in particular those that impact directly on consumers/citizens/SMEs. Similar steps will be taken to improve the quality of the explanatory material that accompanies secondary law/statutory instruments containing major proposals.

The Government will also encourage the establishment of norms and standards for **consultation** processes and will keep under consideration the need for legislation underpinning administrative procedures.

The Government will create new **sectoral regulators** only if the case for a new regulator can be clearly demonstrated in light of existing structures. It will assess the possibilities for rationalisation of sectoral regulators along with promoting the strengthening of existing contacts between the sectoral regulators, the Competition Authority and the Office of the Director of Consumer Affairs.

To further improve customer service delivery, the Government will require Departments to streamline service delivery and **administrative processes** where possible, using the latest technology, along with the introduction of customer charters, to reduce the burden of compliance on the citizen.

The Government intends to strengthen the capacity for evidence-based policy-making by ensuring that **Departments** promote training and awareness-raising of policy analysis skills. Departments will also be required to report, through their Strategy Statements and Annual Reports, on regulatory reforms and service improvements.

A key to Better Regulation will be clarity and accessibility of regulations. The Government will improve the coherence of legislation through **revision, restatement and repeal**, by ensuring greater consistency in the drafting of Statutory Instruments and maximising the use of IT/e-Government initiatives to improve clarity and accessibility of regulations.

Next steps

A detailed Action Programme is set out in this White Paper, along with assignments of responsibility and indicative timescales. A **Better Regulation Group** will be established and it will be asked, inter alia, to report back regularly to the Government on implementation of these actions by Departments, Offices and Agencies.

Glossary of Terms

Some terms explained

Codification: Codification is sometimes used, in a general sense, to describe processes such as restatement and consolidation, which help bring all the relevant legislation on a particular topic into a single, updated text.

Consolidation: Consolidation is the process whereby the Oireachtas passes one, overall Act into which all previous Acts relating to a topic are collected. An example is the Social Welfare (Consolidation) Act, 1993.

Consumer & citizen: The terms ***consumer*** and ***citizen*** are used in this document and it is important to note that these are not interchangeable terms.

The term ***consumer*** means a private individual, participating in the market by buying goods and services for their own use.

The concept of a ***citizen*** denotes a fuller relationship between an individual and the State. In this White Paper, it is not used to denote nationality in any strict legal sense.

In situations where the State is a direct producer or supplier of particular goods or services to citizens and businesses, those citizens/businesses are also consumers.

Governance: Governance has been defined as *"rules, processes and behaviour that affect the way in which powers are exercised.... particularly as regards openness, participation, accountability, effectiveness and coherence"* (European Commission, *European Governance – A White Paper*, 2001). In this Paper the term refers to governance at all levels of Government: national, regional, local and - at times - at the level of specific economic sectors.

The Lisbon Objectives: These are the main targets which were adopted by the Heads of State and Government of EU Member States at their meeting in Lisbon in March 2000. The strategic goal agreed at Lisbon is to make the European economy the most competitive and dynamic knowledge-based economy in the world by 2010, i.e. to create an economy capable of sustainable development, with more and better jobs and stronger social cohesion.

These objectives are designed to focus the EU institutions and Member States on strengthening and deepening the European internal market, by preparing for the transition to a knowledge-based economy and society and promoting investment in research and innovation. Other objectives include promotion of entrepreneurship, support for Small to Medium Enterprises (SMEs), modernisation of the labour market and combating social exclusion. The Lisbon Objectives are the central theme at European Spring Council meetings, attended by Heads of State and Government.

Public Service Obligation (PSO): A PSO is an obligation placed by the State on a supplier to provide a service or to engage in an activity where it is not commercially attractive to do so, but which the State considers to be in the public interest. Examples of PSOs are to be found in local public transport services and regional air services.

Regulation: In this document we generally use "regulation" to mean primary legislation enacted by the Oireachtas and secondary legislation enacted by Ministers empowered under primary legislation. Depending on the context, it can also mean "to regulate" in the economic and social sense of the word. For example, "regulation of telecommunications" would be taken in a general sense to include ComReg (the Commission for Communications Regulation), the Department of Communications, Marine and Natural Resources and the body of regulation that governs telecommunications.

A wider definition of "regulation" would also include, in addition to Acts of the Oireachtas and Statutory Instruments, Bunreacht na hÉireann and the Treaties, rules and regulations of the European Union. Such a definition might also extend to subsidiary rules and regulations, such as those made by Local and Regional Authorities, and self-regulatory bodies with regulatory powers.

Regulation can also be used in a more specific sense to mean an EU "Regulation", as opposed to a Directive. This is a particular class of legal instrument made by the Council, Parliament or Commission and binding on Member States and their citizens.

It will be made clear in the document where these meanings are intended.

Regulatory capture: This is an economic term describing a situation where one operator (or group of operators) in the market uses its influence or resources to extract a regulatory decision, or lack of decision, for their own benefit rather than the benefit of society as a whole. It is associated with patterns of behaviour on the part of a regulatory body in one, or a combination, of the following situations:

- the regulatory body is tending to further producer interests over consumer interests.
- the regulatory body has become overly protective towards the regulated entities.
- the regulatory body is tending to adopt objectives that are very close to those of the entities it is supposed to regulate.

Regulatory Impact Analysis (RIA): RIA is an assessment of the likely effects of a proposed new regulation or regulatory change. It involves a detailed analysis to ascertain whether or not the new regulation would have the desired impact. It also helps to identify the side effects and any hidden costs associated with regulation. RIA clarifies the desired outcomes of the proposed regulatory change.

RIA promotes evidence-based policy-making by giving detailed consideration to the likely impacts of decisions, along with structured consultation with stakeholders and citizens.

RIA is not a substitute for decision-making. It is an approach which improves the quality of political and administrative decision-making, while providing openness, public involvement and accountability.

Regulatory Management and Better Regulation: Increasingly, these terms are being used to convey the concept of an ongoing commitment by Governments to improving regulation, e.g. the processes of policy formulation, legislative drafting and enhancing the overall effectiveness and coherence of regulation.

The idea of "Better Regulation" also helps to draw an important distinction between the wide regulatory reform agenda and the more specific issue of deregulation. In some cases, consumer, investor and the general public interest may be better served by new regulations, while in others it is better served by amending or removing regulations.

Regulatory Reform: Generally, this term describes, *"changes that improve regulatory quality, i.e. enhance the performance, cost-effectiveness or legal quality of regulations and related government formalities"* (OECD, *Regulatory Reform in Ireland*, 2001).

These can be changes in specific regulations governing markets and sectors, such as utilities - telecommunications, energy or transport. Alternatively, it can mean changes to the way regulations are formulated, enacted and enforced. Examples of these changes include: impact analysis techniques, the use of alternatives to regulation and "sunsetting" (see below).

Repeal and re-enactment: Repeal and re-enactment is the process whereby legislation can be repealed and re-cast in more coherent language, but with the same underlying policy. Repeal and re-enactment of secondary legislation can be undertaken by persons authorised by law to make secondary legislation.

Restatement: Restatement is the process used by the Attorney General to make updated versions of Acts of the Oireachtas, or earlier statutes, available. These versions, known as restatements, do not alter the substance of the law and, therefore, do not require Oireachtas approval. They are, in effect, administrative consolidations. They may, however, be cited in court and accepted in court as *prima facie* evidence of the legislation set out in them.

Sunsetting: Sunsetting is when, at the time a regulation is made, a specific date is set on which that regulation will expire unless it is re-made. This ensures that a regulation is formally reviewed at an agreed date in the future, to establish whether or not it is still valid, or if it could be improved, reduced or even revoked.

Universal Service Obligation (USO): A USO is a specific type of Public Service Obligation (PSO) – see above. It is an obligation placed by the State on a supplier to provide a service of a specified quality to all users throughout the country, irrespective of geographical location, at an affordable price. It is used particularly for network industries such as telecommunications and postal services. An example of a USO is where the price of posting a letter is the same irrespective of where in the country it is to be delivered. The cost of a USO is often met by some form of cross-subsidisation, whereby some users of the service pay more than the true cost of providing the service to them, so as to subsidise other users who pay less.

Overview

Why do we need this White Paper?

We need a White Paper on Regulation, mainly because of the impact which regulation has on national competitiveness. We also need it because regulation affects the quality of everyday life. This includes the quality of our food and water, the safety of our workplaces as well as the range of products and services available to us and the price we pay for them. Despite this level of influence, we have rarely paused to consider in a systematic way questions relating to the quality of regulation. Questions such as: why we regulate, how we make regulations, what kind of regulation we want or what constitutes good regulation? This White Paper attempts to address some of these questions by setting down core principles of good regulation.

What are the principles of Better Regulation?

The principles of Better Regulation that the Government wishes to promote are:

+ NECESSITY – is the regulation necessary? Can we reduce red tape in this area? Are the rules and the structures that govern this area still valid?

+ EFFECTIVENESS - is the regulation properly targeted? Is it going to be properly complied with and enforced?

+ PROPORTIONALITY – are we satisfied that the advantages outweigh the disadvantages of the regulation? Is there a smarter way of achieving the same goal?

+ TRANSPARENCY – have we consulted with stakeholders prior to regulating? Is the regulation in this area clear and accessible to all? Is there good back-up explanatory material?

+ ACCOUNTABILITY – is it clear under the regulation precisely who is responsible to whom and for what? Is there an effective appeals process?

+ CONSISTENCY – will the regulation give rise to anomalies and inconsistencies, given the other regulations that are already in place in this area? Are we applying best practice developed in one area when regulating other areas?

What do we mean by “regulation”?

We generally mean primary and secondary legislation. Primary legislation means Acts passed by the Oireachtas and earlier Parliaments. Secondary legislation means legislation for which responsibility has been delegated by the Oireachtas to some other party. In practice, it is usually Government Ministers to whom responsibility has been delegated and secondary legislation usually takes the form of Statutory Instruments. Of course, much of our national regulation is derived from our membership of the European Union, through EU Directives and regulations.

However, at some points in the White Paper we also talk about “regulation” in a wider sense. For example, we may talk about regulation of an economic sector like telecommunications. In such discussions, “regulation” is normally used to describe the entire regime which governs that particular sector or activity. Regulation in this sense includes all of the primary and secondary legislation but also extends to the various authorities which operate in those areas. For example, “regulation of telecommunications” would be taken to include ComReg (the Commission for Communications Regulation), the Department of Communications, Marine and Natural Resources and the body of regulation that governs telecommunications.

How will these principles improve competitiveness?

Competitiveness is a relative concept and Ireland must constantly seek to improve its position vis-à-vis other economies. Inappropriate regulation can adversely affect the competitiveness of the economy. For example, our public services must not become snarled up in red tape. Our businesses must not be made to carry the dead weight of unnecessary or unduly restrictive regulation. We must not stifle competition or innovation through regulation that promotes or protects inefficiencies in the economy.

REGULATION AND COMPETITIVENESS

The Global Competitiveness Report 2003, published by the World Economic Forum (www.weforum.org), provides an assessment of the comparative strengths and weaknesses of 102 countries in relation to their economic competitiveness and growth. In the report, the five most competitive economies – Finland, USA, Sweden, Denmark and Taiwan – all identified tackling inefficient bureaucracy /red tape as a competitiveness issue. In general, respondents – both OECD and developing/transition countries – singled out red tape as one of the two major factors constraining their business operations.

The actions that we will take arising from our application of the principles that we identify in this White Paper will tackle both the "stock" of existing regulation and the "flow" of new regulation. We will scrutinise regulations to ensure that they do not unintentionally damage competitiveness. As far as possible, we will try to ensure that they enhance Ireland's competitive position.

We will pay particular attention to the interaction of competition and regulation. Vigorous competition can frequently deliver great benefits to consumers in terms of the quality and range of products and services as well as lower prices. By ensuring that regulation is supporting competition, we can bring benefits to consumers and enhance the competitiveness of the economy as a whole.

How will these principles improve our everyday lives?

In addition to benefits as consumers, applying these principles to new and existing regulations will improve the quality of our everyday lives. Red tape is at best frustrating and, at worst, it alienates people by placing barriers between the Government on the one hand, and citizens and communities on the other. Sometimes this is because of the quality of the regulations themselves – they might be drafted more with a focus on the administrator than on those whom they are designed to assist or protect. Sometimes it can be because there is confusion as to the structures and processes that are in place for dealing with particular issues. There may be overlap or duplication between regulatory authorities. There might be a lack of clarity on appeals procedures and who is responsible for what. The new principles that we are proposing will mean that we will systematically review and take account of these issues. The goal is to achieve a more coherent regulatory framework and to improve the quality of our everyday lives.

REGULATION IN OUR EVERYDAY LIVES

In an average day, a person will, perhaps without even being aware of it, come into contact with a number of services that are subject to regulation. The radio stations available when one wakes up in the morning, for example, are regulated by the Broadcasting Commission of Ireland. Transportation – on buses, trains, taxis and road usage – is also regulated. If children are left in a crèche during working hours, health, safety and welfare standards in those crèches are subject to regulation under the Child Care Act, 1991. Health, safety and other standards are also enforced in restaurants, cafes, bars, and supermarkets. In other words, our everyday lives are subject to regulation in a number of ways. Providing clarity and transparency in how we make and implement regulations is important, therefore, so that services do not get tied up by excessive red tape and people are clear about how regulation affects them directly.

Are we against regulation?

The Government is not against regulation. Rather, it is in favour of Better Regulation. Regulation is an integral part of the process of governing and it will continue to be so. Legislation and subsidiary regulations have a critical role to play in key areas of economic and social life, including:

+ To protect and enhance the rights and liberty of citizens;
+ To promote an equitable, safe and peaceful society;
+ To safeguard health and safety or protect citizens;
+ To protect consumers, employees and vulnerable groups;
+ To promote the efficient working of markets;
+ To protect the environment and promote sustainable development; and
+ To collect revenue and ensure that it is spent in accordance with policy objectives.

This White Paper recognises that, in certain cases, less regulation may be appropriate while, in other cases, more regulation might be required to achieve particular outcomes. In all cases, however, there should be better quality regulation.

COST OF REGULATION IN THE EU

The European Commission's internal market scoreboard shows that the burden of 'red tape' on business – not including citizens or administrations – is estimated to be between 4% and 6% of Gross Domestic Product (GDP) and that 15% of this burden is avoidable. National studies within the EU have variously estimated the burden on business at levels ranging from 2.2% of GDP (Netherlands) to 4.4% of GDP (Germany).

Taking 3% of GDP as a guideline estimate of the overall administrative burden, and assuming the EU estimate that 15% of this burden was avoidable, then unnecessary regulation could have cost Irish business about €582 million in 2002.

The cost to the European Union as a whole is somewhere in the region of 0.45% of European GDP or nearly 40 billion euro.

What about EU regulation?

While precise measurement is difficult, many EU Member States have estimated that about half of their regulation derives from membership of the EU and Ireland would be no different in this respect. The actions that we are adopting in this White Paper will not stem the flow of regulation at European level. However, many of the measures that we are proposing – such as impact assessment and simplification of regulation – are being adopted at EU level by the Commission and other institutions. Other Member States are also at various stages of implementing similar reforms to their regulatory processes. There is a growing recognition within the EU that Better Regulation can help to achieve the goals that were established by the European Council at Lisbon in 2000, which were designed to make the EU the most competitive economic bloc in the world in ten years.

While the flow of EU regulations (and other international regulations, e.g. United Nations, International Labour Organisation) will continue, Ireland, as a Member State, can influence their quality and content. In addition, just because a regulation originates in the EU and must be implemented at national level does not mean that we should not try to assess its likely impact at the earliest possible stage. The European Union (Scrutiny) Act 2002 requires the engagement of the Oireachtas in early assessment of EU legislative proposals.

Will this White Paper change who has responsibility for regulation?

The fundamentals of the legislative process and the role of the Oireachtas are established in the Constitution and there is nothing in this White Paper which proposes any change in this regard. Nevertheless, some changes have been taking place in recent times to our regulatory "architecture". Like many OECD countries, the role of the Irish Government has changed in some areas, from being service provider to service regulator. Many regulatory decision-making functions have transferred to specific sectoral regulators, in a bid to open competition and promote innovation. These new independent regulators have been established in areas such as communications – both telecommunications and postal services – as well as energy, aviation and financial services. Further developments are expected in the transport sector. The new regulatory bodies do not necessarily have the same structure or powers.

The main regulatory "actors" - those currently designing and implementing regulation in Ireland - are: the Oireachtas (as primary regulator); Government Departments and Offices; agencies at arms-length from Government which have regulatory enforcement functions; local authorities; independent sectoral regulators; and - in certain cases - professional bodies. There is a need to avoid overly elaborate regulatory structures. The challenge is, therefore, to implement regulatory reform while managing the ongoing development and effectiveness of existing regulatory institutions. The principles and actions contained in this White Paper will help to guide future choices about our regulatory system.

What practical difference will this White Paper make?

The White Paper establishes principles and also outlines steps for their implementation. These steps include changes to existing regulatory practices and introduction of some new measures. The net result will be that:

+ Regulations will be prepared in a more transparent way;
+ Public participation in their formulation will be enhanced;
+ Regulations will be clearer in their language and their focus;
+ Regulations will more effectively identify and achieve Government objectives;
+ Regulations will be designed so as to minimise the burden of compliance;
+ Regulations are likely to be better enforced;
+ Unintended effects of regulations will be minimised; and
+ Regulations will be regularly reviewed for their effectiveness and their continued relevance.

Regrets, he's had a few . . .

Kathy Sheridan

Sat, Oct 10, 2009 / http://www.irishtimes.com/news/regrets-he-s-had-a-few-1.754819

THE SATURDAY INTERVIEW: From the old fashioned sitting room of St Luke's, wielding homemade buns and disarming charm, Bertie Ahern vigorously defends his legacy - but if he had his time again, he'd do a lot of things differently.

IS THIS WHERE it ends? In a small upstairs sitting room in St Luke’s that has seen better days? The generously swagged curtains, the old-fashioned, pale-gold three-piece suite, the pieces of dark furniture all once aspired to a kind of glamour. Now they vie with a low sofa shrouded in a sheet, accessorised by a couple of fat, furry toys decked out in Dublin jerseys alongside their donkey pal in blue knicks with a soccer ball. Bronze figurines (the “appreciation” of choice) also feature in industrial quantities: wiry fiddlers, cheeky urchins swinging off lamp-posts, a busty Molly Malone wheeling her wheelbarrow towards the gas fire.

A crystal trophy marking Bertie Ahern’s Person of the Year 2005 award from the Sunday Independentand Irish Nationwide takes centre-stage above the mantel. On the walls hang a large portrait of himself and a pretty rendition of National Botanic Gardens glasshouses. A side table is colonised by a replica of a Chinese emperor’s bronze chariot, leaving just enough space for a respectable book – Patrick M Geoghegan’s Robert Emmet– and a pile of Cyprian Brady’s calling cards, a timely reminder that this is notBertie’s sole domain, but a Fianna Fáil partyhouse.

But take a look through the beige horizontal blinds. Catch the view across the busy airport road to the sweep of the canal, Fagan’s pub, Rosmini Gaels GAA club. It could only be one man’s territory: “Drumcondra,” he writes. “It’s where I’m from. And it’s who I am.”

But who is he? At the end of a 353-page autobiography that carries his authentic voice, the people’s Bertie remains profoundly unknowable. His economic legacy is shredded, his tribunal appearances sparked derision and, finally, contempt. Detractors even disparage his remarkable mediation skills – and, by extension, his towering role in the Belfast Agreement – as the traits of a man with no convictions to call his own. A harsh judgment – but is it fair?

You turn up, battle-ready, with pages of talking points for the allotted hour. Ahern lumbers in like an amiable teddy bear in a suit, looks up doe-eyed from beneath his lashes – shades of a confessional Diana – and murmurs, “tanks for comin’, Katty”. Thereafter he uses your name in almost every sentence. It’s just Bertie and you in this quiet, intimate setting, he helpfully positioning your tape recorder at his elbow; Sandra Cullagh, his long-time secretary, serving up good coffee and home-made buns made by Marion down the road . . .

It is disarming, but only a naif would have failed to anticipate it. The best of Bertie Ahern’s legacy will lie in his contribution to peace on this island and anyone attempting to catch him out should remind themselves of the natural gifts and modus operandi – the Machiavellian cunning, the deep reserves of patience, the willingness to absorb the punches, the ability to plant ideas in protagonists’ heads which they come to believe are their own – that hefted him on to that plinth of honour.

Is he a good mediator because he has no convictions of his own? “It’s totally wrong, but it’s been said about me all the time . . . I hold the view – and it’s a proven fact in world politics and leadership – that the easiest thing to do is come in and preach your aul’ gospel, rant on about your views and convictions according to whoever you are, and then expect everyone else to do it. But it won’t get you anywhere. You have to carry people with you. And in the modern world, people will not be lectured to or talked down to . . . So what you have to do is try and pull people together, and sometimes you have to persuade them of your things but you almost have to make them feel that they’re saying them rather than you’re saying them . . .”

His defence of his legacy is conducted in similar style, patiently, exasperation kept to a minimum even in the face of blatant conflict.

So for example, while his economic legacy may well be the perceived ATM facility he presented to the public sector, as well as Fianna Fáil’s enchantment with house-building, he cannot see a downside to either. Yes, he was shocked to read how the public sector had raced ahead of the private in average incomes. The thing is, he doesn’t believe it. The authors are not comparing like with like, he says, “since private sector people get VHI, car allowances . . .”

Does he regret unwinding some of the Bacon recommendations in 2002, a move which Peter Bacon himself believes led directly to the calamitous bubble? “I really resent some of the things that are said, including by Peter, who’s a good friend of mine,” Ahern says with unusual spirit. “There was a consensus that we had driven the investor out of the market and that, by doing that, we had totally escalated the rental values . . . He was totally in favour of reversing that . . . The only way to reduce the price of housing was to do our damnedest to build more houses. Ultimately, supply has to equal demand and the price has to fall – and that was our logic.”

But the exact opposite occurred? “No, it didn’t, no it didn’t,” Ahern insists. “We got supply up to 80,000.”

The plan was to pull back over three years, but “everything crashed . . . If we saw what was going to happen . . .”

But some people saw, didn’t they? “Well, I have yet to find where they wrote it.”

ere they not the people you suggested should go off and commit suicide at the Irish Congress of Trade Unions (Ictu) conference in 2007? “That wasn’t about a boom-and-bust issue . . . It was trying to get the Ictu to hold their nerve and keep productivity high.”

Anyway, it was the collapse of Lehman Brothers that did the real damage, Ahern insists. “That decision will in history be written as the biggest mistake that American administration ever made, because Lehmans was a world investment bank. They had testicles [sic] everywhere.”

AHERN ACCEPTS THATthe Mahon tribunal was entitled to look into his affairs, but – as we know too well – he bitterly resents the interrogation about his marital separation, his daughters, his bedroom. Yet wasn’t it Ahern himself who first introduced all of these issues as the reasons behind the various dig-outs he received? “I had answered the stuff in the letters,” he says with a heavy sigh. “It was all in the letters . . . I wouldn’t have been renting a house or buying another house if I wasn’t separating, ’cause I would have been living in my own house.”

July, 1998

Ms. Mary Harney,
Tanaiste & Minister for
Enterprise, Trade and Employment.

Dear Mary,

I refer to your letter of 1 July and our previous correspondence concerning regulation of the financial services sector, and in particular, your proposal that a working group be established to examine the feasibility of creating a single financial services authority.

Notwithstanding our agreement on the value of a single regulatory authority, I am of the view that the immediate establishment of a working group to look into this question, under the terms of reference described, would pre-empt various processes currently in train, and, in particular, cut across the work of the Moriarity Tribunal,

July, 1998

Ms. Mary Harney,
Tanaiste & Minister for
Enterprise, Trade and Employment.

Dear Mary,

which was established on a statutory basis by the Oireachtas. You will recall that the terms of reference of the Moriarity Tribunal include a remit to make whatever broad recommendations it considers necessary or expedient for enhancing the role and performance of the Central Bank as regulator of banks and of the financial services sector generally. The bank has already made a lengthy submission on supervisory matters to the tribunal. I consider that the findings of the Tribunal will be the appropriate point of departure for a broader examination of arrangements for the supervision and regulation of financial institutions that you describe.

In this context, you might recall Government Decision S.25989 of 3 March, 1989, in which the Central Bank was given the role of supervising the main financial institutions in the State: The Government decided at that time that the fragmented system of supervision of financial institutions should be encompassed under a single supervisory authority. The Central Bank was chosen as the wisdom of instituting a single new supervisory body was considered questionable.

On the subject of consumer protection, in this context I would mention in passing that the information gathered by the Oireachtas Committee on Finance and the Public Service in the course of its scrutiny of practices in other European countries would suggest that it is only in a minority of countries that any element of consumer protection, other than in the broadest sense, is vested in the agency charged with the

July, 1998

Ms. Mary Harney,
Tanaiste & Minister for
Enterprise, Trade and Employment.

Dear Mary,

regulation of financial institutions.

Yours sincerely

____

Charlie McCreevy
Minister for Finance

July, 1998

Ms. Mary Harney,
Tanaiste & Minister for
Enterprise, Trade and Employment.

Dear Mary,

Mr. O'Gorman } to see

Secretary General } to see

Minister

from Robert Carey

As part of ongoing correspondence on the regulation of the financial services sector, and in particular, the possibility of creating a single financial services authority, the Tanaiste and Minister for Enterprise, Trade and Employment has replied to your Letter May 13 noting your expressions support for the idea of a single regulator and proposing that a working group be established to examine the feasibility of creating a single financial services authority.

Although this Department has no objection in principal to the establishment of a working group, the exact terms of reference of the group and its composition are matters that will need to be worked out in detail.

In general, the Department would be anxious to ensure that its lead role in relation to the regulation of financial institutions is not undermined. If a single regulator is to be established, an expanded role for the Central Bank has traditionally been this Department's preferred option. In this context, you might recall Government Decision S.25989 of 3 March, 1989, in which the Central Bank was given the role of supervising the main financial institutions in the State. The Government decided that the fragmented system of supervision of financial institutions should be encompassed under a single

July, 1998

Ms. Mary Harney,
Tanaiste & Minister for
Enterprise, Trade and Employment.

Dear Mary,

supervisory authority. The Central Bank was chosen as the wisdom of instituting a single new supervisory body was considered questionable at that time. Recent events may provide reason to reconsider this position.

The Tanaiste indicates clearly in her letter that she is in favour of the establishment of a new body with a clear mandate and ethos reflecting a more proactive approach to regulation. The Central Bank currently regulates the bulk of the financial services sector without any cost to the exchequer. A new body established as the single financial services authority could be established as a semi-state body, a company limited by guarantee (such as Britain's new Financial Services Authority) or a department of the Government. The establishment of such a body would inevitably incur start up costs, probably being borne by the taxpayer. Given the logistical problems involved in transferring functions to an already existing supervisory body, the transfer to a new body with no track record might prove even more problematic and cumbersome. The experience and expertise developed by bank examiners is specific to the regulatory environment. With the growth of derivatives over recent years this is increasingly the case so that any new agency to be effective would have to recruit staff now with the Central Bank or with some regulatory agency abroad.

The question of timing of the proposed working group's report also arises in the context of the Moriarity Tribunal. You will recall that the terms of reference of the Moriarity Tribunal include a remit to make whatever broad recommendations it considers necessary or expedient for enhancing the role and performance of the Central Bank as regulator of banks and of the financial services sector generally. The Bank has already made a lengthy submission on supervisory matters to the Tribunal. To avoid pre-empting the work of the Tribunal, the report of the proposed working group would have to await the outcome of the Tribunal and take account of its recommendations.

A draft reply to the Tanaiste's letter of July 1, along the lines outlined above is attached.

July, 1998

Ms. Mary Harney,
Tanaiste & Minister for
Enterprise, Trade and Employment.

Dear Mary,

PROGRESSIVE DEMOCRATS
an páirtí daonlathach

From Good To Great

Continuing Ireland's Radical Transformation

General Election Manifesto 2007

Dear Voter

By any measure, our country has made remarkable progress in the past ten years. Over two million people at work, virtual full employment, an end to enforced emigration and – finally – the prospect of lasting peace in Northern Ireland. This is progress many of us could not have dreamt of just a short time ago.

But it did not happen by accident. It is the fruit of your hard work and good management of the economy. It is also the fruit of good, experienced, steady government.

Ireland is in the process of continuing radical transformation – it is not something that is yet complete, or to be taken for granted. This country is unrecognisable from the failed economic wreck of the mid-1980s. The pace must be kept up if Ireland is to remain at the forefront, to remain the envy of nations across the globe – and most importantly remain a country that can deliver employment and prosperity to its population.

Our economic growth has provided the resources to make unprecedented investment in essential public services such as health and education, and in our infrastructure. This investment has improved both the quality of life that Irish families now enjoy, and Ireland's competitiveness.

The initiative and enterprise that brought about this dramatic change was unleashed by the policies of low taxes, competition, and investment in innovation and enterprise, which the Progressive Democrats have championed in government. These policies have resulted in record inflows of investment and the development of a vibrant indigenous enterprise sector that can compete successfully on world markets.

Although we have achieved much success, we still face major challenges. Above all we face the challenge of ensuring that we continue to develop in an environmentally sustainable way, yet in a manner that continues to meet the needs and expectations of a growing population.

This challenge can only be met by an outward looking, confident and development-orientated society that is open to innovation and change. Such a society will have the resources, flexibility and creativity to meet our environmental obligations by way of the sensible and workable policies to which the Progressive Democrats are committed. It will also ensure that we do so without damaging the employment prospects of our children.

The fundamental issues for this Party - indeed for Ireland - are:

- Sound public finances and progressive taxation policy
- Pro-enterprise, pro-competition polices and reforms
- Comprehensive environmental, energy and climate change initiatives
- Major public sector reform of methods and accountability
- Continuing reform and transformation of our healthcare system
- Delivering transport infrastructure, for today and the future
- Educating our population for continued success and prosperity
- Making sure our communities are safe and that justice is delivered

This manifesto deals comprehensively with these issues and with so much more. It sets out our vision for our new Ireland, and the new opportunities it presents us.

While there has been some focus on job losses recently, it is important to note that new job gains continue to exceed job losses by a substantial margin. This position will only continue as long as our country continues to be both a magnet for inward investment and a place where indigenous enterprise can invest with confidence.

The twin objectives of environmental sustainability and full employment will not be achieved by anti-growth, anti-development policies. Neither will they be achieved by taking our prosperity for granted. They will certainly not be achieved by electing to government parties who are either indifferent or openly hostile to enterprise, initiative and progress.

I invite you to consider our proposals for continued prosperity and progress and to support the return of the Progressive Democrats to government by voting Number One for our candidate in your constituency.

Michael McDowell

Michael McDowell TD
Party Leader

Overview

- Economic Growth forecast at 5% p.a.
- Day-to-day spending to grow in line with economic growth plus inflation *(per Towards 2016)*
- Capital borrowing requirement to rise to 5% of GNP.
- Tax revenues to grow at 1.1 times (nominal) economic growth.

Economic Growth Forecasts:

We assume GNP/GDP growth of 5%, in line with the ESRI's Medium-Term Review (MTR), which is the most respected economic forecasting agency in the state. It is lower than the average for the past five years, which is 5.4%. Note that this period included the aftermath of the bursting of the tech bubble, and "9/11". We are confident that sensible economic policies, not least continuing reductions in tax rates, will underpin this growth, and in fact there is every chance that growth might be stronger – but in order to be conservative we are using the ESRI's forecasts. Note also that this is an average level – undoubtedly there will be years when growth is significantly stronger, and some when it's significantly weaker. But 5% is a reasonable figure to use, on average.

Year	GDP Growth
2001	5.9
2002	6.0
2003	4.3
2004	4.3
2005	5.5
2006	6.1
Average 01-06	5.3%

Tax Revenue Forecasts.

Tax revenues, in the absence of any tax changes, will usually grow by a little more than the growth of the economy. This is because of the progressive nature of the tax system – as incomes increase, they yield more tax. Furthermore, basic goods tend to be taxed at lower rates of VAT/excise, while luxury goods and services have higher rates. So as the economy grows, a higher proportion on national income is spent on higher-taxed-items, so that tax revenues grow more quickly than the economy does. The table below shows this trend. In fact, as there were substantial tax cuts during this period, "normal" tax revenue growth would have exceeded nominal GDP growth by even more than the table shows.

% p.a.	Tax Revenue Growth	Nominal GDP growth
2003	9.6	6.9
2004	10.3	6.2
2005	10.3	9.2
2006	16.0	9.1

We take a cautious approach, however, and assume that tax revenues, without any policy changes, will grow by 1.1 times GDP growth. So if the economy grows by, say, 5%, tax revenues are estimated to grow by 5.5%, and if growth is 10%, taxes will grow by 11%, and so on. This, we believe, is a factor which would be endorsed by most forecasters, and the numbers in the table above show its validity.

Government Spending Growth:

We believe that the appropriate level of spending growth in the medium term is the growth in the economy, plus inflation. We are assuming average annual growth of 5%, as discussed above, and inflation of 2.5%, which gives total spending growth of 7.5%. Over the last three years spending growth has indeed tracked economic growth quite well so we think the evidence shows that this is a reasonable assumption.

Towards 2016 endorses this approach to public spending growth, calling for "a public expenditure profile that reflects the growth in the economy" *(Towards 2016, page 16).*

Growing spending in line with economic growth (including inflation) means, on our economic assumptions, that day-to-day departmental spending will rise from €32.9bn last year to €53.4bn in 2012 – an increase of a little more than €20bn.

In many European countries, government spending rises only in line with inflation. But Ireland has a fast growing population, and an economy that is performing well. So we think it is reasonable to grow public spending in line with economic growth, although we also recognise that problems in public services will never be solved only by "throwing money at the problem".

Capital Spending:
Estimating the likely level of capital spending is complex, as in the Exchequer accounts it is usually presented as the level of capital borrowing that will be required, after taking account of capital receipts (from a range of sources such as repayments of loans, or sales of state property or other assets). The Exchequer's contribution to the National Pension Reserve Fund is also included in this category. We are committed to the expenditure outlined in Transport 21 and the National Development Plan, and estimate that this will require an annual expenditure for capital purposes of 5% of GNP.

This is a net figure, as outlined above, and is somewhat higher than the average over the last few years (as a percentage of GNP) to take account of the ramping up of capital spending over the next few years in order to deliver Transport 21 and the NDP. (Note: This 5% of GNP capital borrowing requirement cannot directly be compared to the 5.4% of GNP figure in the NDP – one is gross and one is net, and there are also other definitional differences).

Budget Balance Measures:
The budget balance measure we use is the General Government Balance (GGB), which is the EU-agreed common definition of the budget balance, and which has largely replaced the old Exchequer Borrowing Requirement (EBR). The differences between them are complex, and mainly relate to the exclusion from the EU measure of the State's contribution to the National Pension Reserve Fund (NPRF), as well as the return from the fund (there are also a variety of other differences, which those interested can see outlined each year in the Budget documents). We assume that the net difference between the two measures will be about 1.3% of GDP each year.

Conclusions:
Taking the above assumptions and forecasts into account, we can forecast that if there are no significant tax changes, the government will collect €6.3bn from taxpayers (in 2012 money) more than it needs, or in other words it will run a budget surplus of about 2.3% of GDP. We believe that our plans set out in this manifesto are so prudent that the net national debt will be eliminated by 2013.

New Ireland

Progress Since 1997

This Party has achieved significant progress in reducing tax. The top rate has been reduced from 48% to 41%. Our commitment, should we be re-elected, is to further cut the top rate by another 1% in Budget 2008. There have been substantial reductions in the basic rate of income tax too, down from 26% to 20%. The net effect is that the income tax system has been made considerably more progressive under this government:

- In 1997, a single person on the average industrial wage paid 22% of their income in income tax. In 2007 such a person will pay just 9%.
- In 1997, the top 1% of income earners contributed 14% of the total income tax take. Now they contribute over 20%.
- As a result, unemployment has tumbled from "old Europe" levels of over 10% with emigration under the opposition parties to less than 5% with considerable immigration today.

Current Background

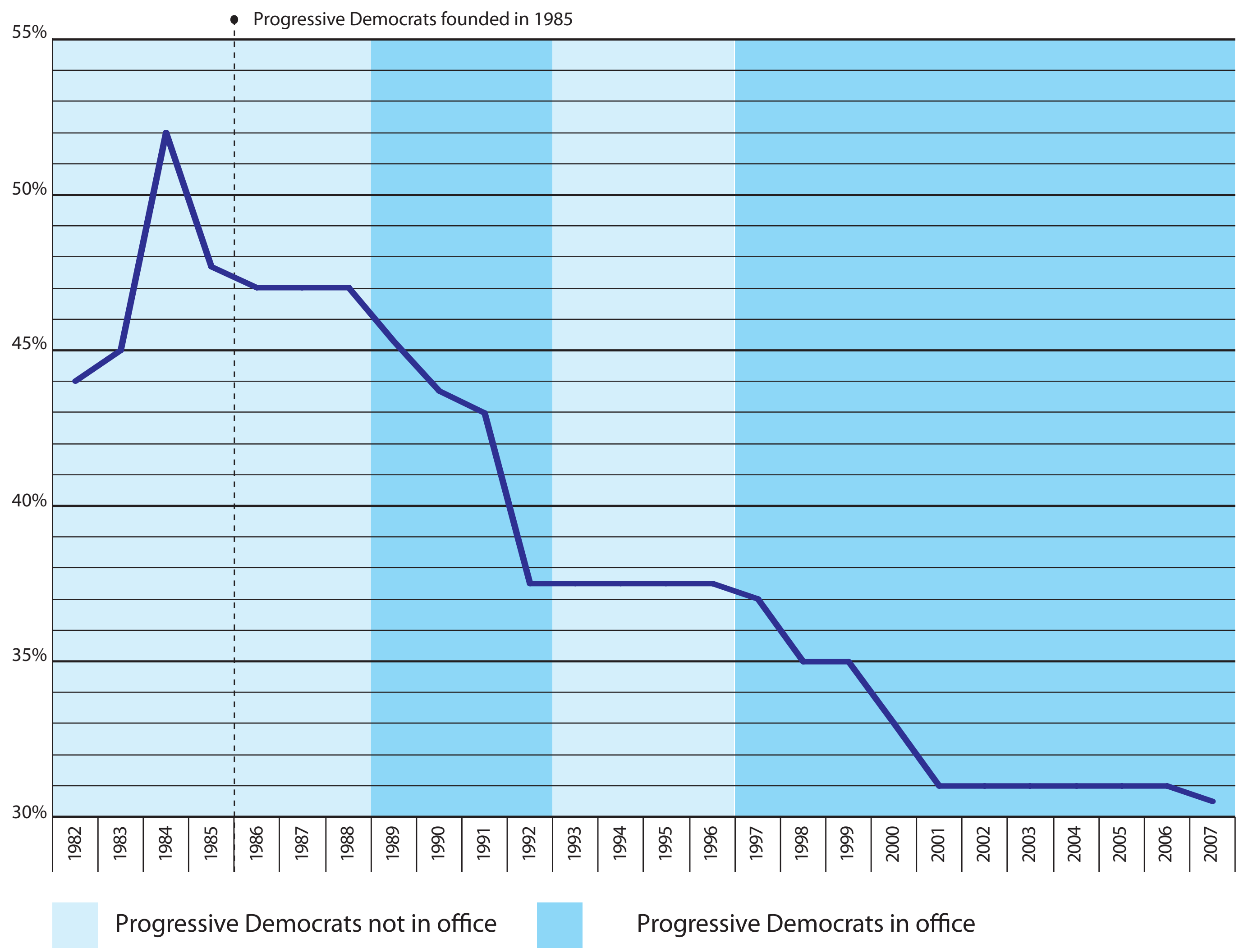
There is a consensus amongst economic commentators that apart from a major external or internal shock the Irish economy should continue to grow strongly in a range from just under 5% to 5.7%. This will generate a considerable increase in the resources available to the Exchequer.

The question is whether all of these resources should be spent further growing public expenditure? The Progressive Democrats believe in returning a significant portion of the increased resources to the people by way of tax cuts. The Progressive Democrats believe that tax reduction should be a strategic objective for the next government. We believe that it will be possible to significantly reduce the tax bill of middle-income earners while allowing for generous growth in public spending.

New Opportunities

Subject to maintaining budgetary prudence, in government the Progressive Democrats will:

- Adjust tax bands so that a couple, both earning, can earn at least €100,000 and only pay income tax at the standard rate. This would mean that a single worker could earn €50,000 and only pay income tax at the standard rate.
- Increase tax credits so that couples earning up to €40,000 will pay no income tax. This would mean that a single worker could earn €20,000 and pay no income tax.
- Reduce the higher rate of income tax to 38% in the lifetime of the next government.
- Reduce the lower rate of income tax to 18% in the lifetime of the next government.
- Ensure no new, additional taxes / levies on employment.
- Guarantee that those earning the minimum wage pay no income tax.
- Continue to increase tax credits and bands so that inflation is not used as a tax-raising mechanism.



Average Income Tax Rate

- Increase tax credits so that couples earning up to €40,000 will pay no income tax. This would mean that a single worker could earn €20,000 and pay no income tax.
- Reduce the higher rate of income tax to 38% in the lifetime of the next government.
- Reduce the lower rate of income tax to 18% in the lifetime of the next government.
- Guarantee that those earning the minimum wage pay no income tax.
- Continue to increase tax credits and bands so that inflation is not used as a tax-raising mechanism.
- The State development agencies will prioritise the attraction and development companies with strong product development and international sales capabilities through focused support for these activities.
- Ensure that such companies have access to competitive sources of finance.
- Invest over €8billion in Science, Technology and Innovation to build on the success of Science Foundation Ireland and the Programme for Research in Third Level Institutions.
- Double the output of 4th Level graduates and provide greater support for applied R&D, and enable Ireland to join the ranks of the world's most innovative societies.
- Complement Ireland's historic commitment to education by a €26billion investment in education and training that will ensure we have the level of education and skills needed to compete in the rapidly changing world of the 21st century.
- Give a firm commitment to the investment in needed infrastructure to boost productivity and promote balanced regional development including the completion of the inter-urban motorway network.
- Guarantee a state-of-the-art communications network, driven by competition, to which all players in the market have equal access.
- Fund nationwide broadband coverage.
- Support consideration of the Dublin commuter belt as a 'single region' in terms of job creation and investment-seeking activity by the IDA and other agencies and aim to create a series of economic clusters within the region.
- Encourage the establishment of a voluntary database of workers and professionals living in the commuter region who are interested in working locally, to readily inform multi-national organisations of the adequate supply of skilled workers.
- Consider the creation of a dedicated taskforce to identify the critical infrastructure needs of the commuter belt and allocate targeted resources to accelerate the development of projects in the region.
- Continue to reduce as much as possible the administrative and regulatory burden on small and medium size businesses, to foster and encourage this vital sector.

Promoting Competition
Effective enforcement of competition is central to our international competitiveness and providing value for money to consumers.

The Progressive Democrats in government will:

- Enhance the implementation and enforcement of the 2002 Competition Act by legislating to:
    - o Allow Competition Authority to prosecute cases on its own initiative.
    - o Provide for the imposition of administrative fines by the Competition Authority where anti-competitive activity or abuse of dominant position is established on the balance of probabilities. If necessary constitutional provision will be made to this end.
- Ensure that competition cases, receive priority in the scheduling of court cases. If necessary, we will establish a dedicated "Competition Court" in order to fast-track competition cases.
- Require the Competition Authority to accelerate the pace at which it completes reports into specific sectors. Reports should normally be completed within strict time limits. It will require a formal vote of the Authority to permit a report on a sector to exceed the pre-determined limit.
- Commit the Government to respond, within 6 months at most, to any formal proposals from the Competition Authority for the improvement of national competition policy.
- Ensure that the planning process is not used to inappropriately stifle competition by ensuring that Local Authorities provide adequate zoning for retail space.
- Require planning bodies to have regard to consumer interests and to consult with the Competition Authority if their decisions are likely to have a significant impact on competition.
- Continue reform of the public transport market so as to promote private sector involvement and competition so as to deliver greater choice and value for our citizens.

New Ireland

Progress Since 1997

Rapid economic growth has brought with it unprecedented demand for housing. The market has responded and built over 600,000 houses since 1997. In 2006, the total number of houses and apartments completed was 93,419. In Ireland we are now producing homes at a rate of over 20 per 1,000 residents, the highest in Europe. This has enabled an unprecedented number of people avail of home ownership. But rising house prices keep home ownership out of reach for too many.

Current Background

A increasing supply of high-standard housing should be available at affordable and reasonable cost to those on the average industrial wage. Increased supply is the key element in addressing the property price issue facing prospective Irish homebuyers. 'High-standard' not only refers to the size and condition of the home, but also its location in terms of the occupants family and work connections.

New Opportunities

In government, the Progressive Democrats will:

- Continue our successful policy-approach of significantly increasing housing supply to reduce the cost burden on homebuyers.
- Abolish stamp duty for first time buyers
- Make stamp duty fairer by "banding" rates so that owner-occupiers pay the higher rate only on the portion of the price over each threshold

Given the critical nature of this particular reform we will:

- Implement our reform with an immediate effect.
- Implement our reform via legislation enacted before the new Dáil rises for the 2007 Summer Recess.

- These changes will mean:
    - o Reducing stamp duty to be paid on the average national house price by €8,250 - from €15,500 to €7,250, and reducing stamp duty charge to be paid on the average home in Dublin by €17,050 - from €32,250 to €15,200

- Release 660 acres of land near Dublin city centre and over 500 acres in Cork City Centre (North Docks and South Docks) for development. Development of housing will be prioritised.
- Invest €17billion under the National Development Plan to expand the range of tailored social housing supports and an accelerated programme of renewal and improvement of the existing stock.
- Invest €4billion in support for people seeking accommodation in the owner-occupied sector through the provision of affordable housing; to assist in the upgrading of the physical condition of homes with particular emphasis on those who are most in need including the disabled and the elderly, under the National Development Plan.
- Evaluate the application of the Dublin Docklands Development Authority model to others large urban area developments.
- Make more affordable housing available by holding open, transparent procurement competitions for available State-owned land. The land should be provided to the developer that scores best against pre-published State -set criteria, not necessarily the one offering the highest monetary price.
- Build on progress made under the Homelessness – an Integrated Strategy 2000, to continue to address factors resulting in homelessness - not only related to the provision of accommodation, but also to health, care and welfare, education and training and prevention in order to effectively tackle homelessness in Ireland.
- Prioritise the development of high-standard affordable homes by amending and expanding the use of Special Development Zones and / or a new permit scheme.
- Create a National Water and Sewerage Services Office in the Environmental Protection Agency to ensure the provision of an adequate and efficient network of water and sewerage infrastructure, and oversee the implementation by Local Authorities of Water Services Investment Programmes. It will oversee and expedite water service provision to new developments. This will speed up supply and reduce the cost of new, as the cost of the developer providing services will not be passed on to the buyer.

Our Core Values

- Build in Ireland a democratic society organised on republican principles, in which legislation, where possible, allows citizens freedom of choice free from unnecessary state interference and regulation, taking into account the views of minorities.

- Promote policies that allow individuals, each in their own way, reach their maximum potential and protect and help weak and deprived members of society and promote social justice for all

- Establish and maintain laws that safeguard the rights of the individual and to minimise unnecessary regulation by the State in the affairs of its citizens.

- Ensure that while society gives the individual rights, the individual has a corresponding responsibility towards society.

- Promote liberal economic policies that: foster competition and innovation; reward initiative and encourage ever-greater economic and political participation by all its citizens; and promote subsidiarity and balanced regional development.

- Foster a fair and just system of taxation that promotes the work ethic and encourages creative endeavour.

- Ensure that the wealth produced by this nation is wisely used to afford a decent standard of living to all its citizens.

- Ensure that the legislative, judicial and administrative arms of government function independently, effectively and with accountability to safeguard the common good.

- Conserve, protect and enhance the natural, the physical and the built environment of Ireland, promote sustainable development and foster civic awareness and pride.

- Promote unity of the Irish people by peaceful means based on consent and pluralist principles.

- Promote and maintain laws that reflect the independence of both Church and State while valuing the contribution to society of religious and philosophical beliefs.

- Promote and support the development of community and voluntary organisations.

- Safeguard and develop all strands of Irish culture, language and heritage.

- Promote a European Union dedicated to liberal and democratic principles.

Regulatory Strategy

The Authority adopted a "principles led" approach to supervision from its inception in 2003, which essentially placed Boards and Management of banks at the centre of responsibility for the prudent conduct of business. The Authority was legally obliged, at least 3 months before the beginning of each year, to prepare a strategic plan and submit this plan to the Minister of Finance. The plan had to specify the objectives of the Authority for the financial year concerned, the nature and scope of the activities to be undertaken and the strategies for achieving these objectives. As soon as possible after receiving this plan, the Minister had to arrange for it to be laid before both Houses of the Oireachtas. When this had been done, the Authority was required to publish the plan and take all reasonable steps to implement it. So, to reiterate, the process was Authority, Minister, Houses of the Oireachtas. The principles-led approach was thus not the sole decision of the Authority. This approach to supervision was followed by all EU countries. The USA is the main proponent of rules-based regulation but this did not protect it from issues with Bear Stearns, Lehman Brothers, AIG, Wachovia and others.

The strategy also set down the objectives of the Authority. One of its objectives was that its regulatory approach would facilitate innovation and competitiveness. It is clear that both of these elements played an important part in the increased availability of credit in Ireland in the years before the crisis, through a combination of more banks entering the market and more innovative types of lending products being developed.

To have taken measures to stifle these developments would have conflicted a fundamental strategic objective of the Authority as mandated by the Minister and the Oireachtas.

In January 2004, a white paper entitled "Regulating Better" was issued by Government to improve national competitiveness. The paper called for wider consultation and more regulatory impact assessment on any new regulations. This illustrates the context in which all supervisory initiatives of the Authority required extensive consultation with a wide range of what were termed "stakeholders"-

-Govt. depts., representative bodies, the Industry and Consumer Panels, banking schools in the Universities. Detailed regulatory impact analysis was extensive. In fact, the Authority also put in place an arrangement with industry called the "Stakeholder Protocol" with enshrined time commitments by the Authority to respond to industry requests for regulatory approvals, issuance of the findings of inspection reports etc. I can understand that initiatives such as this formed a perception of the Authority as a "can do" entity, willing to prioritise industry demands rather than appearing more detached and discerning. This is something which I believe, in hindsight, the Authority got wrong.

In September 2006, the Government published a review of the future of the financial services industry in Ireland entitled "Building on Success". I want to bring two items from the report to your attention:

i. The paper asserted a growing awareness in both Ireland and Europe that poor quality or unnecessary regulation could be a barrier to competitiveness and growth and such regulation could alienate citizens and enterprises through imposing disproportionate compliance costs.

ii. The paper did not propose any increased prudential supervision or suggest a tougher, more burdensome regulatory regime.

The growth in private sector credit arose mainly from the appetite for property acquisition and associated construction activity. This expansion in these areas was due to a number of factors including strong economic growth, an increase in the level of household formation, very low interest rates, lower personal tax rates, a vast range of tax incentives for property investment, the desire of Irish people for property ownership, a "feel-good-element" generated by increasing property values which quickly seasoned loan-to-value ratios, and all supported by readily available bank loans. A further and extremely important factor was the consistent pattern of very positive economic commentary in relation to the performance and prospects for the economy and the property market from the Economic and Social Research Institute, the Central Bank and the Department of Finance.

In formulating its strategy, the Authority always took full account of the output of these authoritative sources, which predicted that the Irish economy would continue to show growth above the EU average and that the property market would experience a soft landing. The Authority relied on the Central Bank which maintained an economic services division with 86 staff, including a dedicated Financial Stability Department, to monitor and assess the overall health of the financial system; there were no economists in Banking Supervision Department. Had these predictions held, there would not have been a bailout.

I do not think, even with the benefit of hindsight, that the Authority, in the context of the time, would have assumed a different approach to supervision. I have come to this conclusion bearing in mind the following:

- The capital requirements in Ireland were higher than the EU demanded;
- The absence of any strong views from the financial stability perspective that a more draconian regime of supervision was warranted;
- The fact that the introduction of a tougher supervisory regime in Ireland compared to other jurisdictions would have conflicted with Government policy to promote the strength and profitability of the financial services industry in Ireland and its attractiveness as an international financial services location.

R1c – Appropriateness of the macro economical and prudential policy

R5c – Analysis of key drivers for budget policy

Information Summary (Section 33AK)

Note: All references are aggregated.

Document category	**Time period**
CBFSAI papers and Board discussions relating to • Macro-economic performance • Financial Stability Reports • Pre-Budget letters • Related economic reports	2004-2007

Financial Stability Report: 2004

- Staff of IFSRA contributed to the preparation of the report under the aegis of the joint Financial Stability Co-ordination Committee. The presentation of the report was noted as a good example of close cooperation between the two sides of the organisation.
- A presentation was made to the CBFSAI Board on the different methodologies used in assessing whether or not there was now a house price bubble in Ireland and the ability of the banking system to withstand a sharp fall in property prices.
- The Committee noted the following points:
  - interest rates were now determined by the ECB on a euro system basis.
  - credit growth was not a problem in the euro area as a whole however the Bank's capacity to restrict the rate of credit growth was very limited.
  - possible options on restricting credit growth were being considered but the Bank was not aware of any actions being taken by other national central banks in the Eurosystem which the Bank was not already taking.
  - the Bank continued to alert the industry and the public to the risks of excessive credit growth.
  - property prices were continuing to increase at an unsustainable level but there was no conclusive indication that a price bubble existed.
  - If prices continue to increase, however, the risk of a price bubble would become more acute.
  - a collapse in property prices would not only affect the quality of security for bank loans, it would also have widespread economic implications as the construction industry was now a very major component in the Irish economy.

CB00222

Pre-budget letters and budget: 2004

- The CBFSAI Board discussed the draft annual pre-budget letter. The draft contained the following statement: "*Fiscal policy could also play a role in smoothing the adjustment of demand for property by limiting its more speculative components. In this regard, it would seem appropriate, for example, to allow no further extensions to the termination date of mid-2006 for the range of tax driven incentive schemes for housing."*
- The need to limit overheating pressures to protect competitiveness was also mentioned. The letter included the following statement: *"In fact, a case could be made for a mildly restrictive stance in the context of full capacity growth*."
- Regarding the overall budget balance, a broadly neutral stance was being recommended. In reviewing the draft letter, it was agreed that the Bank should emphasise risks regarding the economic forecasts.
- The Governor advised the Board that he would issue the letter after meeting the Minister. Later in the quarter, the Board noted that the Governor had met the Minister for Finance before issuing the pre-budget letter.
- After the budget was announced, the Board discussed the budget outcome and it was noted that the advice from the Governor was not fully adhered to.
- Private sector credit growth was discussed but no recommendations were made to slow this down.

CB00231 & CB00260

Autumn bulletin: 2004

- Regarding the content for the "Autumn Bulletin", the CBFSAI Board had already addressed the risks to the housing market in some detail in the Financial Stability Report.
- It was agreed that further commentary on the housing market would be unnecessary and that commentary should focus on the broader economic perspective and outlook.

CB00241

Discussion on the content of the bulletin focused on the fiscal imbalances in the US rather than on the domestic problems with credit growth and house price inflation.

CB00249

"Economist" Articles on the Irish economy: 2004

- A series of articles on the Irish economy, published by the 'Economist' magazine in October 2004 was discussed at CBFSAI Board Level.
- Emphasis of the discussion was on the positive aspects of the series.
- The minutes do not show discussion on the mention of the 'property frenzy' or 'house price bubble'.
- The articles also highlighted a property crash as the most threatening risk ahead.

CB00247

Draft Financial Stability Report: 2005

- In relation to the comments included in the draft Financial Stability Report 2005, the CBFSAI Board noted that, in the absence of national control of monetary policy, it was particularly important that the Minister be fully informed regarding the Board's concerns when framing fiscal policy and the Governor will bring the issues to the attention of the Minister.

CB00331

Spring Bulletin: 2005

- A draft comment for inclusion in the Spring Bulletin 2005 noted the following on the importance of the construction sector:

"*With the strong performance of the construction sector in recent times, this sector now accounts for nearly 12 per cent of total employment; this share is about 50 per cent greater than in most other developed countries. At some point, the share of construction in total employment will inevitably be reduced. It will be important to ensure as far as possible that this labour can be absorbed into other sectors of the economy without disruption*."

"*Regarding mortgage credit, although it appears to have peaked, it is still increasing very rapidly at about 25 per cent a year; this is some three times the increase in nominal disposable income. The easing of house price increases and somewhat reduced housing construction should, with a lag, contribute to a lowering in credit increases to a more sustainable pace. However, until there is some evidence of this, mortgage credit growth continues to be a matter of concern*."

CB00286

Financial Stability Report (FSR): 2005

- There was a CBFSAI Board discussion on the draft Financial Stability Report (FSR) for 2005 of potential actions to be taken by both the Authority and the Board in response to the risks outlined in the Report.
- It was agreed that further analysis would be undertaken of credit growth to assess whether "*there are grounds for serious concern*".
- The Bank was to further examine the real risks to the system and to reflect its considered view in the published Report.
- In a later discussion of the final draft of the FSR, it was agreed that the tone of the published version of the FSR "*should not be too strident because fundamentals help to explain, to a significant extent, the developments to date but it was important to emphasise the risks going forward*".
- It was confirmed that the Report would be published with a press conference and the Director General and the CEO of the FR would chair a further round table meeting with the principal lenders to discuss messages from the Report.

CB00331

Central Bank Strategic Plan: 2007-2009

- The Central Bank 3-year Strategic Plan was discussed by the CBFSAI Board in mid-2005.
- Key extracts from the Plan relating to CBFSAI responsibility are below:

"*Use our economic, financial and monetary expertise, and our institutional independence, to influence other domestic policymakers; and ensure that other policymakers have the information and tools available, to take decisions on policies that support low inflation, growth and financial stability*".

"*The financial system has evolved as a more global, integrated and complex system. This has led to greater financial stability and risk management challenges for the Central Bank, including*

- *managing and aiming to reduce economic, financial and operational risks;*
- *balancing the financial risks we are willing to bear on our investment assets, against the rate of return we are aiming for;*
- *developing crisis management procedures and business continuity arrangements, to be in a position to deal with major disruptions to financial activity or to the financial system*".

"*We must take account of the economic and financial environment facing the Government in carrying out our responsibilities. These issues include:*

- *Greater pressure on Government policies to be in a position to support growth and low inflation, now that monetary and exchange rate policy can no longer be used for Irish purposes;*
- *Pressures on the public finances, given Ireland's need for infrastructure development; and*
- *Balancing Ireland's growing responsibilities in the international community with the need to ensure the domestic economy is safeguarded*."

"*Enhancing our crisis management procedures despite international best efforts to forecast and try to mitigate financial risks, crises can still occur. On* *those rare occasions, it is essential to deal with the damage caused as quickly as possible. We have developed a domestic crisis management framework and are also involved in developing the framework for the EU. We will continue to review and test these procedures, to ensure that they are well geared for dealing with any such events*."

CB00309

Household Mortgage Indebtedness: 2005

- A paper on household mortgage indebtedness which was presented to the CBFSAI Board examined whether the personal mortgages-related aspect of growing indebtedness was capable of being explained by developments in the macro economy and banking sector over recent decades.
- It also warned of potential risks from a deterioration of the 'fundamental driving forces'.

CB00364

Steps taken to deal with Financial Stability Risks: 2005

A document outlined steps taken up to Q3/2005 to deal with Financial Stability Risks, as follows:

Macro-level:

- Publications – most importantly FSR,
- Roundtable discussions with banks,
- Stress testing,
- increase Consumer awareness;

Micro level:

- On-off site monitoring,
- specific measures around 100% LTV mortgages,
- meetings with CEOs of banks.

CB00368

Pre-Budget letter and budget: 2005

- The letter commented on the macro-economic situation mentioning the high level and rapid increase in the private sector credit, and an expectation of a gradual decline in housing output, "*however, a more abrupt adjustment cannot be ruled out*".
- The letter recommended a limitation in any indirect tax changes in the 2006 Budget, and in its summary called for a prudent approach to the fiscal stance next year.
- An assessment paper of the budget measures announced later in the year mentioned in its conclusion that it pointed to relaxation of budgetary policy in 2006.

CB00129

"Euro Area and International Developments": 2006

- A Table showing Private Sector Credit Growth, Residential Mortgage Growth and Irish Contribution to Euro Area Money Supply (M3) was included in monthly reports "Euro Area and International Developments", which were distributed before all CBFSAI Board Meetings.
- Private Sector Credit growth is shown as follows:

Year	**%**
2003	17.9
2004	26.6
2005	28.8
2006[1]	28.2 – 30.3

- Similar numbers were reported for Residential Mortgage Lending Growth.

CB00469

[1] first 8 months of 2006

Property risks: 2006

- The Regulator briefed the CBFSAI Board meeting:

  - on proposals under consideration to increase the capital weighting for residential mortgages where the loan to value ratio of mortgages exceeds 80 per cent and introduce a more rigorous stress testing;

  - on the intent to introduce higher standards "in agreement with the Industry" without publicity as the Regulator would not wish the measures to unsettle the market;

  - that, from discussions with the chief lending institutions, the proposals did not appear to raise competitiveness concerns;

  - that discussions would also be held with the Department of Finance before the measures were introduced.

- In a later meeting, it was noted that the Financial Regulator would convey the message to the market that the increase in the risk weighting on certain categories of mortgages should be seen as a relatively low key prudent measure targeted at a specific category of loans and not as an attempt to curtail the availability of credit for house purchases.

CB00391

Macro economy: 2006

- The Governor had met with the Minister for Finance on the Board's views on the domestic economy and the international outlook in accordance with the established practice for periodic meetings.

- The CBFSAI Board considered the commentary for the Spring Bulletin, with inclusion of a risk of a sharp correction in house prices and rising ratio of personal debt to disposable income besides others.

CB00405

- The Board discussed tax dependency on the house price boom which included the following considerations:

"the Exchequer is benefiting strongly from the booming construction sector and the large tax take from it. As indicated, the scale of this sector must contract in due course with a likely sizeable adverse effect on tax revenues". *"These developments have served to increase the economy's already high dependence on the health of the broad property sector to an extent that constitutes a significant risk*."

CB00395

- The Governor briefed the Board on a "substantive" discussion which he had with the Minister for Finance at which he had elaborated on the Bank's views on the economic outlook.
- The Governor briefed the Board that he would also be meeting the Taoiseach after the summer to discuss the economic outlook in advance of preparatory work on the Budget for 2007.

CB00454

Report entitled "Is there a homogenous Irish Property Market?": 2006

- The CBFSAI Board considered a report entitled "Is there a homogenous Irish Property Market?"
- The question addressed in the report was whether, based on historical experience of the property market, any fall in Irish property prices could be expected to occur across all segments simultaneously.
- Key findings included:
  - a high degree of correlation between all residential property types and residential locations;
  - the retail sector had grown at a relatively stronger pace in recent years by comparison with the office and industrial sectors;
  - while the correlation between retail and commercial property was smaller, statistics showed that significant correlation existed.

- On the question of publication, it was agreed that it was important to get the message conveyed in the Report across to lending institutions.
- Consideration would have to be given as to how this should be done as the Bank would wish to avoid provoking an "over-reaction" to the findings.
- It was agreed therefore that the message should be conveyed in the Financial Stability Report.

CB00445

Interim Financial Stability "Update on Risks and Vulnerabilities" Report: 2006

- This document raised the alert on the financial stability risks from private indebtedness, re-accelerating house price growth and strong loan volume growth of the Irish Banks.
- It also raised concerns on the strong rise of loans to commercial property-related non-financial corporates, which had played a minor part in the commentary of former Financial Stability Reports to date.
- Liquidity issues were also raised:

> "*the funding gap continues to widen, suggesting that the risk of a country-specific shock could pose liquidity or refinancing risks for banks*".

- The CBFSAI Board reviewed the assessment in the Draft Financial Stability Report in detail.
- It was agreed that the main issues identified in the Report were the key concerns and the issue would "increasingly arise" as to whether there was any further action which the Bank or the Financial Regulator can or should take to address the risks.

CB00396 & CB00442

Pre-Budget letter: 2006

- The pre-Budget letter to the Minister for Finance was considered. While pointing out a number of specific risks, the letter ultimately recommended a "*broadly neutral Budget for 2007*".
- Domestic risks were outlined in the text:

"*There are also a number of domestic risks, principally surrounding the housing market and the construction sector generally. The re-acceleration in house prices this year is a particular concern, as this upturn does not appear to have been driven by fundamental factors. It seems that a gap may now be opening up between actual prices and prices warranted by fundamentals. International observers such as the IMF and OECD have produced estimates of an overvaluation in the range of 15 to 20 per cent.*

Another indicator that house prices are becoming overvalued is that, based on a debt-service threshold of 40 per cent of disposable income, an increasing proportion of potential buyers are being priced out of the market.

The weight of the construction sector in the economy has increased markedly over the last decade, accounting now for 13 per cent of total employment, an exceptionally high ratio by international standards. Allowing for indirect effects, it would seem reasonable to assume that currently about one in every five jobs is reliant on the construction sector".

"This points to the need for fiscal policy to avoid incorporating too optimistic a scenario for the construction sector and to target a sufficiently comfortable budgetary position to absorb any sudden downturn".

"*Given that the overall price level in Ireland is 23 per cent higher than the EU average and inflation is once again significantly in excess of the euro area average, there is a strong economic argument that the forthcoming Budget should not be framed so that it will contribute to inflation".*

"With the economy operating at around full employment, it would be preferable to avoid a pro-cyclical fiscal stance in 2007 - a message also

conveyed in the recent IMF Article IV report on Ireland. A stimulus to demand can only heighten the risk of exacerbating inflationary and competitiveness pressures to the ultimate detriment of good economic performance."

CB00457

CBFSAI Board meeting: 2006

- It was confirmed that the Minister for Finance was to brief the Cabinet on the Authority's decision to increase risk weightings on mortgage loans and that the consultative panels were to be advised of the decision.
- The Minister's agreement was being sought not to levy the Industry with the Financial Regulator's costs in 2006 associated with the new Market Abuse Directive.

CB00442

Macro-economy: 2007

- Discussion was held in the CBFSAI Board on the first fall in house prices and its potential implications for the economy, the Exchequer and employment.
- The price sensitivity of building land and potential impact on those who had large holdings in building sites was mentioned.

CB00528

Draft Financial Stability Report: 2007

- The Draft of the FSR was discussed in a CBFSAI Board Meeting.
- The first sentence of this draft ended in an option to choose the preferred wording: "*The overall assessment is that financial stability risks have on balance [remained unchanged/very slightly increased] since the 2006 Report*."
- The following key points were raised:

> "*While this has reduced the vulnerability posed by the previous substantial increase in house prices, it increases the uncertainty regarding the future path of prices*."
>
> "*Many commentators have cited arguments in favour of a sharp downturn, namely, the international evidence on house-price cycles, uncertainty over investors' participation in the property market as capital returns are eroded, the sustainability of current rates of immigration and the future direction of monetary policy as important issues. However, the evidence is not convincing on the likely negative impact of these factors. Furthermore, the underlying fundamentals of the residential market appear to be strong and the current trend in prices would seem not to imply a significant correction. The central scenario is, therefore, a soft landing*. "

CB00545

The 'tone' of the 2007 FSR report was discussed:

> *"Following the presentations, there was a detailed discussion on the content on the draft Financial Stability Report. The meeting considered that in the continuing turbulence and uncertainty in the financial markets since early August, the tone and comment in the Financial Stability Report will be of particular importance and sensitivity"*.
>
> *"Care should be taken to ensure that risks are set in context of the strengths of Ireland's strong economic performance and prudential environment*."

CB00584

- It was agreed that particular care should be taken to ensure that comment on risks are not liable to over-interpretation by the international and domestic media. In this context it was suggested that a Box entitled 'House Price Booms and Busts: the International Experience', could be over-interpreted.

- The fall in house prices was also considered:

> "*However, the evidence is ambiguous on the likely negative impact of these factors, the underlying fundamentals of the residential market appear to be strong and the current trend in monthly price developments does not imply a sharp correction. The central scenario is, therefore, for a soft, rather than a hard, landing*."

- International market turbulences were considered:

> *"The international banking system has been affected directly through losses on their US subprime assets and indirectly through holding of investments exposed to US subprime losses, from credit commitments to conduits/special purpose vehicles, and from a general disruption to business. As is the case for banks worldwide, liquidity pressures in the interbank and commercial paper markets are likely to be an issue for the domestic banks. However, the domestic banks report no significant direct exposures to US subprime mortgages and very limited exposures through investments and credit lines extended to other financial companies or special purpose vehicles. The domestic banks' shock absorption capacity does not appear to have been much reduced by these events."*

CB00566

Liquidity: 2007

- The liquidity turbulences were discussed on the CBFSAI Board and the low level of interbank lending for longer periods (over one week) was noted.
- The meeting noted that the Bank had confirmed with the Irish banks that they had no shortage of collateral eligible for the ECB tenders. Accordingly, there was no reason to anticipate any requirement for emergency liquidity assistance.

CB00584

Pre-budget letters: 2007

- The draft pre-budget letter to the Minister of Finance included an additional paragraph regarding the recent financial crisis:

> "*The forecasts for the year ahead are based on the premise that there will be limited effects from possible domestic or external shocks to the economy. In terms of the external environment, international conditions have been favourable reflecting robust growth in Ireland's main trading partners. It is too early to gauge the full impact on the real economy of the current uncertainties in financial markets, nevertheless the risk of a downturn in the international environment must be considered. While the direct impact on the euro area may be limited, there is scope for more of an effect in the US, thereby increasing the downside risks to global growth*."

- House price inflation changes are reflected:

> "*Over the past year, there have been some important favourable developments in the domestic economy - in particular, the large increases in house prices that were apparent up to last Autumn are no longer evident. The levelling off and subsequent moderate decline in prices reflects a softening in demand due to higher interest rates. This development in house prices has been warranted in the light of already high price levels and the need for borrowing levels to fall back to more sustainable rates of increase*."
>
> "*There is a risk, however, that an unduly large downturn in the housing market*

and the construction sector in general could have serious ramifications for the overall General Government position given the importance of property related tax revenues.

"*In light of this and your recent statements, it would be appropriate that the rate of increase in current spending next year is kept in line with nominal GDP growth, a point that was also emphasised by the IMF in its recent Article IV report on Ireland*."

"*Over the past number of years, the growth in the property market has resulted in substantial windfall gains for the Exchequer, most of which appear to have been saved, which was prudent. This permitted a sufficient buffer in the public finances to be in place to cope with a more challenging economic environment. In the current climate, this buffer needs to be maintained, which would imply aiming for a small surplus in the public finances again in 2008. Limiting the growth of current spending would also enable continued development of the country's infrastructure to take place through the National Development Plan*."

CB00684

Six-monthly survey of business sentiment: 2007

- The survey showed a clear deterioration of sentiment:

"*Of the more important results, businesses were generally much more pessimistic with regard to the outlook for the Irish economy. 63 per cent of respondents felt the outlook for the Irish economy was unfavourable, compared to just 23 per cent in the March Survey*".

- Housing output was set to slow more rapidly than previously expected.
- Data from the Department of the Environment, Heritage and Local Government (DEHLG) indicated that there were approximately 56,000 units added to the domestic housing stock in the first three quarters of this year.
- While output looked set to slow towards the end of this year, the Bank was still expecting somewhere in the region of 75,000 completions this year.

- Very few developers, it was suggested by a major Dublin-based construction firm, had actually started any new developments in the last number of months.
- It was suggested that there were at present over 40,000 housing units unsold, with very little movement in the market.
- Some fall in overall house prices next year in the region of 10 per cent was expected. Some regions, however, would possibly experience greater falls than this.

CB00602

Speech by the Taoiseach, Mr. Bertie Ahern, T.D., at the IMI's National Management Conference, The Ritz-Carlton, Powerscourt, County Wicklow, Friday, 4th April, 2008 at 9.00a.m. –

Against that broad background, I would like to turn to the current economic situation. It is, manifestly, a time of great challenge.

The ongoing market turbulence has spread from the United States to global financial markets and has led to downward revisions to global growth forecasts for 2008.

These events have shown how global markets have become more complex and intertwined. The effects of the problems arising from the US sub-prime market spread around the world's financial systems with surprising speed and intensity.

We in Ireland have a very well developed financial system that is one of the most open in the world. Its banking and financial markets are highly integrated with others, internationally. It is hardly surprising, therefore, that we would not be immune from these events.

However, there are a number of factors that have left our banks here in a strong position to withstand the current difficulties on the international financial markets:

- The economic backdrop in Ireland is one of relatively solid performance, with the economy continuing to grow and unemployment remaining at moderate levels. In addition, our public debt is at very low levels by international comparison.
- The indicators that measure the health of the banking system, such as capital adequacy ratios and the quality of loan books, as well as the ability of the banks to fund their operations, all continue to signal a strong state of health for the industry here.
- Our domestic banks have virtually no exposure to the sub-prime mortgage market, or to related instruments, in the US or elsewhere.

Of course, the resilience of the banking sector here is underpinned by the institutional arrangements governing financial stability. The Central Bank and Financial Services Authority of Ireland is the institution charged with contributing to financial stability in Ireland under both domestic and EU legislation. The two pillars of the organisation, the Central Bank and the Financial Regulator, contribute to maintaining financial stability in complementary ways and do so in the closest cooperation on a daily basis. It is within this context that the Central Bank and Financial Regulator have together maintained an active and ongoing dialogue with domestic credit institutions in order to keep issues relating to the domestic banking system under continuous review.

Indeed, these arrangements have played a very important part in how we have been able to deal in this country with the recent market events.

Given these circumstances, I have no doubt that the Irish banking system remains sound and robust.

http://www.taoiseach.gov.ie/eng/News/Archives/2008/Taoiseach's_Speeches_2008/Speech_by_the_Taoiseach,_Mr_Bertie_Ahern,_T_D_,_at_the_IMI%E2%80%99s_National_Management_Conference,_The_Ritz-Carlton,_Powerscourt,_County_Wicklow,_Friday,_4th_April,_2008_at_9_00a_m_.html#sthash.wMSZ8OFT.dpuf

A principles-based approach to supervision imposed general standards and principles on regulated institutions and essentially placed the onus of responsibility for compliance with such principles, and other requirements imposed, on the boards and senior management of the institutions.

The supervisory authority (the regulator) operated a fitness and probity regime to ensure that those in control of the organisation had a proper background and operated control systems that were consistent with the strategy of the bank.

The approach was consistent with that adopted by supervisory authorities in most of the main financial centres, including the United Kingdom.

Internationally, it was considered to be the most appropriate manner of supervision to address the growing complexity of banking, advances in risk management and for facilitating innovation in the industry; the latter being a factor which was considered to have increased the overall resilience of the financial system. Such innovation was identified as a key component in bringing about what had become known as the 'Great Moderation'. This phrase was coined by economists to describe the long-period of pre-crisis macro-economic calm, with stable growth, stable inflation and stable banks (Appendix: Section 1).

Speeches and corporate publications of IFSRA made regular references to the desire to foster innovation and competitiveness and, for the system to work properly, the need to trust those at the helm of financial institutions to act prudently. Given the international trends, a principles-based approach to supervision was also seen as important in developing Ireland as an international centre for financial services. Further, in accordance with the 'Better Regulation' agenda, the financial services industry in Ireland had been given significant influence over the approach to supervision in Ireland. The Financial Services Consultative Industry Panel ('FSICP'), which considered itself the 'lender of last resort' in a regulatory context for the financial services industry in its dealings with the regulator, was a strong supporter of the approach.[3]

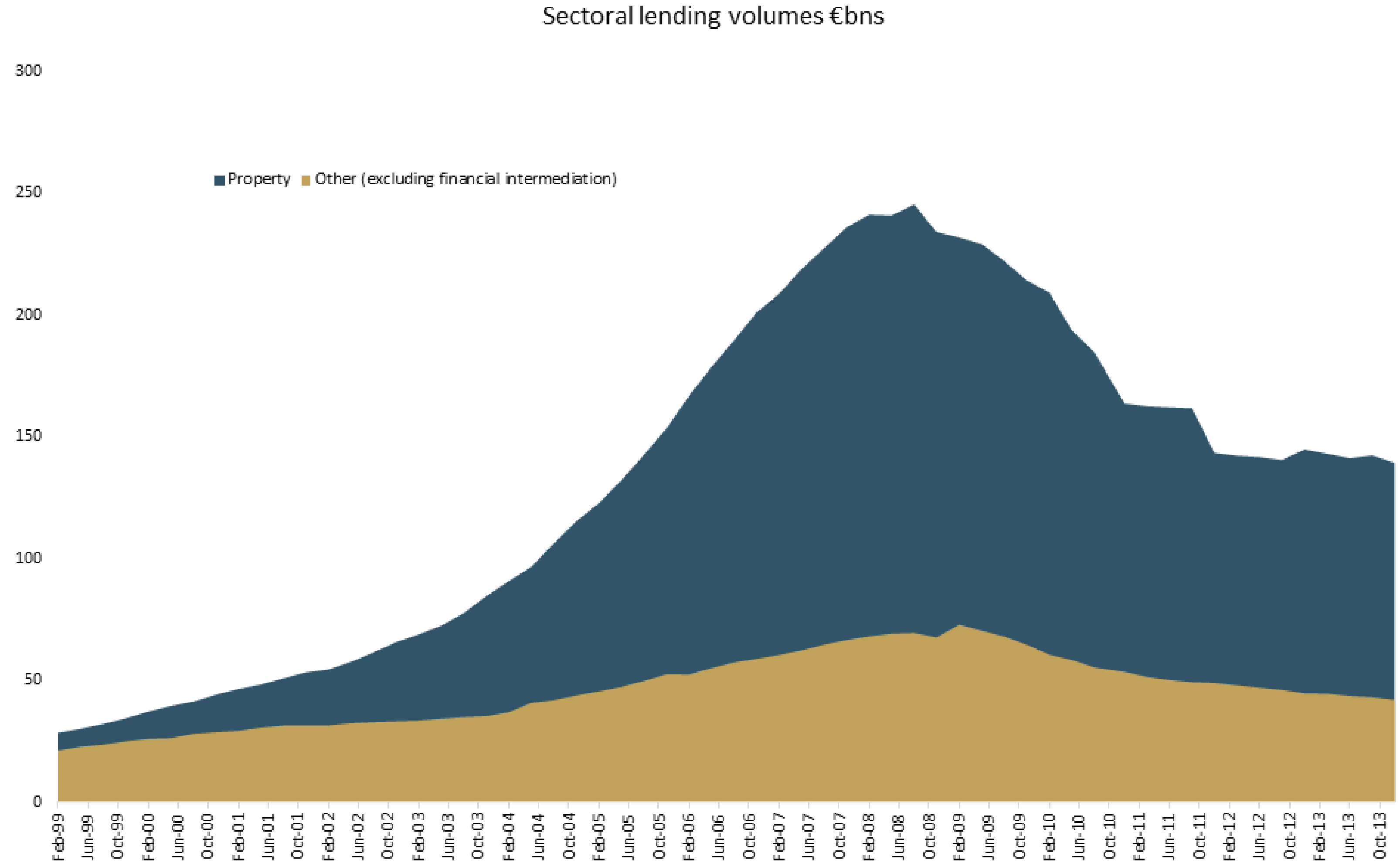
Crucially, principles-based supervision was also promoted as best practice by the International Monetary Fund (IMF). In a paper entitled '*IMF Performance in the Run-Up to the Financial and Economic Crisis: IMF Surveillance in 2004–07,* the IMF identified that, pre-crisis, it had recommended to advanced countries to follow the 'light touch' U.S./U.K. approaches to the financial sector as a means to help them foster greater financial innovation.

Therefore, it is not surprising that another review of the crisis by the IMF *("The Making Of Good Supervision: Learning to Say "No")*, found that, internationally, there were "abundant" examples of supervision: (1) staying on the side lines and not intruding sufficiently into the affairs of regulated institutions; (2) being too deferential to bank management; (3) not being proactive in dealing with emerging risks and; (4) not being comprehensive in their scope.

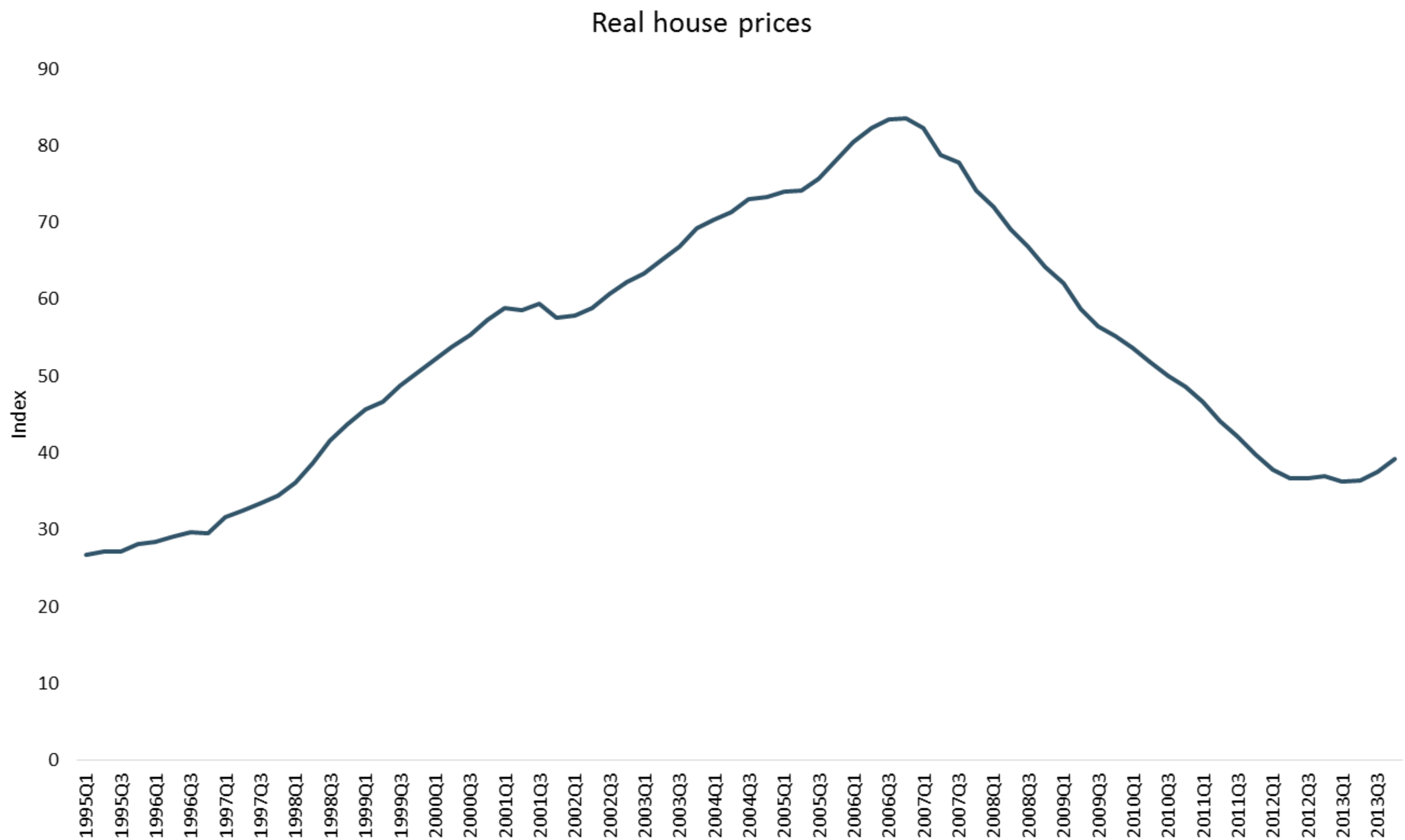
However, no particular system of supervision fared well in the run-up to the crisis. The Spanish approach, which was initially lauded for its rules-based approach and intrusiveness (which involved the placing of large numbers of bank inspectors permanently on-site in the major banks), suffered similar problems to Ireland.

[3] Consultative Industry Panel Annual Report 2005

Massive increase in credit

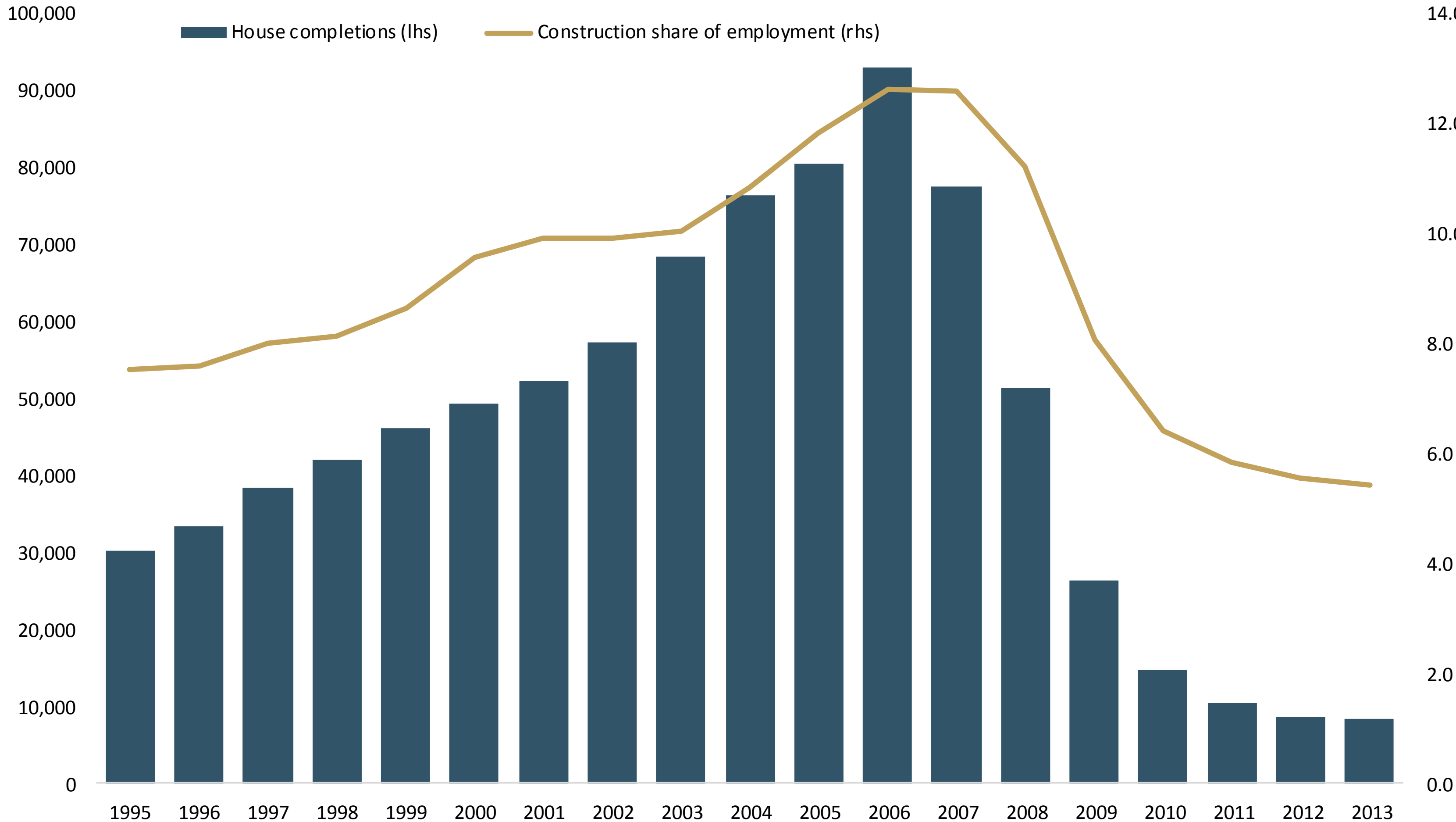


Accumulating imbalances



An Roinn Airgeadais
Department of Finance

Mis-allocation of resources



Witness Statement from Tom Considine to the Joint Committee of Inquiry into the Banking Crisis.

This statement covers the themes and lines of inquiry I was directed to address in respect of my roles as Secretary General of the Department of Finance, March 2002 to June 2006.

Effectiveness of the regulatory, supervisory and governmental regime structure

The role of the Department of Finance was to bring forward to the Minister primary and secondary legislative proposals to maintain an appropriate legal framework for regulating the Financial Services Sector. The Department also represented Ireland in the development of EU legislation governing the regulation of financial services and, in turn, that EU legislation had a strong influence on domestic legislation. By 2002 the bulk of the regulation of the Irish financial sector was the responsibility of the Central Bank of Ireland within the legislative framework provided by the Minister, the Government and the Oireachtas.

The Minister did have an appeal function in relation to the approval of payments systems and he also made appointments to appeals panels and to the Central Bank Board, with the exception of the Governor who was appointed by the President on the advice of the Government. The Secretary General of the Department of Finance was ex-officio a member of the Central Bank Board.

On 20 October, 1998 the Government agreed in principle to establish a Single Regulatory Authority and established an Implementation Advisory Group chaired by Mr Michael McDowell, Senior Counsel. The Group reported on 19 May, 1999 and recommended that the Single Regulatory Authority (SRA) should be an entirely new independent organisation. As a member of the Implementation Group, I proposed an alternative model on behalf of the Department of Finance. This model located the SRA within a restructured Central Bank while providing for increased autonomy for the regulatory function but under the direct control of the Central Bank Board. This alternative model, supported by a minority of the Group, is at Appendix 2 of the report. In the event the Government legislated for a model with a separate Board for regulation but within an overall Central Bank and Financial Services Authority framework. The Regulatory Board was appointed by the Minister for Finance after consulting the Minister for Enterprise, Trade and Employment and did not include a representative of the Department of Finance. The new two board model came into operation on 1 May, 2003.

The Financial Services Regulatory Authority published a Strategic Plan for the years 2004 – 2006. This Plan stated the Authority believed that a mainly principles-based supervisory system would deliver a good balance between having a competitive industry and requiring high entry standards for doing business. That Plan stated that a key part of the approach would be “Putting a comprehensive on-site review process in place”.

The Government’s White Paper “Regulating Better” was published by the Department of the Taoiseach in January, 2004. It identified the principles of good regulation as: Necessity, Effectiveness, Proportionality, Transparency, Accountability and Consistency. The White paper advised that “The recommendations and actions in this White Paper are best seen in the context of the continuing drive for competiveness and people’s expectations of high quality public services”.

The 2006 Annual Report of the Irish Financial Regulator (page 26) refers to its approach to regulation as follows:

> "In order to ensure that our regulatory requirements do not become a barrier to competiveness and innovation, we apply the Better Regulation principles which the Government published in January 2004 (table reference) and are an active member of the Taoiseach's Better Regulation Group"

This approach in turn appeared to be aligned to the prevailing international belief, particularly in the US and Europe, in the economic benefits of rational self-correcting markets and the merits of financial intermediation. For example, in his evidence to this Committee on 18 February last Mr Buti, EU DG for Economic and Financial Affairs stated:

> "Yes, we understood that the Irish housing boom would not be sustainable. But in line with the "Great Moderation" paradigm we, as others, did not anticipate that the end of the housing boom could give rise to the dislocations that eventually emerged after 2007 and which later on lead Ireland to ask for financial assistance from the EU and the IMF. The Financial sector was thought to simply channel funds in an efficient manner to where the real economy needed them. Dangerous excesses were thought to originate only in monetary and fiscal policy making".

The Larosiere Report of 25 February, 2009 gave the following examples of regulatory tools which can help meet counter-cyclical objectives:

> Introducing dynamic provisioning or counter –cyclical reserves on banks in "good times" to limit credit expansion and so alleviate pro-cyclicality effects in the "bad times";
>
> Making rules on loans to value more restrictive; and
>
> Modifying tax rules that excessively stimulate the demand for assets.

However, the Report states that "These tools were not, or were hardly, used by monetary and regulatory authorities in the run-up to the present crisis." Despite the background environment, Ireland did move to increase the capital weighting on high loan to value mortgages and to phase out tax support for a number of property schemes. With the benefit of hindsight, it is reasonable to say that these measures should have been taken sooner.

The Department of Finance was staffed to deal with the functions and regulatory model outlined above and that was considered adequate during the 2002 to 2006 period. The Central Bank and the Regulatory Authority had the structures needed to decide the required staffing levels for the functions they were required by legislation to perform. Clearly, with the onset of the crisis it was necessary for all three organisations to review their staffing and skill levels and to move as quickly as possible to secure and allocate any additional resources required to manage the crisis. With the benefit of hindsight, more consideration could have been given to how the legal framework would cope with a major crisis.

THEME: R4

Appropriateness and effective utilisation of the expert advice

LINE OF INQUIRY: R4a

Appropriateness of the expert advice sought, quality of analysis of the advice and how effectively this advice was used

Council Logo

COUNCIL OF THE EUROPEAN UNION

Brussels, 5 April 2001

6168/01

LIMITE

PV/CONS 5
ECOFIN 31

DRAFT MINUTES[1]

Subject :	**2329th** meeting of the Council (**ECONOMIC AND FINANCIAL QUESTIONS**), held in Brussels on 12 February 2001

[1] Information relating to the final adoption of Council acts which may be released to the public is contained in Addendum 1 to these minutes.

Concerning item 8 of the agenda

COUNCIL OPINION

On the 2000 update of Ireland's Stability Programme, 2001-2003

THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty establishing the European Community,

Having regard to Council Regulation (EC) No 1466/97 of 7 July 1997 on the strengthening of the surveillance of budgetary positions and the surveillance and co-ordination of economic policies[1], and in particular Article 5-(3) thereof,

Having regard to the recommendation of the Commission,

After consulting the Economic and Financial Committee,

HAS DELIVERED THIS OPINION:

On 12 February 2001 the Council examined the 2000 update of Ireland's Stability Programme, which covers the period 2001-2003.

The Council notes that the Irish economy continues to grow rapidly in 2000, with real GDP growth of 10.7% expected in the 2000 update. Employment growth in 2000 is estimated at 4.5%, with the unemployment rate declining further to 4.1% on average. Inflationary pressures have intensified. Average HICP inflation rose to -5.3% in 2000. While this upsurge in price inflation is partly due to external and temporary factors, which are expected to gradually fall out of the consumer price index, domestically-generated inflation has increased too, house price inflation remains very high and wages are rising rapidly.

[1] OJ L209, 02.08.1997

As a result of strong economic growth, the projections in the 1999 update of the Stability Programme for the improvement in the budgetary situation were exceeded by a large margin. The Council welcomes the fact that the general government balance for 2000 remains in substantial surplus, estimated to be around 4.7% of GDP, and that another sharp reduction in the general government debt ratio was achieved.

Projections for the period 2001 to 2003 show an average surplus ratio of 4.2%, with the debt ratio declining further to less than one quarter of GDP by 2003. The Council welcomes the fact that, as in the original programme and its 1999 update, Ireland fully and comfortably fulfils the Stability and Growth Pact obligations throughout the period covered. The projected general government surplus is clearly sufficient in each year to provide a safety margin against breaching the 3% of GDP reference value in the event of normal cyclical fluctuations.

The macroeconomic scenario underlying these projections assumes a gentle decline in real GDP growth and in inflation over the period. The positive output gap, after an estimated 4.5% of trend GDP in 2000, is expected to peak in 2001 at 5.4% and to gradually decline thereafter. In this context, the Council considers that the stimulatory nature of the budget for 2001 poses a considerable risk to the benign outlook in terms of growth and inflation portrayed in the 2000 update. The Council considers that this budget - the main measures of which are indirect and direct tax cuts and substantial increases in current and capital expenditure – is pro-cyclical. The Council finds that it will give a boost to demand of at least 0.5% of GDP and that its possible supply effects are likely to be small in the short term, thereby aggravating overheating and inflationary pressures and widening the positive output gap.

In particular, the strategy of inducing labour force increases through an alleviation of the direct tax burden, which was recommended in the 2000 BEPG with respect to the labour market,- may have become less effective than in the past because it took place in the context of an expansionary budgetary policy, and the tightness of the labour market could well hamper further attempts at encouraging wage moderation with direct tax cuts. Further, while indirect tax cuts have a once-and-for-all effect on the price level, they probably have no lasting effects on the rate of inflation but clearly further stimulate demand.

Given that the monetary policy is now set for the Euro area as a whole and no longer available as an instrument at national level, other policies, including budgetary policies, must be used more actively. Against this background, the Council finds that the planned contribution of fiscal policy to the macroeconomic policy mix in Ireland is inappropriate. The Council recalls that it has repeatedly urged the Irish authorities, most recently in its 2000 broad guidelines of the economic policies, to ensure economic stability by means of fiscal policy. The Council regrets that this advice was not reflected in the budget for 2001, despite developments in the course of 2000 indicating an increasing extent of overheating. The Council considers that Irish fiscal policy in 2001 is not consistent with the broad guidelines of the economic policies as regards budgetary policy. [The Council has therefore decided, together with this Opinion, to make a recommendation under Article 99(4) of the Treaty establishing the European Community with a view to ending this inconsistency.]

concerns might have been voiced internally.

Why did the IMF team get things so badly wrong? There are several explanations. First, the analysis was grounded largely on acceptance of the CBI view favouring the soft landing outcome for house prices. While some stress tests involved larger price falls, the possible rise in non-performing loans, NPLs, was, it appears, capped at 5% of all mortgage loans. Second, the neglect of commercial property lending was a crucial omission, Third, while the increased dependency on wholesale external funding by the banks was noted, no one considered what might be the catastrophic effect of a worldwide drying up of liquidity as actually occurred in 2008. Finally, the IMF team appeared to have had no inkling of the indecisiveness and lack of firm engagement underlying the detailed interaction between the Financial Regulator and key individual institutions, problems that were uncovered only much later by the Honohan inquiry.

These were serious shortcomings to which can be added the general approach at the time that favoured so-called principles-based, what is sometimes called light touch, financial regulation. The IMF, being a creature of its member countries, was undoubtedly heavily influenced by this prevailing philosophy. That said, in my view, it would have been incumbent on the FSAP report, as a minimum, to have posted a health warning and cited more explicitly the limitations that underlay the positive conclusions it presented. The Irish experience suggests that the absence of such warnings can seriously undermine the credibility of the IMF's work.

The third area is the budget. The last major area covered by the consultation reports was the budget. Until 2008, Ireland had been running small overall budget surpluses. However, the IMF staff generally urged that these surpluses be increased somewhat, both to counteract what was thought to be overheating, often described as using contra-cyclical policies, and to build up a reserve against future unknowns. By and large this recommendation fell on deaf ears.

A far more serious shortcoming in my view was the conclusion by the IMF up to and including 2007 that the underlying, that is, cyclically adjusted, fiscal balance, CAB, was in approximate balance throughout 2007. This CAB measure attempts to strip out so called temporary factors, such as higher than average growth or transitory revenue flows, that mask the true underlying fiscal picture. In Ireland's case, the IMF, together with the Department of Finance, went along with a common EU methodology used to calculate the CAB.

The problem was that this methodology assumed that the high output levels reached by Ireland in the first half of the decade of the 2000s, which in turn reflected the massive reliance on the construction sector, were permanent structural features. The same assumption applied to the artificial boost in revenues associated with the property boom. Using more technical phraseology, it was assumed that actual output was close to potential output, but the reality was the other way around. Irish output throughout the latter years of the boom was far above sustainable potential. After all, as was pointed out by very few at the time, there was a limit to how many homes people can actually live in. By 2009, the assumptions underlying the earlier IMF calculation of the CAB were clearly untenable. In a quite dramatic reversal, the 2009 IMF report re-estimated the CAB for earlier years using a quite different methodology. For example, the CAB for 2007 turned out to be a deficit of 8.7% of GDP compared with an originally estimated surplus of 0.7%, a change of more than nine percentage points in GDP for the same year. Seldom has the picture of a country's fiscal health deteriorated so sharply and so quickly. The question can be asked if, starting from 2009, a far more appropriate methodology was used, why this was not done in earlier years or at least presented as a variant of the standard approach that had been uncritically accepted.

The last area concerns the overall macroeconomic interlinkages. The various IMF reports did point out to some extent the vulnerabilities associated with particular sectors, that is, property, financial and fiscal, but they explore the dynamics of a possible downward self-reinforcing spiral such as eventually ended up happening. At best, some first round effects were considered. While precise quantification of a worst case scenario would have been very difficult, some key elements could have been addressed more explicitly. It is possible that the IMF reports did not go down this route because of the somewhat speculative nature of what was involved. It would likely also have been seen as highly alarmist, and provoked strong negative market and, one assumes, political and media reaction. Nevertheless, that complication could have been dealt with by raising the issues confidentially with the Irish authorities as opposed to including a discussion in the published staff report. However, there is no evidence available indicating that such discussions occurred. There could have been pressures both within the IMF and *vis-à-vis* the Irish authorities to dismiss the possibility of such very negative outcomes. The consensus, reflecting perhaps strong elements of groupthink, was to stay with the soft landing hypothesis and to hope that perhaps, in the end, our luck would hold out.

I will turn briefly to the second period, 2008 to 2010, when, of course, things were quite different. The 2007 report was the last rosy IMF report on Ireland. By the time of the 2009 consultation two years later, the picture had changed dramatically. The property market was in free fall, the budget deficit had exploded, unemployment was soaring and the full extent of the banking disaster was starting to emerge. However, no consultation took place in 2008. Normally, the consultation would have taken place as scheduled, unless the authorities indicated a desire to postpone it. The reasons underlying this hiatus are not in the public domain. The postponement meant that during this critical two-year period, from mid-2007 to mid-2009, there was no formal dialogue between the IMF and the Irish authorities. This must be considered a significant flaw. If IMF surveillance is to be meaningful, there should be at least the opportunity for timely inputs from the IMF at a time when, amidst global financial disarray, many key policy options were being considered on the Irish side.

In particular, there are no indications, at least on the public record, suggesting that the IMF staff provided input on the end of September 2008 bank guarantee, either before this decision was taken or afterwards. The 2009 consultation report described the guarantee but did not offer any views as to its appropriateness or otherwise. It did, however, contain a useful table summarising the key features of guarantees provided by various other countries during the past 30 years. This table is summarised as part of chapter 10 on page 214 of the book Dr. Murphy and I wrote. The chapter deals extensively with the guarantee decision. Perhaps contrary to what is sometimes said, it appears from this table that the coverage of the Irish guarantee was not that radically different from that contained in several other earlier guarantees.

Overall, it seems that around this critical time, the IMF did not provide sufficient timely professional technical advice to the Irish authorities. Whether this was primarily a supply side issue, perhaps because the IMF was busy elsewhere, or reflected demand side factors, because perhaps the authorities preferred not to hold the consultation in 2008, remains an important question to which I do not have the answer.

I thank the Chairman and committee members for their attention. I am, of course, very happy to answer any questions they may have on the foregoing or on any other related aspects covered in our book or elsewhere. I received a list of possible questions that committee members may raise and I am certainly happy to do my best to try to answer them as far as I can.

Chairman: Thank you, Dr. Donovan. Before I bring in the lead questioners, he might deal