EUROPEAN COMMISSION

Brussels, 25.10.2017
C(2017) 7066 final

PUBLIC VERSION

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Subject: State aid SA.49194 (2017/N) - Ireland
Sixth prolongation of the Credit Union restructuring and stabilisation scheme

Sir,

I. PROCEDURE

(1) On 16 October 2014 the Commission approved the restructuring and stabilisation scheme for the Credit Union Sector in Ireland[1] ("the scheme") by its decision in State aid case SA.36262 ("the original decision"). The scheme was approved until 1 April 2015. On 5 May 2015 the Commission approved a first prolongation of the scheme until 31 October 2015[2], on 16 November 2015 a second prolongation until 30 April 2016[3], on 4 May 2016 a third prolongation until 31 October 2016[4], on 11

[1] Commission Decision in State Aid case SA.36262 (2014/N) – "*Restructuring and stabilisation scheme for the Credit Union Sector in Ireland"*, OJ C 126, 18.04.2015.
[2] Commission Decision in State Aid case SA.41371 (2015/N) – *First prolongation of the Credit Union restructuring and stabilisation Scheme*". OJ C 234, 17.07.15.
[3] Commission Decision in State Aid case SA.43423 (2015/N) – *Second prolongation of the Credit Union restructuring and stabilisation Scheme*". OJ C 46, 05.02.16.
[4] Commission Decision in State Aid case SA.45129 (2016/N) –"*Third prolongation of the Credit Union restructuring and stabilisation Scheme*". OJ C 220, 17.06.2016.

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October 2016 a fourth prolongation until 30 April 2017[5] and on 17 May 2017 a fifth prolongation until 31 October 2017[6].

(2) On 27 September 2017, Ireland notified a sixth prolongation of the scheme until 30 April 2018.

II. FACTS

Legal basis and budget

(3) The scheme is based on the Credit Union and Co-operation with Overseas Regulators Act 2012 ("the 2012 Act"). The 2012 Act was prepared under the Programme of Financial Support for Ireland from the European Union and the International Monetary Fund (the "EU-IMF programme").

(4) The 2012 Act provides for the establishment of a Credit Union Fund of EUR 250 million to support the restructuring of credit unions and a further EUR 30 million to support their stabilisation. It also provided for the establishment of the Credit Union Restructuring Board (ReBo) with the mandate of approving stabilisation plans as well as restructuring plans and recommended the provision of repayable financial support for restructuring proposals.

The current state of the credit union sector

(5) Credit unions are member-owned, not-for-profit entities, whose business primarily relates to savings and consumer loans (not mortgages). They are distinctive in nature in that they are co-operative financial organisations that are geared to attaining the economic and social goals (financial inclusion) of their members. Credit unions cannot do business with the general public but only with their members.

(6) On 30 June 2017, the credit union sector comprised 302 credit unions registered in Ireland (including 26 inactive credit unions awaiting deregistration). Their average balance sheet size is EUR 60.5 million. The sector as a whole has approximately EUR 16.6 billion of assets (approximately 4.8% of the total assets of credit institutions in Ireland). Credit union members' savings account for about 6.5% of deposits from Irish residents, while their consumer loans account for 2.4% of total loans to Irish residents. The sector's loan-to-total savings ratio is approximately 32.8%.

(7) The liability side of a credit union's balance sheet consists of two sections: members' savings and reserves. Members' savings have no fixed remuneration rate but members receive a dividend which is proportionate to their deposits. Despite those equity-like characteristics, members' savings are considered as deposits and are covered by the general deposit insurance. Credit unions are required by the Central Bank of Ireland ("CBI") to hold regulatory capital of at least 10% of assets. CBI reported (December 2016) that 3 credit unions are considered

[5] Commission Decision in State Aid case SA.46437 (2016/N) –"*Fourth prolongation of the Credit Union restructuring and stabilisation Scheme*". OJ C 452, 02.12.2016.

[6] Commission Decision in State Aid case SA.48099 (2017/N) –"*Fifth prolongation of the Credit Union restructuring and stabilisation Scheme*". OJ C291, 21.08.2017.

undercapitalised (<10%) with 2 of those considered seriously undercapitalised (<7.5%).

Objective and description of the scheme

(8) The currently notified prolongation of the scheme does not change the budget, eligibility and all other conditions from the previously approved versions of the scheme[7]. A detailed description of the scheme has been provided in recitals (6) to (19) of the original decision.

(9) The scheme aims both to encourage voluntary amalgamation between credit unions ("restructuring support") and to provide aid in the form of capital to certain viable credit unions on an individual basis ("stabilisation support").

(10) The objective of restructuring is to reinforce the stability and long-term viability of the entire credit union sector by supporting the amalgamation of strong credit unions with weaker ones. Amalgamation is a voluntary process and all credit unions may participate in the scheme provided that at least one of the participating credit unions has a reserve ratio above the minimum required level.

(11) Stabilisation involves providing capital support to individual credit unions whose reserves have fallen below the statutory reserve requirement of 10% of total assets but remain equal to or above 7.5%.

(12) The key to both restructuring and stabilisation proposals is the viability of the entity (the amalgamated entity in a restructuring/amalgamation case and the individual entity in a stabilisation case). Any such entity must undergo a triple assessment by ReBo, the CBI and the Minister for Finance before any funds can be made available.

(13) Regarding the status of the State capital provided through the scheme, that contribution is fully loss-absorbing but in case of liquidation it ranks senior to the reserves. An initial remuneration of 5% on contributions received under the scheme is required from the beneficiary with step-ups to 6.25% after five years and 7.5% after 10 years in order to incentivise early repayment. The remuneration ranks senior to member share dividend payments.

(14) A credit union can only benefit from the scheme once, either in the context of an amalgamation or of a stabilisation.

(15) The scheme will last for six months. The present decision assesses the compatibility of the scheme until 30 April 2018.

Use of the scheme

(16) As of 27 September 2017, i.e. the date when Ireland notified the proposed 6-month prolongation, the Irish authorities had granted no financial assistance for amalgamations or restructurings under the scheme.

(17) ReBo ceased to accept restructuring proposals on 31 March 2016. Up to that date ReBo had engaged with 223 credit unions. The position as of 23 August 2016 is that 208 different credit unions have been involved in 112 merger projects. 133 of these credit unions across 66 projects have completed the merger process (without any aid from the scheme) with the remainder yet to complete. It is not yet known

[7] See footnote 1-5.

how many of the amalgamation proposals that are currently under consideration will be successful. The Minister for Finance, the CBI and ReBo would then decide if such proposed amalgamations indeed merit financial assistance. ReBo has fully completed 82 restructuring projects involving 156 credit unions.

III. THE POSITION OF IRELAND

(18) The Irish authorities request a prolongation until 30 April 2018 of the scheme without any changes as compared to the scheme approved by the original decision.

(19) The Irish authorities submit that the scheme constitutes State aid within the meaning of Article 107(1) of the Treaty on the Functioning of the European Union ("the Treaty"), but are of the view that the notified prolongation is compatible with the internal market on the basis of Article 107(3)(b) of the Treaty as it is necessary in order to remedy a serious disturbance in the economy of Ireland.

(20) The Irish authorities emphasise that the EU-IMF programme concluded that parts of the credit union sector were distressed, and this posed a threat to the financial stability of Ireland and that Ireland thereby requires sectoral reform.

(21) Ireland's understanding is that the scheme is fully compatible with applicable State aid rules.

(22) The scheme is open to all credit unions established in Ireland.

(23) In addition, the Irish authorities consider that the scheme is proportionate to the challenge faced, and does not go beyond what is necessary to achieve that objective.

(24) The Irish authorities furthermore have committed to report to the Commission on the operation of the scheme on a six-monthly basis.

(25) Finally, the Irish authorities commit to not making use of the scheme for the period between the expiry of the previous prolongation (31 October 2017) and the date of adoption of the present decision.

IV. ASSESSMENT

1. Existence of State aid

(26) As set out in Article 107(1) of the Treaty, any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the internal market.

(27) For the reasons indicated in recitals (28) to (31) of the original decision, the Commission considers that the scheme constitutes State aid within the meaning of Article 107(1) of the Treaty. The notified prolongation of the scheme does not affect that finding. Therefore, the scheme remains State aid within the meaning of Article 107(1) of the Treaty.

2. Compatibility

Legal basis

(28) The Commission considers that the conditions for State aid to be assessed pursuant to Article 107(3)(b) of the Treaty are still present. Therefore, the Commission continues to base its assessment of State aid measures in the banking sector on Article 107(3)(b) of the Treaty.

(29) In order for an aid to be compatible under Article 107(3)(b) of the Treaty, it must comply with the general principles for compatibility under Article 107(3) which is viewed in the light of the general objectives of the Treaty. Therefore, according to the Commission's decisional practice, any aid or scheme must comply with the following conditions: (i) appropriateness; (ii) necessity; and (iii) proportionality.

(30) The 2013 Banking Communication[8] also establishes that *"the Commission is willing to authorise schemes for recapitalisation and restructuring of small institutions where such schemes have a clear remit and are limited to a six-month period, provided they respect the principles set out in the Crisis Communications and in particular the burden-sharing requirements of this Communication. The application of any such scheme must furthermore be restricted to banks with a balance-sheet total of not more than EUR 100 million. The sum of the balance-sheets of the banks that receive aid under the scheme must not exceed 1.5% of the total assets held by banks in the domestic market of the Member State concerned."*[9]

(31) Any restructuring and recapitalisation scheme should also be assessed in respect of how its provisions ensure restoration of long-term viability, own contribution (burden-sharing) and measures limiting the distortion of competition as set out in the Crisis Communications[10] if it is to be considered as appropriate.

(32) The detailed Commitments provided by the Irish authorities are set out in the Annex[11] and remain unchanged.

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[8] Communication from the Commission on the application, from 1 August 2013, of State aid rules to support measures in favour of banks in the context of the financial crisis, OJ C216, 30.7.2013, p. 1.

[9] 2013 Banking Communication, point 54. The 2013 Banking Communication is applicable to credit unions – like all financial institutions – even though they are not banks.

[10] Communication on the application of State aid rules to measures taken in relation to financial institutions in the context of the current global financial crisis ('2008 Banking Communication'), OJ C 270, 25.10.2008, p. 8; Communication on the recapitalisation of financial institutions in the current financial crisis: limitation of aid to the minimum necessary and safeguards against undue distortions of competition ('Recapitalisation Communication'), OJ C 10, 15.1.2009, p. 2; Communication from the Commission on the treatment of impaired assets in the Community financial sector ('Impaired Assets Communication') (OJ C 72, 26.3.2009, p. 1); Communication on the return to viability and the assessment of restructuring measures in the financial sector in the current crisis under the State aid rules ('Restructuring Communication') (OJ C 195, 19.8.2009, p. 9); Communication from the Commission on the application, from 1 January 2011, of State aid rules to support measures in favour of financial institutions in the context of the financial crisis ('2010 Prolongation Communication'), OJ C 329, 7.12.2010, p. 7, Communication from the Commission on the application, from 1 January 2012, of State aid rules to support measures in favour of financial institutions in the context of the financial crisis ('2011 Prolongation Communication), OJ C 356, 6.12.2011, p. 7 and Communication from the Commission on the application, from 1 August 2013, of State aid rules to support measures in favour of banks in the context of the financial crisis, OJ C216, 30.7.2013, p. 1.

[11] Those commitments dated 15 April 2015 were originally communicated to the Commission by the Irish authorities for the first prolongation and have been reconfirmed in the notifications for the second though fifth prolongations.

Prolongation of the scheme

(33) In recitals (42) to (78) of the original decision, the Commission analysed whether the scheme fulfilled the conditions for compatibility with the internal market. The Commission's assessment remains the same as its initial assessment because since the original decision was approved: (a) the scheme has not changed; and (b) there have been no substantive changes in respect of the reasons for requiring implementation. That finding is explained in further detail in the subsequent recitals.

(i) Appropriateness

(34) The scheme should be appropriate to remedy a serious disturbance in the Irish economy. The objective of the scheme is to temporarily offer appropriate measures to address the currently existing problems in the Irish credit union sector in a timely and efficient manner.

(35) The assessment of the scheme's appropriateness consists of a number of distinct aspects, notably the *viability assessment*; as well as the *remuneration of the capital* provided and the generated *burden-sharing*.

1. Viability

(36) Participation in the scheme is fully voluntary and open to all credit unions. However, there are certain limits to eligibility under the scheme, providing some safeguards for viability. Credit unions whose reserve ratio is negative will not be able to obtain restructuring support under the scheme underlining the fundamental doubts about their viability. Stabilisation support under the scheme will only be provided to credit unions with a reserve ratio greater than or equal to 7.5%, underlining the commitment to provide stabilisation support only to institutions with financial problems of a temporary nature.

(37) The Irish authorities commit that the CBI will assess the future viability of any credit union participating in the scheme and that financial aid will not be granted without a prior positive assessment of viability from the CBI. The CBI will be as strict as the Commission in its assessment of the future long-term viability of the credit unions that may receive State aid under the scheme. Furthermore, the CBI will apply the same principles as the Commission for such assessments. The Irish authorities also commit to the fitness and probity regime for credit unions.

(38) In view of the commitments reviewed in recitals (36)-(37), the simple business model of the credit unions and the fact they are relatively very small in size, the Commission considers that it is appropriate for the CBI to carry out the viability assessment in the framework of this particular scheme.

2. Remuneration and burden-sharing

(39) All aid granted under the scheme will be repaid and remunerated appropriately.

(40) Regarding repayment, funds provided under the scheme are fully loss-absorbing on the same level as reserves, but those funds remain attributable to the Credit Union Fund, unlike the un-attributable status of reserves. If there are any reserves

which remain available for distribution in a liquidation scenario, any distributions of reserves to members will be paid only after the State capital contribution has been repaid in full. Therefore, the State capital can be considered senior to reserves in the case of liquidation, which reduces the risk for the State.

(41) The Irish authorities have committed that the beneficiaries of the scheme will pay State capital remuneration in full before a dividend is paid on the credit union shares. That commitment ensures that State capital effectively has a senior rank to member shares in terms of remuneration and can therefore be considered the most senior claim on net earnings in any given year. Only if the remuneration due to the Credit Union Fund can be paid in full may any remainder be used for the build-up of reserves, the payment of a dividend to members or the repayment of outstanding capital to the Credit Union Fund. In addition:

- The remuneration on the funds provided by the Credit Union Fund ranks as the super-senior claim on net revenues.
- The repayment of the funds provided ranks equivalent to hybrid capital in an equivalent bank balance sheet.
- The remuneration cap to staff is applied.

(42) Regarding the remuneration level of the capital provided, the Irish authorities commit to a non-cumulative remuneration rate (dividend) for the scheme of 5% on the proportion of the Credit Union Fund's capital outstanding, increasing to 6.25% after 5 years and 7.5% after 10 years.

(43) The Commission concludes that the proposed remuneration is appropriate in view of the above as well as the not-for-profit character of the sector, the extremely low risk operational model and related low profitability, and the very small size of each individual institution.

(44) In respect of burden-sharing, it must be noted that the scheme involves the capital of the credit unions in two circumstances where:

(i) the resources of credit unions participating in the amalgamation have already fulfilled the required regulatory reserve levels which contribute to the costs of the amalgamation. In addition, the depositors of the same credit unions share the burden (moreover, in case of amalgamation the weakest credit union will disappear as an individual operator); and

(ii) the depositors who have the right to any surplus beyond reserves and in proportion to their deposits[12] effectively contribute to the remuneration and repayment of the required State capital injection by agreeing to reduced returns on their savings.

(45) As regards burden-sharing, it must be pointed out that the Irish credit unions, while covered by the deposit guarantee scheme (see recital (7)), do not fall under Directive 2014/59/EU establishing a framework for the recovery and resolution of credit institutions and investment firms[13].

[12] See recital (7) above.

[13] OJ L 173 12.06.2014, p.190-348.

3. *Conclusion as regards appropriateness*

(46) In view of the provisions made to ensure the viability of the sector through the specific assessment of each specific transaction as well as the due consideration given to appropriate levels of remuneration and burden-sharing, the Commission considers the scheme appropriate.

(ii) Necessity

(47) As regards the necessity of the scheme, the following needs to be considered:

- The EU-IMF programme concluded that the fragmented credit union sector needs to be restructured.
- With regard to the scope of the measure, the Commission endorses Ireland's commitment to limit the scheme's budget for restructuring to EUR 250 million and an additional EUR 30 million for stabilisation.
- The amalgamations are an effective course of action designed to strengthen the sector and minimise the amount of aid needed. Amalgamations allow smaller credit unions to be absorbed into larger ones, thereby permitting wider sharing of fixed costs and ensuring that the smaller credit unions have access to the necessary banking expertise. In order for such amalgamations to take place voluntarily, a minimum amount of aid may be necessary.
- Given the specific characteristics of the sector and the capital structure of credit unions, the Commission also concludes that in the context of a general financial crisis, stabilisation aid as a temporary bridge financing measure which is limited in amount and provided to fundamentally viable credit unions is necessary for financial stability.

(48) In the light of the preceding considerations, the Commission considers that the scheme is necessary.

(iii) Proportionality

(49) As stated in point 54 of the 2013 Banking Communication, the Commission is willing to authorise schemes for the recapitalisation and restructuring of small institutions, such as the scheme under assessment, provided that such schemes respect the principles set out in the Crisis Communications. One of the principles in the Crisis Communications is limiting the distortion of competition. The Irish authorities have committed to a number of safeguards such as a remuneration cap, the remuneration of State funding, and a dividend policy to ensure proportionate administrative treatment whilst ensuring that competition distortion is limited to the minimum.

(50) Distortions of competition in respect of the scheme will be limited due to the above conditions and the specific nature of the credit unions sector:

- credit unions which do business only conduct them with their members and operate on the basis of a common bond; in addition, the 10% reserve ratio

imposed on credit unions limits the potential growth rate of a credit union significantly (EUR 10 balance sheet growth requires EUR 1 of retained profits);

- most credit unions are very small in size therefore the impact on competition caused by the aid is limited. In addition, the Irish authorities commit to restrict the scheme to credit unions with a balance sheet total which does not exceed EUR 100 million and limits the post-amalgamation size for credit unions receiving restructuring support to EUR 400 million;

- restructuring (amalgamation) is voluntary and open to all credit unions meeting the eligibility criteria. There is no discrimination between the members of that sector, and support is theoretically available to all credit unions willing to merge into a new, viable entity;

- the Irish authorities have committed to an advertising ban.

(51) The Irish authorities have not committed to an acquisition ban in relation to the beneficiaries of State aid under the scheme. As part of the principle of limiting distortion of competition, points 39 to 41 of the Restructuring Communication foresee that aided credit institutions should not use State aid for the acquisition of competing businesses for a period of at least three years. The Commission considers that the evaluation expressed in recitals (73) to (75) of the original decision continues to apply and reiterates its assessment that in the exceptional case of the Irish credit unions, an acquisition ban is not required to avoid distortion of competition and, if imposed, would in fact undermine the purpose of the notified scheme, an objective of which is to support amalgamations in the sector.

(52) The Commission considers that the scheme is proportionate to the objectives which need to be achieved due to the explicit and implicit limitations on competition distortion.

Monitoring

(53) In line with point 55 of the 2013 Banking Communication, the Commission welcomes that the Irish authorities undertake to present a report on the operation of the scheme every six months to the Commission. Those reports will also include updates from the CBI on the participating credit unions and details on the viability assessment of successful credit unions.

Conclusion on the compatibility of the aid measure

(54) The prolongation of the scheme remains an appropriate, necessary and proportionate measure to remedy a serious distortion of Ireland's economy. Therefore, in light of the commitments agreed by Ireland in the Annex, the notified prolongation is compatible with the internal market pursuant to Article 107(3)(b) of the Treaty and the Commission does not object to a prolongation of the duration of the scheme until 30 April 2018. Any further prolongation will require the Commission's approval.

CONCLUSION

The Commission has accordingly decided to consider the aid to be compatible with the internal market pursuant to Article 107(3)(b) of the Treaty and not to raise objections to the scheme.

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Yours faithfully,
For the Commission

Margrethe VESTAGER
Member of the Commission

CERTIFIED COPY
For the Secretary-General,

Jordi AYET PUIGARNAU
Director of the Registry
EUROPEAN COMMISSION

Annex

Ireland commits to

Viability

(1) Commitment that credit unions will apply the Fitness and Probity Standards for Credit unions

The Irish authorities commit to the continued introduction of the fitness and probity regime for credit unions. The Irish authorities commit to implementing the fitness and probity regime for credit unions.

The Irish authorities commit that where a credit union is involved in a transfer of engagements or amalgamation, the merged credit union will be subject to the fitness and probity requirements. Any changes in Chair or Manager positions for the merged credit union will require Central Bank pre-approval before they could be appointed by the merged credit union.

(2) Commitment on assessment of viability

The Irish authorities commit that the Central Bank will assess the future viability of a credit union proposing to receive financial aid under this scheme and that financial aid will not be granted without a positive assessment of viability from the Central Bank. Central Bank assessment of viability will apply the same principles and be as strict as the Commission's assessment.

Burden sharing

(3) Commitment related to the remuneration cap

According to paragraph 38 of the August 2013 Banking Communication, any bank in receipt of State aid in the form of recapitalisation or impaired asset measures should restrict the total remuneration to staff, including board members and senior management, to an appropriate level. The Irish authorities therefore commit that the total remuneration of any such individual may not exceed 15 times the national average salary in the Member State where the beneficiary is incorporated or 10 times the average salary of employees in the beneficiary bank. (The highest threshold applies).

(4) Commitment related to the capital contribution

The Irish authorities commit that the capital contribution provided through this scheme is fully loss-absorbing. Such capital does not confer ownership or control rights to the State. In the case of a liquidation, to the extent that there are any reserves remaining that are available for distribution, any distributions to members shall be paid after the capital contribution has been repaid in full.

The Irish authorities commit that to reduce exposure to overtly risky ventures, the restructuring element of the scheme, is limited to credit unions, with a positive reserve ratio,

with at least one credit union with a reserve ratio greater than 10%[14] and at least one credit union with a reserve ratio of less than 10% The stabilisation scheme is limited to credit unions with a reserve ratio equal to or greater than 7.5% and less than 10%.

(5) Commitment related to remuneration

The Irish authorities commit that the non-cumulative remuneration rate for the scheme is 5% on the proportion of the Credit Union Fund's capital outstanding, increasing to 6.25% after 5 years and 7.5% after 10 years.

(6) Commitment related to credit union members dividends

The Irish authorities commit that the payment of any dividend to credit union members is subordinate to the payment of dividends to the Credit Union Fund.

The Irish authorities note the importance of dividend payments to members of participating and potentially participating credit unions. In such circumstances where a nominal dividend may be paid , the amount paid to credit union members in aggregate will be limited to be less than or equal to the amount paid to the Credit Union Fund. For the purposes of this scheme, a nominal dividend shall be no greater than 0.5%.

Distortion of Competition

(7) Commitment related to the size of credit unions participating in the scheme.

According to "*3.3. Schemes for recapitalisation and restructuring of small institutions*", paragraph 54 of the August 2013 Banking Communication, the application of any such scheme must be restricted to banks with a balance-sheet total of not more than EUR 100 million and the sum of the balance sheets of the banks that receive aid under the scheme must not exceed 1.5% of the total assets held by banks in the domestic market of the Member State concerned.

The Irish authorities commit to restrict this scheme to credit unions with a balance sheet total of not more than EUR 100 million. In relation to the restructuring element of the scheme, the threshold of EUR 100 million applies to any credit union that has a reserve ratio of less than 10%, but does not apply to credit unions with a reserve of greater than 10%. The Irish authorities also commit that the restructuring element of the scheme will be limited to entities with a balance sheet of maximum EUR 400 million post-merger. Any transactions involving higher amounts would trigger the need for a notification to the Commission.

[14] Or a higher threshold if the Central Bank is of the opinion that a higher reserve ratio is applicable to an individual credit union. This provision applies to all references to the reserve ratio of 10% throughout this document.

Additional Commitments

(8) Commitment related to reporting of the use and implementation of the scheme

The Irish authorities commit to send information about the implementation of the scheme every 6 months to the Commission. These reports will also include:-

1. updates from the Central Bank on the participating credit unions,
2. details on the viability assessment of successful credit unions,
3. the name of any credit union that, has received assistance under the scheme and has in the period under review subsequently amalgamated with one or more other credit union(s)

(9) Commitment related to credit unions that benefit from the scheme

The Irish authorities commit that a credit union can benefit only once from aid under this scheme, i.e. once under stabilisation or once under restructuring, but not from both.

(10) Commitment related to restriction on advertising

The Irish authorities commit to imposing a ban on advertising referring to State support by the credit union benefitting from the scheme for the purpose of acquiring new members.

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