



An Roinn Airgeadais
Department of Finance



**Ms Niamh Maguire
Committee Secretariat
Clerk of the Committee of Public Accounts
Leinster House
Dublin 2**

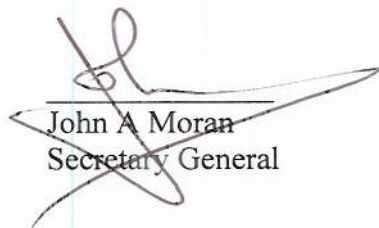
Thursday 29th May 2014

Dear Ms Maguire,

I refer to your letter of 13th May 2014 concerning matters arising from my appearance before the Public Accounts Committee on 8th May 2014 and about which they wished to have further information.

Please see my response to the various queries at Appendix 1 attached herewith.

Yours sincerely,


John A Moran
Secretary General

Appendix 1

- *A note on the tendering process employed in appointing the liquidators to IBRC and confirmation of the fees paid to date to the liquidators.*

The Special Liquidators of IBRC were appointed by Ministerial Order signed immediately following the enactment of the Irish Bank Resolution Corporation Act 2013 (the “IBRC Act”). As you know the IBRC Act was emergency legislation which passed through all stages of the Oireachtas and was signed into law within approximately twelve hours of its introduction. The appointment of the Special Liquidators was not, nor could it have been, the subject of a public procurement process requiring prior public notice. The confidentiality required in connection with the preparation for the liquidation of IBRC was an absolute prerequisite and any advance warning to the bank and/or its creditors or other counterparties could have had very significant implications for financial stability and would have made it impossible to proceed with the transaction as envisaged. It was imperative that the liquidation was executed in a controlled manner so as to help ensure that value was not eroded and that there were no material adverse consequences for the financial system as a whole.

Against this backdrop it was necessary to select a firm with significant expertise, a detailed understanding of Irish insolvency law and practice based on recent liquidation experience, and local and international resources available to deal with an assignment of this magnitude. As we were not in a position to run a public procurement process ourselves, we looked to a State agency which had run a recent public procurement process for insolvency practitioners so as to make our appointment based on another analogous competitive tender process. We consulted with NAMA as to who on their insolvency panel had the necessary qualifications and experience. After careful consideration KPMG was engaged and agreed the same rates which applied to work carried out by KPMG on behalf of NAMA. These rates had been set following a competitive tender process conducted by NAMA.

In the normal course of events, the Special Liquidators would file a statement of affairs on the second anniversary of their appointment as liquidators and this statement would contain, inter alia, details of the fees incurred. Having regard to the public interest the Department of Finance requested the Special Liquidators back in February 2014 to prepare an interim report detailing the work performed, the sale process outcomes and the level of fees incurred to 31 March 2014. This interim report is at an advanced stage of preparation and will contain comprehensive information on the Special Liquidation including details of the following workstreams:

- Transactions
- Loan management
- Finance
- Legal
- Regulatory and compliance
- Operations
- Loan migration
- HR

- IT
- Facilities
- Deposits
- Tax

In view of the Committee's specific interest in the subject, we asked the liquidator to expedite the completion of this report which will include details of fees paid to the liquidators. I now anticipate that the interim report will be issued in early June 2014 and I will forward a copy of this report to the PAC upon receipt.

It should be recalled that these fees are not just for what might be commonly understood as consulting advice. The liquidator, using its own staff or the staff of the bank (somewhat interchangeably), has been involved in the ongoing running of the bank and its liquidation. The interim report will therefore analyse costs by service provided and distinguish between services relating to the various loan book disposals and services relating to the ongoing operations of IBRC so as to identify costs to allow replacement of existing staff and management. The Committee will also recall, as I pointed out at our meeting, that it was unclear what level of co-operation the liquidator would get from existing teams which necessitated some "double cover" in earlier weeks to ensure protection of the value of the State's assets. It should finally be noted that the costs incurred are settled out of the proceeds from the liquidation and are therefore not a direct cost to the State.

- ***An analysis of the impact on the level of General Government Debt arising from the transfer of debts and liabilities from local authorities to Irish Water.***

There are a number of components to existing Local Authority water related debts and liabilities, with debt outstanding to both Government agencies (HFA/NTMA) and third party banks. Detailed analysis of these items by the Local Authorities and Irish Water (together with water sector fixed assets and current assets) is nearing completion. To the extent that third party debt and liabilities transfer from Local Authorities to Irish Water and provided that Irish Water debt is not consolidated with the rest of government debt, this would improve general government debt (there being no impact in relation to borrowings from Government agencies).

- ***A note on whether water charges will be liable for VAT***

The supply of water by local authorities and Irish Water is exempt from VAT. This VAT exemptions applies to all supplies of water, including supplies to domestic households, businesses and others. Ireland's long standing VAT exemption for the supply of water is currently contained in paragraph 14(2) of Schedule 1 to the VAT Consolidation Act 2010.

- *A note on the consultancy work undertaken by the BOI Chairman, Archie Kane, which resulted in a payment of €50,000 being made in 2013.*

By way of background, Bank of Ireland's 2013 Annual Report sets out the roles and responsibilities of the Governor which include overseeing the operation and effectiveness of the Court, ensuring that agendas cover the key strategic items confronting Bank of Ireland and encouraging all Directors to participate fully in the discussions and activities of the Court. In addition to this, the Governor ensures that there is effective communication with stockholders and promotes corporate governance standards. The Annual Report also discloses that the Governor commits significant time to Bank of Ireland and his role has priority over any other business commitment.

As disclosed in the Annual Report for 2013, Mr. Kane attended the following Court and Court sub-committee meetings:

	Court - scheduled	Court - unscheduled	Nomination & Governance - scheduled	Nomination & Governance - unscheduled	Remuneration
Scheduled	12	3	5	1	4
Attended	12	3	5	1	3

Bank of Ireland has a significant presence in the UK with c35% of total assets located there based on revenue generation. Mr Kane has extensive experience of the financial services industry in the UK having spent more than twenty five years in various senior commercial, strategic and operational roles in Lloyds Banking Group plc and TSB bank plc.

At the time of his appointment, we were advised by Bank of Ireland that Mr. Kane would be performing additional services for the UK businesses and remunerated separately therefor.

There are extensive disclosures relating to directors' remuneration for the year ended 31 December 2013 set out on pages 157 to 162 of the 2013 Annual Report including the existence of a consultancy agreement between Mr. Kane and Bank of Ireland (UK) plc in respect of which he receives an annual fee of €59,000. This consultancy agreement relates to advice and services and the specific terms and conditions of this consultancy agreement are a commercial matter between Bank of Ireland and Mr Kane and it would not be appropriate for the Department, as a c14% shareholder, to disclose these terms.

Should you require additional details, I suggest you might address those to Mr. Boucher, CEO of Bank of Ireland (whom I have advised you may contact him in this regard).

We would note though that Mr. Kane's total remuneration for 2013 was €490,000 (including the consultancy agreement) which is below the maximum annual salary cap of €500,000 which applies to senior executive positions in covered institutions. We also

note that Resolution 2 at Bank of Ireland's Annual General Court held on 25 April 2014 considered the Report on Directors' Remuneration for the year ended 31 December 2013 and was approved by 99.36% of shareholders voting on that resolution.

- *A note on the provisions that have been set aside in the three PCAR banks to deal with impaired loads – whether a breakdown is available between provisions relating to mortgages, SME lending, etc,*

Based on publically available information, the three PCAR banks (AIB, Bank of Ireland and Permanent TSB) held €209 billion of gross loans at 31 December 2013. Of these loans €154.4 billion (74%) were not impaired. The banks also disclosed c€54 billion of defaulted loans and impairment provisions of c€29 billion, implying a provision coverage ratio of 54%. This represents management's best estimate of the losses incurred in the loan portfolios at that reporting date in accordance with International Financial Reporting Standards and having been audited.

In addition, the impaired loans and impairment provisions in 2013 reflect much more stringent Impairment and Provisioning Guidelines issued by the Central Bank in May 2013 and, to varying degrees, the results of the comprehensive Balance Sheet Assessment (including an Asset Quality Review) undertaken by the Central Bank in late 2013.

The table in figure 1 provides a breakdown of the stock of provisions held by the covered banks across each of the sectors including mortgages and SMEs, as at 31 December 2013¹.

¹ Important details in relation to the categorisation of these portfolios are included in the respective annual reports for each of the banks, available on their websites

FIGURE 1

€m	Mortgages		SME		Other				2013	2012
	Rol	UK	Rol	UK	Corporate	Land & Development	Investment property	Consumer	Total	Total
AIB										
Gross loan balance	38,151	2,613	9,500	4,279	4,307	6,301	13,409	4,291	82,851	89,872
% of total gross loans	46%	3%	11%	5%	5%	8%	16%	5%	100%	
Defaulted loans - €m	8,788	295	4,060	715	476	5,523	7,631	1,423	28,911	29,416
Defaulted loans - %	23%	11%	43%	17%	11%	88%	57%	33%	35%	33%
Provisions - €m	3,796	156	2,840	399	307	4,288	4,150	1,147	17,083	16,528
Provisions - coverage	43%	53%	70%	56%	64%	78%	54%	81%	59%	56%
Bank of Ireland										
Gross loan balance	26,700	25,000	10,300	3,300	7,900	3,200	13,600	2,800	92,800	100,200
% of total gross loans	29%	27%	11%	4%	9%	3%	15%	3%	100%	
Defaulted loans - €m	3,800	600	2,700	600	600	2,800	5,800	200	17,100	17,700
Defaulted loans - %	14%	2%	26%	18%	8%	88%	43%	7%	18%	18%
Provisions - €m	1,900	100	1,400	300	200	1,900	2,200	200	8,200	7,500
Provisions - coverage	50%	17%	52%	50%	33%	68%	38%	100%	48%	43%
permanent tsb										
Gross loan balance	24,070	6,782	-	-	-	-	2,106	358	33,316	34,908
% of total gross loans	72%	20%	-	-	-	-	6%	1%	100%	
Defaulted loans - €m	6,755	248	-	-	-	-	1,448	101	8,552	7,027
Defaulted loans - %	28%	4%	-	-	-	-	69%	28%	26%	20%
Provisions - €m	2,950	76	-	-	-	-	911	98	4,035	3,150
Provisions - coverage	44%	31%	-	-	-	-	63%	97%	47%	45%
Total										
Gross loan balance	88,921	34,395	19,800	7,579	12,207	9,501	29,115	7,449	208,967	224,980
% of total gross loans	43%	16%	9%	4%	6%	5%	14%	4%	100%	
Defaulted loans - €m	19,343	1,143	6,760	1,315	1,076	8,323	14,879	1,724	54,563	54,143
Defaulted loans - %	22%	3%	34%	17%	9%	88%	51%	23%	26%	24%
Provisions - €m	8,646	332	4,240	699	507	6,188	7,261	1,445	29,318	27,178
Provisions - coverage	45%	29%	63%	53%	47%	74%	49%	84%	54%	50%

Note 1: Defaulted loans are defined as loans with a specific provision attaching to them together with loans which are more than 90 days past due

Note 2: Appendix 1 includes breakdown of Rol mortgages at 31 December 2013 over PDH and BTL

The estimation of loan losses is inherently uncertain and depends upon many factors, including loan loss trends, portfolio grade profiles, local and international economic climates, conditions in various industries to which the banks are exposed and other external factors such as legal and regulatory requirements.

A specific provision is made against problem loans when, in the judgement of management, the estimated repayment realisable from the debtor, including the value of any security available, is likely to fall short of the amount of principal and interest outstanding on the debtor's loan or overdraft account. The amount of specific provision required on an individually assessed loan is highly dependent on estimates of the amount of future cash flows and their timing.