Rule Amendments - Supplementary Information

What are the proposed Rule amendments?

Credit Union Baywide (**Credit Union**) is seeking member approval of proposed amendments to the Rules of the Credit Union to allow for the following aspects under the proposed Transfers of Engagements:

1. the temporary governance arrangements, allowing initial representation from each of the Transferring Credit Unions;
2. the transfer of Credit Union South's Securitisation Programme to Credit Union Baywide; and
3. other associated Rule amendments.

Refer to [https://nzcubaywide.co.nz/about-us/legal-ts-and-cs/Special-Meeting-March-2019] for a full copy of the proposed amendments to the Rules, including marked up changes.

Governance

The proposed Transfers of Engagements will see the unification of five credit unions. While there are many similarities across the credit unions there are also some differences. For this reason it is important that the current credit unions interests are appropriately represented on the Board of the combined credit union. The proposed Transfers of Engagements will see the Board increase to 15 directors for a period of time. The merger terms include a target Board size of seven directors by the 2022 Annual General Meeting. In practice this will involve a progressive reduction over a three year period. An amendment to the Rules is required to allow for the increased number of directors for the initial period after the Transfers of Engagements.

Securitisation

What is the Securitisation Programme?

A securitisation programme allows for a Credit Union to obtain wholesale funding (e.g. from a bank). This form of funding would complement its member deposits as a means to fund its member loans. Securitisation is a common mechanism used by a number of financial institutions within New Zealand as a means to diversify their funding requirements.

Credit Union South's Securitisation Programme is arranged by Westpac New Zealand Limited (**Westpac**) and currently has a limit of $25 million. The Securitisation Programme involves Credit Union South selling some of its loans to the Credit Union South Warehouse A Trust (**Trust**), which are then used as security for the Trust to borrow funds from Westpac. These funds are used by the Trust to pay Credit Union South for the loans it has sold. Refer to the section below 'How does securitisation work?'

If Credit Union South members approve the Transfer of Engagement to the Credit Union, then the Credit Union would like to maintain this programme by taking over Credit Union South's securitisation programme (**Securitisation Programme**).

What are the benefits of a Securitisation Programme?
The Board considers that transferring the Securitisation Programme is advantageous to the Credit Union because it provides an additional form of funding. It increases liquidity and improves cash management, which should lead to the Credit Union increasing profitability and reserves.

The specific advantages to the Credit Union of securitisation are:

- It provides the Credit Union with greater certainty over its liquidity (access to funding) enabling it to better manage its lending and cashflows
- The bank funding is for a longer term than most members' deposits which better matches the Credit Union's home loans
- The funding cost for securitisation is dependent on wholesale market conditions and has historically tracked below the cost of retail term deposits. Securitisation is therefore projected to reduce the Credit Union's costs and consequently increase profitability.

How does securitisation work?

Securitisation means the Credit Union will sell loans to another entity especially established for the purpose (**Trust**). The Trust receives funding from the bank (**Westpac**) using the security of the loans. The Trust pays the Credit Union for the loans it has sold.

The money that the Credit Union receives from selling loans to the Trust can be used to fund the day to day business of the Credit Union including making further loans to members.

The Trust is owned by the Credit Union. They are separate legal entities, but from an accounting perspective the Trust and its assets (the loans) and liabilities (bank loan) are consolidated into the Credit Union's financial statements.

The Credit Union's operations are still limited by the ratios in its Trust Deed and the need to maintain adequate capital reserves.

Only loans meeting certain agreed criteria can be sold by the Credit Union and the total exposure is limited to a specified cap (currently $25 million).

The Credit Union still administers the loans held by the Trust according to the same policies and procedures applying to its own loans. New Zealand Guardian Trust Limited, a third-party securitisation trustee, reviews the Credit Union's and the Trust's performance and the bank regularly checks on the Trust and the Securitisation Programme generally.

What is the impact on Members?

Acceptance of the Securitisation Programme will not result in any change to the terms of the deposits individual members have with the Credit Union.

Members' deposits continue to be secured by a first ranking security held by the Supervisor. When loans are sold to the Trust they no longer form part of the assets legally owned by the Credit Union and therefore they no longer form part of the security held by the Prudential Security. However they are replaced by other assets (e.g. cash) which is subject to the security.

The Credit Union must continue to comply with any conditions set by the Supervisor, the financial covenants set out in its Trust Deed and other regulations.

The Supervisor continues to monitor the Credit Union. The capital and related party ratios are monitored on a consolidated basis, that is including the assets and liabilities of the Trust.