

## **Replacement Product Disclosure Statement (PDS)**

**for the Product Disclosure Statement dated 25 July 2023 relating to an offer of Shares issued by Credit Union Auckland Incorporated**

**Date: 1 September 2023**

This document gives you important information about this investment to help you decide whether you want to invest. There is other useful information about this offer on [www.business.govt.nz/disclose](http://www.business.govt.nz/disclose).

Credit Union Auckland Incorporated has prepared this document in accordance with the Financial Markets Conduct Act 2013.

You can also seek advice from a financial adviser to help you to make an investment decision.

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## Section 1 Which products are offered under this PDS?

### 1.1 Description of the debt securities

#### *Shares*

This is an offer of debt securities called Credit Union shares (**Shares**) issued by Credit Union Auckland Incorporated, trading as NZCU Auckland (**Credit Union Auckland**). Credit Union Auckland's Shares are not like shares in a company but are more like a bank savings or other deposit account.

You invest money in Credit Union Auckland, and in return Credit Union Auckland promises to pay you any interest that you may be due (depending on your accounts held) and repay your money when you want to withdraw it or at the end of the term of your deposit.

This offer is only made to people living in New Zealand and who comply with the common bond requirements described in section 2.1 (**Depositors**).

Shares rank behind other creditors on a liquidation of the Credit Union. On a liquidation of the Credit Union, your rights and claims under the Shares would rank:

- **after** all creditors preferred by law (e.g. the Inland Revenue for unpaid PAYE and employees for holiday pay), the Supervisor, and any permitted prior security interests;
- **equally** with all other existing and potential Depositors;
- **ahead** of any lesser ranking secured and unsecured creditors (if any). This includes any 'credit union securities' that have been issued by the Credit Union as subordinated debt.

### 1.2 Products Offered

#### *Share accounts*

At the date of application, and at all times while a Depositor with Credit Union Auckland, Depositors may elect in writing to have all or any part of their deposits held in one or more of the Share accounts operated by Credit Union Auckland.

#### *Types of Share accounts*

Credit Union Auckland offers four different types of Share accounts, being:

- On Call Share Accounts;
- A "Notice of Withdrawal" Account (with 14 days' notice of withdrawal);
- Special Share Accounts; and
- Term Share Accounts.

Each Share account may offer different terms and conditions as to:

- any return payable, and when;
- whether the account can be held alone or in conjunction with one or more other accounts;
- the term of investment (term deposits); and
- the timing of repayment.

The financial return on Shares is dependent on the type of Share account in which Depositors' shares are placed, the terms of the account, the timing of the application and the duration of the term of the deposit. During the term of this PDS, the Credit Union reserves the right, subject only to any restriction in this PDS, the Trust Deed, the terms and conditions of the Share account or otherwise at law, to alter the terms and conditions as to financial return, the minimum amount of Shares required to be invested and the timing of repayment rates or terms of any Share account.

You can find more information about the dates of when the interest is due and paid on: <https://www.nzcuaukland.co.nz/rates-fees/interest-rates/>

Until 30 September 2023 Credit Union Auckland is not paying interest on On-Call Accounts or Notice of Withdrawal Accounts.

### **Terms and Conditions common to all Share Accounts**

Timing of repayments: Depositors operate their share accounts in a similar manner to deposits and withdrawals in a bank savings or deposit account. While shares are usually available to be withdrawn at call (unless on term deposit), the Credit Union's Rules provide that in special circumstances (for example, if the Credit Union could not meet its debts as they fell due) a 60 day notice period for withdrawal may be required.

### **Specific Terms and Conditions for Share Accounts**

#### **On-Call Accounts:**

On-call accounts allow you to withdraw funds whenever you need to. There are no restrictions on when you can retrieve your funds from your account.

#### **Everyday Account**

Minimum deposit: Nil.  
Timing of repayments: On demand.  
Terms and conditions: Open to all Depositors.

#### **Goal Saver**

Minimum deposit: Nil.  
Timing of repayments: On demand.  
Terms and conditions: Interest, if offered, is calculated on the basis of the minimum monthly balance and paid monthly. Credit Union Auckland reserves the right to change the interest rate (including the suspension of interest) and the basis on which the interest is calculated.

#### **BillPay Account**

Minimum deposit: Nil.  
Timing of repayments: On demand.  
Terms and conditions: Open to all Depositors.

#### **Success Saver**

Minimum deposit: Nil.  
Timing of repayments: On demand.  
Terms and conditions: Interest, if offered, is calculated on the basis of the minimum monthly balance and paid monthly. Credit Union Auckland reserves the right to change the interest rate (including the suspension of interest) and the basis on which the interest is calculated.

#### **Kid's Cash Saver**

Minimum deposit: Nil.  
Timing of repayments: On demand.  
Terms and conditions: All Depositors for this account must be under 18. Interest, if offered, is calculated on the basis of the minimum monthly balance and paid monthly. Credit Union Auckland reserves the

right to change the interest rate (including the suspension of interest) and the basis on which the interest is calculated.

**Notice of Withdrawal Accounts:**

**Loyalty Saver**

Minimum deposit: Nil.  
 Timing of repayments: 14 days' notice.  
 Terms and conditions: Interest is calculated on the basis of the minimum monthly balance and paid monthly. Credit Union Auckland reserves the right to change the interest rate and the basis on which the interest is calculated.

**Special Share Accounts:**

**Christmas Saver**

Minimum deposit: Nil.  
 Maximum Balance: \$100,000  
 Timing of repayments: 1 December through to 31 January of any year.  
 Terms and conditions: Interest is calculated on the basis of the minimum monthly balance and paid annually. Credit Union Auckland reserves the right to change the interest rate and the basis on which the interest is calculated.

Any withdrawal after 31 January and before 1 December each year is at the discretion of Credit Union Auckland.

**Term Share Accounts:**

Minimum deposit: \$500.00.  
 Timing of repayments: On maturity in 3 to 60 months depending on term selected.  
 Interest Rate: Interest rate is variable depending on date of investment. Interest rates can rise and fall without notice and the interest rate for each term is available on application.  
 Terms and conditions: Term Account for 60 months is available for minimum shareholding of \$10,000.  
 Reinvestment: If a Depositor has given instructions for any money held in a Share account to be automatically reinvested at the end of the term of the Deposit, the reinvestment money will earn the interest return applicable at the time of reinvestment to the Share account nominated. Credit Union Auckland will not be required to give a Depositor notice of the reinvestment of their money, unless Credit Union Auckland has received notice in writing from the Depositor that notice of reinvestment is required.  
 Early repayment: The policy of Credit Union Auckland is to not make repayments prior to maturity. In the event of financial hardship or extraordinary circumstances, written application may be made to Credit Union Auckland, who may exercise its discretion to repay the funds in whole or in part. In such cases the interest payable will be subject to adjustment in accordance with the terms of the share account.

You can find more information about interest rates and other terms here: <https://www.nzcuackland.co.nz/rates-fees/interest-rates/>.

Please note that until 30 September 2023 Credit Union Auckland is not paying interest on On-Call Accounts or Notice of Withdrawal Accounts.

### **1.3 Service fees associated with all accounts**

You can find more information about fees and charges applicable to all accounts here:  
<https://www.nzcuackland.co.nz/rates-fees/fees/>

## Section 2 Credit Union Auckland and what it does

### 2.1 About Credit Union Auckland

Credit Union Auckland is a financial co-operative and has been established for more than five decades, being first registered as a credit union on 6th October 1965. It is now registered under the Friendly Societies and Credit Unions Act 1982 (**FSCU Act**) under registration number 1802846, on the Financial Services Providers Register with registration FSP13041 and has a Non-Bank Deposit Taker (**NBDT**) licence - refer to the Reserve Bank of New Zealand's (**RBNZ**) website [here](#).

Credit Union Auckland offers similar products and services to a bank, such as savings accounts, loans, and insurance. Credit Union Auckland is owned by its Depositors (who are also described as members of Credit Union Auckland). This means that Depositors' funds are pooled together and are used to provide loans to all members, but not to people who are not depositors (non-members) except as are provided for in the FSCU Act and Credit Union Auckland's Trust Deed. Credit unions are not registered banks, but they are called "non-bank deposit takers". Non-bank deposit takers are regulated and monitored by the Reserve Bank of New Zealand and supervised by licensed supervisors regulated by the Financial Markets Conduct Authority. Credit Union Auckland's supervisor, for the purposes of the Financial Markets Conduct Act 2013 and as defined under the Financial Markets Supervisors Act 2011, is Covenant Trustee Services Limited (**Supervisor**).

Credit Union Auckland has entered into a Trust Deed with the Supervisor under which Credit Union Auckland has granted first ranking security interest over all its personal property and has charged all of its other property to the Supervisor as security for the payment of the principal and interest payable to Members under their accounts.

As of 1 January 2020, Credit Union Auckland is an incorporated entity under the FSCU Act as amended by the Friendly Societies & Credit Unions (Regulatory Improvements) Act 2018 which came into force on 1 April 2019 (the **Amendment Act**). At the Annual General Meeting on 16 September 2019, the Credit Union's Members approved the incorporation application and updated Rules to reflect the requirements of the Amendment Act and to improve business processes.

The Amendment Act amended aspects of the credit union's structure and in particular provided for credit unions to become incorporated entities. This means that from now on the board of directors (instead of internal trustees) are solely responsible for all aspects of Credit Union Auckland's strategy, oversight and governance. The role of the external Supervisor remains unchanged.

The Amendment Act also expanded the type and range of services and products which credit unions can offer including for example loans to member-related small and medium size enterprises. Credit Union Auckland will only provide those loans if they comply with Credit Union Auckland's credit risk policies and procedures.

As the entity status comes into effect by operation of law, all existing assets, contracts and obligations are now vested in the incorporated entity. As the provisions of the Amendment Act are intended to provide business continuity, Credit Union Auckland does not consider the regulatory changes to place any additional risk on members.

Credit unions work within a common bond - meaning that a certain credit union is only open to a specific community or group of people. Credit Union Auckland is open to people who meet the common bond described in the rules, which is:

- (a) Natural persons living in New Zealand including any such person aged 16 years or younger.
- (b) Any person who is a member of the same household as, and is a relative of, a person who has been admitted to membership and who continues to qualify for admission to membership, of the Credit Union under paragraph (a) hereof.
- (c) A charitable entity as defined by the Charities Act 2005.

(d) An incorporated society registered under the Incorporated Societies Act 1908 and amendments thereto.

In paragraph (b), the term 'relative', in relation to any person, means:

- (i) The spouse of that person including any former spouse or de facto spouse;
- (ii) any lineal ancestor, lineal descendent, brother, sister, uncle, aunt, nephew, niece, or first cousin of that person or that person's spouse;
- (iii) The spouse (including any former spouse or de facto spouse) of any relative specified in subparagraph (ii) hereof.

The objectives of Credit Union Auckland are essentially:

- the promotion of thrift amongst its members by the accumulation of their savings,
- the use and control of the members' savings for their mutual benefit, and
- the training and education of the members in the wise use of money and in the management of their financial affairs.

Credit Union Auckland's primary activity since its registration has been to provide a co-operative saving facility for members to form a loan fund.

For more information on Credit Union Auckland, the terms and conditions of investment, a copy of this PDS and the prevailing rates and fees on any particular day, visit [www.nzcuaukland.co.nz](http://www.nzcuaukland.co.nz). Please note that until 30 September 2023 Credit Union Auckland is not offering interest on On-Call or Notice of Withdrawal Share Accounts.

#### *Transfer of Engagements from New Zealand Firefighters Credit Union*

On 20 June 2022 Credit Union Auckland accepted a transfer of all of the engagements of New Zealand Firefighters Credit Union (**NZFCU**) pursuant to the FSCU Act, meaning all of the assets and obligations of NZFCU were taken over by Credit Union Auckland and all of the members of NZFCU became members of Credit Union Auckland. This was following the NZFCU Special General Meeting held on 6 May 2022 where 95.9% of voting members voted in favour of the transfer of engagements.

## **2.2 Key drivers of returns**

Credit Union Auckland must make profit to meet certain requirements in the Trust Deed with its supervisor. Currently, Credit Union Auckland's key source of income is the loan receivables generated by lending money to its members. These loan receivables are the principal assets that are charged as security pursuant to the Trust Deed, and are used solely for furthering the objectives of Credit Union Auckland. Credit Union Auckland has not granted any other charges over its principal assets.

Credit Union Auckland also generates income from commissions it receives on arranging insurance for its members and also fees on financial transactions such as card payments.

The current fees and charges are available through the government's public register, Disclose Register (**Disclose**) <http://www.business.govt.nz/disclose> or on Credit Union Auckland's website <http://www.nzcuaukland.co.nz>.

## **2.3 Financial Covenant Breaches**

In August 2018, the members of the NZ Association of Credit Unions (trading as Co-op Money NZ (**Co-op Money**)) using the services of Co-op Money fell to ten in number. This reduction in Co-op Money members created a related party relationship between the Credit Union and Co-op Money under the Deposit Takers (Credit Ratings, Capital Ratios, and Related Party Exposures) Regulations 2010 (the **Regulations**). As a result, the Credit Union breached its obligations under the Regulations. In October 2018 the Non-bank Deposit Takers (Exposures to Co-op Money NZ) Exemption Notice 2018 was published exempting the Credit Union from the requirement to include exposures to Co-op Money in the calculation of related party exposures until 30<sup>th</sup> September 2019. When the Exemption expired, the Credit Union was back



### in order. **Section 3 What is Credit Union Auckland Incorporated's Credit Rating?**

A credit rating is an independent opinion of the capability and willingness of an entity to repay its debts (in other words, its creditworthiness). It is not a guarantee that the financial product being offered is a safe investment. A credit rating should be considered alongside all other relevant information when making an investment decision.

Credit Union Auckland has been rated by Equifax Australasia Credit Rating Pty Limited (**Equifax**). Equifax gives ratings from AAA through to C.

Equifax has assigned Credit Union Auckland a credit rating of 'CCC+' at 22 June 2023, which is a credit watch classification with a very high level of risk.

The outlook for the rating is 'Negative', and a rating upgrade is unlikely in the short-term. The rating may be revised downwards in the event of continued operating deficits, leading to a breach of regulatory minimum capital requirement, and/or Trust Deed covenants.

| Moody's | Fitch | S&P  | Rating | Default rates (5 years) | Classification   | Risk Level      |
|---------|-------|------|--------|-------------------------|------------------|-----------------|
| Aaa     | AAA   | AAA  | AAA    | 0.17                    | High Grade       | Negligible      |
| Aa1     | AA+   | AA+  | AA+    | 0.31                    |                  |                 |
| Aa2     | AA    | AA   | AA     | 0.44                    |                  |                 |
| Aa3     | AA-   | AA-  | AA-    | 0.55                    |                  |                 |
| A1      | A+    | A+   | A+     | 0.76                    | Investment Grade | Very Low        |
| A2      | A     | A    | A      | 0.81                    |                  |                 |
| A3      | A-    | A-   | A-     | 1.47                    |                  |                 |
| Baa1    | BBB+  | BBB+ | BBB+   | 2.08                    |                  |                 |
| Baa2    | BBB   | BBB  | BBB    | 3.19                    | Near Prime       | Low             |
| Baa3    | BBB-  | BBB- | BBB-   | 4.37                    |                  |                 |
| Ba1     | BB+   | BB+  | BB+    | 7.13                    |                  |                 |
| Ba2     | BB    | BB   | BB     | 7.49                    | Sub Prime        | Low to Moderate |
| Ba3     | BB-   | BB-  | BB-    | 10.52                   |                  |                 |
| B1      | B+    | B+   | B+     | 16.34                   |                  |                 |
| B2      | B     | B    | B      | 22.21                   | Credit Watch     | Moderate        |
| B3      | B-    | B-   | B-     | 24.16                   |                  |                 |
| Caa1    | CCC   | CCC+ | CCC+   | 28.16                   |                  |                 |
| Caa2    |       | CCC  | CCC    | 29.90                   |                  |                 |
| Caa3    |       | CCC- | CCC-   | 39.16                   |                  |                 |
| Ca      |       | CC   | CC     | 52.87                   | Distressed       | Very High       |
| C       | C     | C    | 55.00  |                         |                  |                 |
|         | D     | D    | 100.00 |                         |                  |                 |

## Section 4 Credit Union Auckland's Financial Information

Credit Union Auckland is required by law and its trust deed to meet certain financial requirements. The following sub-sections shows how Credit Union Auckland is currently meeting those requirements. These are minimum requirements. Meeting them does not mean that Credit Union Auckland is safe. The section on specific risks of investing sets out risk factors that could cause its financial position to deteriorate. The offer register provides a breakdown of how the figures in this table are calculated, as well as full financial statements.

### 4.1 Key ratios table and selected financial information

As this is a continuous offer, Disclose contains our key ratios table as required by the Trust Deed and selected financial information. All are contained in the single document referred to as "Key Ratio and Other Financial Information" found on <http://www.business.govt.nz/disclose>.

### 4.2 Other Limitations, Restrictions and Prohibitions

#### *Other financial covenants*

Under the Trust Deed, Credit Union Auckland has agreed, subject to the terms and conditions contained in the Trust Deed, to:

- (a) **Borrow money** - not borrow money or lend other than as permitted by the Trust Deed and the Rules;
- (b) **Liabilities** - not at any time permit Credit Union Auckland's Creditor Liabilities to exceed 10% of Total Liabilities (terms as defined under the Trust Deed); and

#### *Permitted security*

Although Credit Union Auckland may borrow money for the sole purpose of managing cash flows or to cover Credit Union Auckland's settlement obligations, such borrowing must not cause a breach of the Trust Deed's minimum capital, related party and liquidity restrictions or any laws to which Credit Union Auckland may be subject or Credit Union Auckland's Rules and provided the principal amount outstanding at any time does not exceed 10% of Credit Union Auckland's Total Tangible Assets at that time and an amount reasonably determined by the Supervisor to be adequate at that time to cover the Credit Union's day-to-day exposure to BanzpayTechnology Limited in relation to any permitted prior funding.

#### *Settlement Bond*

Under the terms and conditions of our banking arrangements, we have lodged a settlement bond which is held in a trust arrangement solely for such purpose. In the event that we are unable to settle our inter-bank requirements the settlement bond provides security to Westpac and ultimately to the bank(s) that provide settlement services. The bond is held on term deposit in a trust account. The Supervisor has consented to the bond and an amount of up to 4% of our total tangible assets being excluded from the Supervisor's Security Interest.

#### *Find out more*

The Trust Deed gives the Supervisor wide ranging powers to enforce Credit Union Auckland's obligations under the Trust Deed, including the ability to appoint a receiver in certain circumstances. Depositors requiring further information as to Credit Union Auckland's covenants and the enforcement powers of the Supervisor are referred to in the Trust Deed, a copy of which can be found here: <http://www.business.govt.nz/disclose>, or alternatively on Credit Union Auckland's website: <https://nzcuackland.co.nz/investor-information>.

### 4.3 Other Matters

#### *Purchase of Base Capital Notes from NZCU Baywide*

On 13th November 2019, the Credit Union, along with all other Credit Union members of Co-op Money NZ, received an offer (the **Offer**) from NZCU Baywide (now Unity Credit Union) to purchase their Base Capital Notes holdings in Co-op Money NZ (now Banzpay Technology Limited) at \$0.75c in the \$1 with a deferred payment of the remaining \$0.25c on 30 June 2027 (subject to meeting certain contractual conditions, the principal one of which is to continue to use the Bureau services through to that date).

The Board of the Credit Union resolved to accept the Offer and on 21st November 2019 received payment in full within the terms of the Offer and relinquished all ownership rights of Co-op Money NZ.

#### *Breach of Financial Markets Conduct Act 2013 and Friendly Societies and Credit Unions Act 1982*

Pursuant to the Financial Markets Conduct Act 2013, Credit Union Auckland is required to complete its audited financial statements within 4 months from its balance date, which in Credit Union Auckland's case is 31 October.

Due to complications with the extraction of data from NZFCU's systems following completion of the transfer of engagements, the financial statements were not able to be completed and filed until 2 November 2022, meaning that Credit Union Auckland breached its obligations by not filing its audited financial statements within the statutory time period.

The obligation to file an annual return with audited financial statements within 4 months of its full year balance date is also required pursuant to section 127 of the Friendly Societies and Credit Unions Act 1982. Credit Union Auckland has obtained confirmation from the Registrar of Friendly Societies and Credit Unions that no action is required due to the filing on 2 November 2022.

#### *Event of Review*

On 18 August 2023 the Supervisor declared an Event of Review pursuant to the Trust Deed. The Supervisor has re-forecasted the capital ratio for the Credit Union and has formed the reasonable opinion that the Credit Union will breach the capital ratio on 31 October 2023.

The capital ratio of the Credit Union is a measure of the extent to which the Credit Union is able to absorb losses with out becoming insolvent. The lower the capital ratio, the fewer financial assets the Credit Union holds relative to its financial exposure.

The capital ratio is required to be at least 8%. The Supervisor's re-forecast indicates the capital ratio will be 7.24% as at 31 October 2023.

Pursuant to the Trust Deed, the declaration of an Event of Review provides the Supervisor with various powers under the Trust Deed. The Credit Union has until 15 September 2023 to provide written notification to the Supervisor of the various steps it proposes to take to ensure compliance with the capital ratio requirements.

## **Section 5 Guarantors**

Neither the Supervisor, directors or any other party guarantees the repayment of any Shares, or the payment of any interest or dividends in respect to any shares held in Credit Union Auckland.

## **Section 6 Specific risks of investing**

Risk, in terms of your investment with Credit Union Auckland, relates to the risk that the credit union may default on any of its obligations to you including not paying your investment back, or paying a lower return than you expected. All investments have some level of risk.

The main risk of you not getting your principal money back from Credit Union Auckland is where it becomes insolvent. The principal risks that may significantly affect the solvency of Credit Union Auckland, and consequently any investment with the credit union are set out below.

The main risk of you receiving a lower return than expected is where Credit Union Auckland does not make enough money to be able to afford to pay the returns you may have expected. The principal risks that may affect the profitability of Credit Union Auckland are also set out below.

### **6.1 Operating Risk**

#### **Significance to Credit Union Auckland**

Operating risks can potentially have a significant impact on Credit Union Auckland's profitability or solvency. This type of risk might arise where core systems fail to operate or key personnel leave at the same time. These circumstances can be significant for a relatively small institution like Credit Union Auckland.

#### **Operating Systems**

The main operating system needed for Credit Union Auckland to effectively function is its computer system. This is a 'bureau service' previously provided by Banzpay but now operated under the control of Unity Credit Union. (Also see Service Providers Risk under 6.5).

#### **Likelihood of Impact**

The bureau has two outsourced data centres located in the CBD of Auckland and in Albany North Shore. Both sites are purpose built data centres operated by Datacom (Albany) and Spark Digital (Auckland CBD). Each site is protected by a back-up system providing 24x7 services for power, fire suppression, air conditioning, UPS and generators.

All critical services to credit unions are housed in these environments. All systems and services are monitored 24x7 and staff are on-call to immediately respond to critical outages.

#### **Nature of Impact**

If a major system failure occurred members would not be able to transact business electronically. However, with a small institution like Credit Union Auckland there is an ability to manage member records manually (this may not be available to a large institution like a bank). This would allow investors to receive cash payments by visiting Credit Union Auckland. Credit Union Auckland's capability to run a manual system has been required in the past when Credit Union Auckland took over another credit union that did not have sufficient electronic systems. That Credit Union transacted those members accounts manually until systems were integrated.

#### **Potential Magnitude of Impact**

A major system failure would be very disruptive until fixed. Depending on the length of time of any outage, it may affect Credit Union Auckland's profitability to a degree but probably not its solvency.

## **Key Personnel**

Key personnel are the Chief Executive Officer, Operations Manager, Administration Manager, Finance Manager. If several key personnel left at the same time it could have a significant impact on a relatively small institution like Credit Union Auckland.

### **Likelihood of Impact**

Key personnel staff at Credit Union Auckland has been traditionally stable. There have been no occasions in its history where several key staff members have left at the same time (such as has happened with other financial institutions where whole teams have been poached by competitors).

The Board has adopted an Operating Risk Management policy which provides for a Chief Executive Officer succession plan, initially to a designated person until a replacement is obtained. All other key personnel have back up personnel who are reasonably familiar with their roles.

### **Nature of Impact**

The impact from several key staff members leaving at the same time might take the form of delayed supply of information through reporting lines or inexperienced personnel taking over roles until a replacement is found. Major staff changes may affect Credit Union Auckland's profitability to a degree but probably not its solvency.

### **Potential Magnitude of Impact**

Senior staff are important to Credit Union Auckland and any loss of key management may affect Credit Union Auckland's profitability to a degree but probably not its solvency.

## **6.2 Lending Risk**

### **Significance to Credit Union**

Lending risk is the credit risk inherently involved in lending money to people where they may not repay the loan amount, or make interest payments, and the lender (in this case Credit Union Auckland) is unable to realise the value of the loan through enforcement (against the borrower and also by realising any security taken as part of the loan). Lending risk incorporates factors such as the value of security provided by the borrower (for example a house or car), the nature of the security (for example a first mortgage as opposed to a second mortgage), and the ability of the borrower to service and repay the loan.

To balance the credit risk, Credit Union Auckland has a lending policy that results in a high number of smaller sized loans, with no concentration of credit risk to a single individual member.

### **Likelihood of Impact**

Credit Union Auckland runs the risk of implementing misjudged lending policies. This has occurred in the past but Credit Union Auckland has identified the problem as arising from the fact that it departed from its traditional methodology on relying on face to face dealings with its borrowers and instead relied on third parties to arrange loans. Credit Union Auckland is now mindful of that risk from departing from its traditional 'savings and loans' practice.

Credit Union Auckland has a risk policy for loans to deal with this credit risk. The policy involves credit assessment of the borrower and the security available; setting exposure limits for borrowers; monitoring and reviewing any arrears in payments; setting debt recovery reviews and maintaining internal audit of compliance with the lending policy.

## **Nature of Impact**

If borrowers do not repay their loans and Credit Union Auckland cannot recover the loan amount from the sale of any security provided, then Credit Union Auckland not only loses the interest on those loans (which then reduces the returns to members) but also the money held by Credit Union Auckland as a buffer for member repayment (**Reserves**) is reduced. As a result of the one occasion of misjudged lending policies, Credit Union Auckland suffered two to three years of losses which had an effect on its profitability.

## **Potential Magnitude of Impact**

A combination of bad lending policies and outside circumstances leading to substantial borrower default could have a significant effect on Credit Union Auckland's profitability and possibly its solvency. Credit Union Auckland had Reserves of \$3.263 million as at 31<sup>st</sup> May 2022 to help cover repayment of your money in such an event and so the magnitude of the impact would have to be greater than Reserves for you not to get your money back.

## **6.3 Profitability (Return) Risk**

### **Significance to Credit Union**

To be profitable, Credit Union Auckland must first attract members to invest with Credit Union Auckland and secondly to lend that money to other members and recover that money by loan and interest repayments to ensure the investing members are also repaid. While Credit Union Auckland does have other substantial sources of income, including fees from member transactions, investment income from Credit Union Auckland investing its surplus funds for interest, and income from commissions on, for example, placing insurance policies, if Credit Union Auckland cannot attract new members or satisfy existing members to invest further money in Credit Union Auckland, then it will not be able on-lend that money and its profitability will suffer.

### **Likelihood of Impact**

The profitability of Credit Union Auckland largely comes from the fact that borrowers also have to be savers (unlike banks and finance companies).

Approximately half of Credit Union Auckland's funding is from call deposits, that is, the savers' funds are available to borrowers. This part of the business is mainly small personal lending and so there is a good relationship between members - you save and you can borrow. This has meant that Credit Union Auckland did not suffer like finance companies during the Global Financial Crisis.

The other approximate half of Credit Union Auckland funding activities are from term deposits where higher interest rates can attract normally non-borrowing investors.

The ability to attract new members' savings or existing members to continue to invest requires Credit Union Auckland to have suitable marketing campaigns or to offer attractive interest rates compared to other financial institutions. Historically Credit Union Auckland has not needed large advertising budgets to maintain its membership. Investment in Credit Union Auckland is constantly monitored and its profitability margins allow it to increase investment rates to attract new investors.

### **Nature of Impact**

If Credit Union Auckland did not gain or even maintain members or new investment, it would over time have less money to lend and therefore would earn less income from interest and transaction fees. This would be gradual and apparent to Credit Union Auckland Directors.

### **Potential Magnitude of Impact**

A loss of investments or reinvestments would have a gradual impact on Credit Union Auckland's profitability and, if it continued, on Credit Union Auckland's viability but it would not necessarily affect Credit Union Auckland paying your investment back.

## **6.4 Liquidity Risk**

### **Significance to Credit Union**

Credit Union Auckland faces Liquidity Risk where a significant number of investors wish to withdraw their money and Credit Union Auckland does not have sufficient cash on hand to pay them all or to pay interest and other returns due to investors. An inability to pay investors interest and other returns or their investment back could arise as a result of a serious lending problem (referred to in paragraph 6.2) or investment downturn (referred to in paragraph 6.3).

### **Likelihood of Impact**

General liquidity risk is managed through the monitoring of actual and forecast cash flows (that is, mainly new investment by members and loan and interest repayments) and monitoring maturity dates of assets and liabilities (that is, the timing of when loans and deposits or other investments are due to be repaid).

During the Global Financial Crisis when other financial institutions faced liquidity difficulties, Credit Union Auckland did not experience any significant liquidity problems.

### **Nature of Impact**

If a large number of investors wished to withdraw their money at the same time or a significant number of borrowers defaulted in repaying their loans this could, depending upon the amount of money involved, significantly increase the risk of Credit Union Auckland defaulting in paying back its investors.

### **Potential Magnitude of Impact**

Credit Union Auckland monitors the potential for this risk by analysing its members' investments both as to the amount and term of the investments and also the size of investments for any group of investing members. It also analyses the type of lending to borrowing members to assess whether repayments can be obtained in sufficient time to repay investors if there was an unusual (that is, not the normal amount of investors taking their money out) number of investors wanting repayment.

The potential size of the impact of a liquidity problem arising is partly dealt with by the FSCU Act, which allows Credit Union Auckland to require not less than 60 days' notice of withdrawal of funds (this time delay is not available to other lending institutions). Loans made by Credit Union Auckland (made up as to half by personal loans) are also repayable on demand to help ensure investors can be paid (although this is likely to be only effective with smaller loans where borrowers may be able to borrow elsewhere).



## **6.5 Service Providers Risk**

### **Significance to Credit Union Auckland**

Service providers risk can potentially have a significant impact on Credit Union Auckland's ability to meet its obligations to Depositors in ensuring access to their funds and also on its profitability or solvency. This type of risk might principally arise in relation to Credit Union Auckland's main service provider Banzpay (a wholly owned subsidiary of Unity Credit Union).

Credit Union Auckland not only receives its computer system from Banzpay (see Operating Risk under 6.1) but also banking and card services, Central Banking facility and IT facilities. These are core services to Credit Union Auckland and to Depositors.

Accordingly, any circumstances that would impair the ability of Banzpay to provide these core services to Credit Union Auckland could in turn have a significant impact on Credit Union Auckland being able to provide the same services to Depositors (mainly access to their money for a time until services are restored). Such circumstances may arise out of any financial difficulties of Banzpay.

### **Likelihood of Impact**

During 2019 Banzpay advised that its liquidity and financial performance had deteriorated as a result of capital expenditure, operating losses, decreased trading activity and one-off costs and losses. This resulted in Banzpay operating a net deficit and a negative cash position. Unity Credit Union subsequently provided funding to meet specific obligations of Banzpay so that they remained in a solvent position.

The effect of the relinquishment of ownership rights in Banzpay (as described in 4.2) is that Unity Credit Union acquired all the assets of Banzpay. Conditions of the Offer include an amendment to the Bureau Services Exhibit previously held with Banzpay guaranteeing the Credit Union's continued access to all the services necessary for the Credit Union to carry on its business until at least 30<sup>th</sup> June 2022.

The likelihood of any service failure is now dependent on Unity Credit Union being able to perform the functions previously undertaken by Banzpay in a manner that is both cost effective for the Credit Union and proficient for the benefit of our members. Unity Credit Union has Assets of \$456m and Net Assets of \$64m as at 31 December 2021 and a FitchRatings credit rating of BB/Stable as at 17 Feb 2022.

### **Nature of Impact**

If Banzpay was unable to provide any one or more of the core services then, at least until Banzpay was able to restore the services, Depositors may not be able to access their funds through normal channels. However, such a circumstance would not necessarily place Depositors money at risk unless Banzpay had acted in a way to place at risk Credit Union Auckland's funds that have been lodged with Banzpay.

### **Potential Magnitude of Impact**

If Banzpay was unable to provide any one or more of the core services to Credit Union Auckland, the magnitude of the impact on Credit Union Auckland's ability to provide the same services to Depositors is high.

## **6.6 Regulatory risk**

The Credit Union is required to comply with various obligations under legislation and associated regulations.

### **Significance to Credit Union**

Any material failure to comply with these regulations and legislative requirements could result in exposure to financial and/or other penalties and damage to the Credit Union's reputation and could affect the Credit Union's ability to operate.

### **Likelihood of Impact**

The Credit Union has developed processes and procedures to ensure compliance with its regulatory requirements, along with the reporting obligations under its Trust Deed, and as required pursuant to regulations. Staff receive also receive compliance training to minimise risks of accidental breaches of any regulations.

### **Nature and Potential Magnitude of Impact**

Potential magnitude of any impact includes the revocation of statutory licenses, and being ordered to cease operations, together with the financial impact of any fines or requirements to pay damages.

### **Related Party Exposure**

As set out in 2.4 Financial Covenant Breaches, the Credit Union breached its related party exposure limits under the Regulations. However, as Credit Union Auckland is no longer a member of Banzpay there is no further risk of Credit Union Auckland breaching the exposure limits.

## **Section 7 Register Entry**

Further documents with regard to the debt securities offered by Credit Union Auckland can be found by searching Credit Union Auckland (as issuer) on <http://www.business.govt.nz/disclose> or on request from the Registrar of Financial Service Providers by emailing: [registrar@fspr.govt.nz](mailto:registrar@fspr.govt.nz).

The information contained on the disclosure register includes among other things a copy of the Trust Deed, financial information for Credit Union Auckland, summary of key details and accounts and credit rating report.