

**GLEBE ADMINISTRATION BOARD
BANKING SERVICES
RISK MANAGEMENT POLICIES**

**CREDIT RISK MANAGEMENT
(Treasury and Lending)**

28 March 2012

GAB Banking Services Credit Risk Management Policy

Objective of this Policy

1. The objective of this Policy is to set out the policies of Glebe Administration Board (“GAB”) for the management of credit risk within its Banking Services. In particular, it sets out a framework to ensure that credit risk is managed in line with, so far as it is appropriate they be applied, the core principles of the relevant standards and guidelines of the Australian Prudential Regulatory Authority (“APRA”), prudent business management, and relevant internal policies.
2. This Policy specifically covers –
 - the counterparties to which treasury investments and loans can be made, and
 - limits on exposures to different counterparties, or classes of counterparty, and
 - the principles to be followed to make and manage loans, and
 - the provision of adequate and timely reporting to ensure the effective management of credit risk.

Credit Risk

3. “Credit Risk” is the risk of a counterparty to GAB not meeting its financial obligations to GAB as and when they fall due. More specifically –
 - Credit risk relates to a future event of default where a third party who has a debt obligation to GAB fails to meet that obligation either by the due date or not at all. This has the potential to trigger actions by GAB (eg. arrears management) and ultimately to a financial loss from writing down the value of the asset.
 - The occurrence of the future default event is uncertain.
 - The consequence of a credit default event is always negative because it will increase expenses and reduce interest margins. The direct consequences of a default includes some or all of the following –
 - triggering arrears management
 - triggering foreclosure and recovery of any security
 - writing off any remaining balance
4. GAB's exposure to credit risk arises from –
 - investing in treasury investments
 - making loans

Credit Risk Management

5. Credit risk management is the process of identifying, mitigating and managing the risk of default and the consequences if a default occurs.

Regulatory Considerations

Australian Prudential Standards

6. Banking Services operates on the basis of an exemption from the *Banking Act 1959*, with certain conditions. However, GAB has decided generally to adopt the relevant core underlying principles for effective risk management contained in APRA's Australian Prudential Standards (APS) as a basis for good management.
7. The most relevant APS standards in relation to credit risk management are –
 - *APS 112 Capital Adequacy: Standardised Approach to Credit Risk*
This standard sets out the capital requirements for credit risk. The Capital Allocation Policy specifically addresses the capital adequacy component.

- *APS 220 Credit Quality*
This standard covers the requirements for an effective credit risk management system.
- *APS 221 Large Exposures*
This standard deals with the management of large credit exposures.

Objectives of Credit Risk Management

8. The objective of GAB's credit risk management process is to ensure that –
- credit risk is identified, mitigated and managed for all transactions and reviewed on a regular and timely basis,
 - credit risk is measured using appropriate measurement techniques based on the principles of APRA capital adequacy measurement methods on a regular and timely basis,
 - GAB is regularly informed of the level and nature of credit risk within Banking Services,
 - credit risk is reviewed against credit risk limits and specified credit risk practices on a regular basis and any breaches are reported to GAB on a timely basis, and
 - corrective action is taken when any breaches occur.

Credit Risk Management of the Treasury Portfolio

Authorised Investments

9. An investment in a treasury investment is an Authorised Investment if, when the investment is made –
- it is with an Authorised Treasury Counterparty, and
 - it is a Permitted Investment made in Australian dollars, and
 - the Authorised Treasury Counterparty meets any applicable Credit Rating Grade, and
 - it does not cause a breach of the exposure limits applicable to that Authorised Treasury Counterparty.
10. The Authorised Treasury Counterparties, the Permitted Investments and applicable the Credit Rating Grades (if any) are as follows –

Authorised Treasury Counterparty	Permitted Investment	Credit Rating Grade
Australian Government	<ul style="list-style-type: none"> • Treasury notes • Treasury bonds • Treasury index bonds 	
State Government or Territory central borrowing authority	<ul style="list-style-type: none"> • Semi-government promissory notes • Semi-government bonds • Semi-government indexed bonds 	
Entity being an Authorised Deposit Taking Institution	<ul style="list-style-type: none"> • At call accounts and deposits, including 11 am deposits • Term deposits • Bank bills • Certificates of deposit 	1, 2, 3
Entity, being an Authorised Deposit Taking Institution, which is the clearing house for the account through which the Glebe Income Accounts are cleared.	<ul style="list-style-type: none"> • Deposit sufficient to meet clearing house requirements 	

11. An investment in an Authorised Treasury Counterparty will not be a Permitted Investment if the rating of the investment is lower than the credit rating grade of the counterparty.
12. The exposure limits applicable to an Authorised Treasury Counterparty are as follows –

Authorised Treasury Counterparty	Credit Rating Grade	Exposure Limit (excluding accrued interest) % of capital of Banking Services at the time investment is made
Australian Government		100%
A state government or territory central borrowing authority		50%
An authorised deposit taking institution	1	50%
	2	40% ¹
	3	30% ¹

1. These exposure limits are lower than those for ADIs with these credit ratings set out by APRA in APS 221. GAB considers that lower exposure limits should apply to such ADIs.

13. To determine the equivalent credit rating grade for an institution with a rating issued by an external credit rating agency (Standard & Poors, Moodys or Fitch) the mapping set out in tables 1 and 2 of APRA's *Prudential Practice Guide APG 112* applies. For the purposes of this Policy, the rating from Standard & Poors is to apply. Where there are different credit rating grades for an institution from Moodys and Fitch and no rating from Standard & Poors, the lowest of those ratings will be the credit grade rating for the institution for the purposes of this Policy.
14. As at the date of this Policy, GAB has exposures to several treasury counterparties which exceed the limits specified in this Policy. It is proposed to reduce those exposures within those limits when the relevant treasury investments mature.

Credit Risk Management of the Loan Portfolio

Loan Approvals

Obtaining loan approval

15. Loans are to be approved by GAB by resolution. A submission for approval for a loan is to contain, or be accompanied by a report about the proposed loan which contains, details of –
 - the borrower, which must be an Authorised Loan Counterparty (see paragraph 16),
 - the amount of the proposed loan, which must not exceed the applicable Exposure Limit for Lending (see paragraph 17),
 - the purpose of the proposed loan (see paragraph 19),
 - the loan term (see paragraph 20),
 - the proposed repayment arrangements (see paragraph 21),
 - a full financial assessment of the borrower for the preceding 2 financial years, and projections for the current and following financial years, which shows that the borrower will be able to meet the key financial ratios, and will otherwise be able to service debt and repay principal (see paragraph 22),
 - the proposed loan pricing (including interest rate and fees) (see paragraph 23),
 - the security for the loan (see paragraph 30 and Annexure A),
 - full details of the guarantors, (if any),
 - any proposed special conditions.

Authorised Loan Counterparties

16. The following entities are Authorised Loan Counterparties –
- a parish or other ecclesiastical district of the Anglican Church of Australia in the Diocese of Sydney, and
 - an organisation constituted by or under an ordinance of the Synod or the Standing Committee of the Synod of the Diocese of Sydney, and
 - an organisation, not being a Diocesan Organisation, which undertakes Christian ministry within the geographic boundaries of the Diocese of Sydney.

Amount of the Proposed Loan / Exposure Limit for Lending

17. The maximum exposure limit to an Authorised Loan Counterparty, and its subsidiary entities, is 20% of the capital allocated to Banking Services at the time the loan is made. Loans are to be made only in Australian dollars.

Note: If an exposure to an Authorised Loan Counterparty exceeds 10% of the capital allocated to Banking Services, additional capital is required to be allocated to support the loan. See the Capital Allocation Policy.

18. As at the date of this Policy, GAB has exposures to several loan counterparties which exceed the limits specified in this Policy. It is proposed to reduce those exposures within those limits when the opportunity to do so arises in accordance with the terms of the relevant loan commitments.

Purpose of the Proposed Loan

19. The loan must be for a purpose which is related to the charitable objects of the Authorised Loan Counterparty, and not be a purpose which is primarily investment related.

Loan Term

20. The maximum loan duration is 5 years.

Proposed Repayment Arrangements

21. Interest is to be paid by monthly instalments throughout the term.
22. Usually, repayments on account of principal are to be made at an appropriate rate during the term, in accordance with a repayment schedule which is determined at the date of approval of the loan.
23. At the borrower's request, provision may be made for principal reductions to be made in excess of any minimum payments required provided all accrued interest has been paid.

Financial Assessment

24. The financial projections of the borrower should indicate that prospective interest cover (ie net interest cover should the loan be approved) should be not less than 1.5 times.
25. For these purposes –
- $$\text{Net Interest Cover} = \text{EBLIT} / (\text{Net Interest} + \text{Finance Lease Charges})$$
$$= y \text{ times}$$
 - EBLIT is earnings before interest, finance lease charges and tax, and calculated by taking operating profit before tax and abnormal items plus net interest (ie interest paid less interest received and finance lease charges)

26. In respect of a loan to or for the purposes of a parish or other ecclesiastical district the interest commitment must not generally exceed 20% of the general offerings of the parish or district together with up to 80% of specific loan servicing pledges.

Proposed Loan Pricing

27. Loans will usually be made on a variable rate basis, with interest rates subject to variation each quarter, based on changes in the funding cost.
28. The interest rate margin applying to a loan (being the difference between the interest rate payable by the borrower on the loan and the funding costs of providing the loan) is to be determined at the time

the loan is approved and will not change for the term of the loan unless specifically provided for in the loan application/loan documentation. The interest rate margin is to be determined having regard to the following factors –

- the direct costs for the loan such (such as legal costs), and
- the overhead costs allocation, and
- risk related costs, including –
 - the costs of holding liquidity
 - the costs of holding capital
 - the costs of expected credit losses.

29. The following fees will be charged in respect of loans made by GAB at such rate as may be determined at the time the loan is approved –

- loan establishment fee
- line fee
- undrawn facility fee

Security for the loan

30. The principles relating to security for the loan are set out in Annexure A.

Acceptance by the Borrower

31. Upon a loan being approved by GAB, a written communication setting out the terms and conditions of the loan is to be sent to the borrower for its acceptance. The communication is to state that the borrower will be responsible for the cost of valuations, all legal fees and stamp duty, and other taxes relating to the proposed loan. Preparation of the formal loan documentation is not to commence until the borrower accepts the terms and conditions.

Loan Review during the Term

32. During its term, the loan will be reviewed in accordance with the following principles –

- where the total exposure to an Authorised Loan Counterparty is more than 10% of the capital allocated to Banking Services from time to time (a “Large Exposure”), the loan is to be reviewed no less frequently than every 6 months, and
- otherwise, the review will be undertaken no less frequently than every 12 months.

Arrears Management

33. A commercial view of arrears management is to be undertaken. While sensitivity and reasonableness are to be applied in all circumstances, GAB will undertake a professional approach to the default process. This includes seeking legal advice at an early stage about the action to be taken to enforce the rights of GAB under the loan documentation and enforce the security provided.

34. Arrears in excess of 15 business days are to be reported to GAB with information about the action proposed to be taken.

35. Where a loan is in arrears for a period of 90 days or more consideration is to be given to the creation of an appropriate provision for doubtful debts.

Maturing Loans

36. Not less than 3 months prior to maturity date a letter is to be sent to the borrower seeking an indication as to whether the borrower –

- intends to arrange repayment of the loan, or
- will seek to renew the loan, or
- will seek to renew the loan with additional funding.

37. Where consideration to be given to renewing a loan, with or without additional funding, an application to renew the loan is to be made in accordance with this Policy as if it were an application for a new loan. The application should be accompanied by –

- an updated valuation of the security,

- information about the current financial status of borrower,
- confirmation of insurance, and
- any other relevant information requested by GAB.

Reporting

38. Applications for loans are to be submitted to GAB for consideration.
39. Each month, GAB will receive a report about the following matters –
- the investments in Authorised Treasury Counterparties, identifying each Counterparty by name, the total of the amount invested, and
 - the loans made to Authorised Loan Counterparties, identifying each Counterparty by name, the amount lent and the term of the loan facility, and
 - arrears, and advice of the action taken in respect thereof, and
 - confirmation from management about compliance with these Policies.
40. Every 6 months, GAB will receive a report about the review of each Large Exposure.
41. GAB will receive reports about the following matters, when required –
- if at any time after a treasury investment is made, the investment ceases to be an Authorised Treasury Investment (as a consequence, for example, of the credit rating of the Treasury Counterparty having been downgraded), GAB is to be notified as soon as is practical about the rectification action (if any) which has been taken or which should be prudently taken, and the timeframe for that action,
 - if at times after a loan is made the maximum exposure to an Authorised Loan Counterparty, and its subsidiary entities, exceeds 20% of the capital allocated to Banking Services, GAB is to be notified as soon as is practical about the rectification action (if any) which should be prudently taken and the timeframe for that action,
 - reports about the reviews of loans (other than Large Exposures) will be provided to GAB if the relevant review foreshadows difficulties on the part of the borrower in complying with the terms of the loan, and the action (if any) which should be prudently taken and the timeframe for that action.

Staff Training

42. All staff involved in recommending, approving, implementing, monitoring and administering credit risk are to have appropriate experience in, training and understanding of interest rate risk and this Policy. As a result, such staff are required to undertake appropriate training.

Review of this Policy

43. GAB will review this Policy each year, and more frequently if circumstances require.

Commencement of this Policy

44. This Policy commences on 1 April 2012.

Document Approval

45. This Policy was approved by GAB on 28 March 2012.

Security for the Loan

Security

1. All loans are to be secured by a first registered mortgage of freehold land located in Australia. However, if the borrower is Anglican Church Property Trust Diocese of Sydney, acting on behalf of a parish, consideration will be given to approving a loan on an unsecured basis if –
 - prior to the loan being made, an ordinance is passed by the Standing Committee authorising the sale of property or the application of funds at the direction of GAB if the borrower fails to meet its obligations under the loan agreement, and
 - the borrower undertakes not to apply for, or obtain funding or financial accommodation from any person or corporation, or to encumber or dispose of its real property assets or encumber its cash flows, in either case, without the consent of GAB.
2. Land will not be acceptable security if –
 - the buildings on the land are of a purpose built design or construction or specialised usage and is not regarded as readily saleable in normal market conditions, or
 - it is used for any of the following –
 - for illegal or immoral purposes or for activities likely to offend the moral sensitivities of the Anglican Church Diocese of Sydney,
 - in any way in connection with gambling or betting,
 - for the sale by wholesale of tobacco in any form,
 - for the manufacture, sale, distribution or consumption of liquor other than for medicinal purposes or for purposes other than human consumption,
 - in any way in connection with narcotic drugs except as part of the trading practices of a registered pharmacist / chemist,
 - for the production, sale or distribution of 'X' or 'R' rated video or digital images or films,
 - for the manufacture, promotion, distribution or sale of armaments,
 - any other purpose or use deemed unacceptable by Standing Committee, or
 - the property is subject to or is likely to be subject to an environmental risk or risk of nature (such as flooding) which may adversely impact its value or saleability.

Valuations

3. Land to be taken as security is to be valued by a valuer acceptable to GAB who is –
 - a member of not less than 5 years standing of the Australian Institute of Valuers & Land Economists, and
 - the holder of a licence to practise as a valuer of the kind of property to be taken as security, and
 - experienced in valuing property of the kind offered to be taken as security.
4. The valuation is to state the valuer's opinion as to –
 - the fair market value of the land as at the date of the report,
 - the replacement cost for insurance purposes, and
 - general environmental issues.
5. The valuation is to be addressed to GAB, and state that the valuation has been undertaken for mortgage purposes.
6. If the valuation raises any concerns about environmental issues, a formal environmental report should be obtained to ensure that the property is not or is unlikely to be subject to an environmental risk.

Loan to Valuation Ratio

7. If the proposed loan would be a Large Exposure where the proposed security is residential property, the loan amount is not to exceed 70% of GAB's valuation of the security. For other forms of property, the loan amount is not to exceed 60% of GAB's valuation of the security.
8. For a proposed loan which would not be a Large Exposure, where the security is residential property, the loan amount is not to exceed 85% of GAB's valuation of the security. For other forms of property, the loan amount is not to exceed 65% of GAB's valuation of the security.

Insurance for Property

9. A policy or policies of insurance for each property to be taken as security must be maintained for the term of the loan and until the security is discharged. Such insurances are to –
 - be for the full insurable value of the property on a replacement and re-instatement basis and include the cost of demolition, removal of debris and professional fees,
 - be taken out with an insurance office or company acceptable to GAB,
 - contain conditions acceptable to or required by GAB,
 - have no exclusions, endorsements or alterations unless first approved in writing by GAB, and
 - be taken out in the names of both the mortgagor and GAB as mortgagee as the insured for their respective rights and interests.
10. A public risk insurance policy is also to be taken out for an amount of not less than \$10 million either as part of the comprehensive building insurance or as a separate policy.
11. The mortgagor is to pay all premiums and other moneys payable in relation to the insurance policy as they fall due and produce to GAB a receipt for the last premium and a certificate of currency on each anniversary date and whenever otherwise reasonably required to do so by GAB.
12. If a policy of insurance is not maintained as required by this Policy, GAB may effect any such insurance and recover the cost from the borrower or mortgagor.
13. The provisions of this section do not apply to security provided for or on behalf of a Parish or Diocesan Organisation if –
 - a. insurance for the property and public risk insurance for the mortgagor is effected and maintained by Anglican Church Property Trust Diocese of Sydney under the Church insurances program, and
 - b. the coverage provided by such insurances is at least that required by this Policy.