RECOMMENDATION FOR RETAIL DEPOSIT GUARANTEE SCHEME PROVISION

For the Year Ending June 2010

Prepared for the Treasury DGS Provisioning Committee meeting of 11 June 2010

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1. PROVISION RECOMMENDATION

The quantum of the provision recommended for June 2010 is $782m.

The provision for June 2010 represents a **decrease of $105m from the May 2010 provision of $887m** and a **decrease in the number of entities covered by the provision to 4** from the 8 agreed at the Treasury DGS Provisioning Committee for May 2010.

The provision is made up of three key components:

the Crowns share of the **loss given default** of $595m, which has decreased by $71m ($666m to $595m);

The **credit loss associated with SCF has dropped from $613m to $559m**. The prime driver of the reduction in credit loss is an improvement in the quality of the information on SCF's loan book, which has enabled circa $100m of delinquent loans to be recategorised as performing.

the estimated cost of **post acceleration interest of** $113m, which has decreased by $63m ($176m to $113m) due to :

Post acceleration Interest for SCF has reduced from $152m to $106m. The prime driver of the reduction in interest is improved information, in that we have a copy of the debenture register showing that 32% of the debentures are on the revised deed which allows the Crown to limit post acceleration interest. In addition, there has been a significant reduction in guaranteed deposits.

Post acceleration Interest for ANF, has reduced from $14m to $6m. Predominantly due to the significant reduction in guaranteed deposits from ($188m to 142m). In addition the information on which the calculation is based has improved markedly, in that we have a copy of the debenture register showing those debentures on the revised deed allowing the Crown to limit post acceleration interest.

the **net effect of discounting** cash flows of $74m, which has increased by $29m ($45m to $74m) due to:

The reduced benefit of delayed payout with investments under the revised deed being paid out earlier.

Updating discount rates to the year end discount rates used in the Government accounts.

1. PROVISION RECOMMENDATION

Key points for the June 2010 provision are:

- SCF continues to be inspected by KordaMentha. Areas of focus for the inspection are; a full discounted cash flow model of the expected loss to the Crown under receivership , expected loss to the Crown under the potential "recapitalisation" proposals, and an audit of it's debenture register (to speed up any payout that may be required).

- Mutual Finance Limited entered receivership on the 14th of July 2010 (post balance date event).

- On the 3rd of August 2010 ANF's parent Allied Farmers Limited ("ANF") announced a partially underwritten $19m capital raising, which was expected to be used to repay its banking facility and provide additional support to ANF – this is not currently proceeding due to the announcement of the 6th of August 2010.

- On the 6th of August ANF's Trustee announced that ANF had breached a trust deed ratio (total liabilities to total tangible assets) and had 14 days to remedy the breach. To remedy this breach ANF will need to inject addition capital, however additional capital will not resolve ANF's liquidity issues.

- On the 11th of August ANF was downgraded by Standard and Poor's to CC from BB- (post balance date event).

The table below provides an elemental break down of the provisioning recommendation for June 2010 .

Entity Name	Risk Ranking Measures					Guaranteed		Loss Given Default Calculations			Estimated Failure Parameters	
	Liquidity[1] x's	Asset Quality[2] %	Income Margin[3] %	Capital Ratio[4] %	Related Party Exposure[5] %	Depositors #	Deposits $m	Estimated Crown Loss	Post Acceleration Interest	Total Crown Loss	Date of Failure	Reason for Failure
South Canterbury Finance Limited	0.40	55.65	0.80	0.69	1,302.97	23,119	1,611	559	106	665	Aug-10	Equity, Liquidity
Allied Nationwide Finance Limited	0.64	39.54	10.48	0.12	-	4,558					Aug-10	Equity, Liquidity
	0.38	65.27	7.71	21.81	-	204	*[Withheld under s.9(2)(b)(ii)]*				Sep-10	Equity, Liquidity
Mutual Finance Limited[6]	*1.71*	*43.12*	*22.77*	*6.36*	*3.16*	*395*					*Jul-10*	*Equity, Liquidity*
	Sub Total					**28,276**	**1,767**	**595**	**113**	**708**		
	Plus Nett Effect of Discounting									**74**		
	Total Crown Loss / Provision Reconmendation									**782**		

Notes

[1] Liquid assets + short term asset maturities + committed facilities as a multiple to short term liability maturities

[2] Impaired + past due + 75% Cap Interest + 50% restructured loans as a percentage of total loans

[3] Net margin: Annualised net-interest-income + Fee Income to gross loans

[4] Capital ratio methodology utilising the proposed capital framework for NBDTs

[5] Related Party exposure as % of Net Tier 1 Capital

[6] Based on May 2010 data. June 2010 data was not submitted - entity failied 16 July 2010.

2. HISTORICAL PROVISIONING RECOMMENDATIONS

	Movements in the Provision by Month										
	Jun-09	Sep-09	Oct-09	Nov-09	Dec-09	Jan-10	Feb-10	Mar-10	Apr-10	May-10	Jun-10
Loss given default incl PAI interest											
South Canterbury Finance Limited	742	742	716	704	687	672	696	721	721	765	665
Allied Nationwide Finance Limited											
					[Withheld under s.9(2)(b)(ii)]						
Viaduct Capital Limited[1]										receivership	receivership
Rockforte Finance Limited[2]										receivership	receivership
Vision Securities Limited[3]										receivership	receivership
Mutual Finance Limited[4]											
Total Loss given default incl interest	**894**	**799**	**814**	**806**	**734**	**726**	**803**	**830**	**829**	**839**	**708**
Discounting of Cashflows											
Benefit of delayed payout	(80)	(77)	(140)	(151)	(144)	(143)	(145)	(81)	(82)	(83)	(13)
Cost of delayed receivers' distribution	0	137	217	217	184	185	190	131	130	128	87
Net impact of discounting	**(80)**	**61**	**77**	**66**	**40**	**42**	**45**	**49**	**48**	**45**	**74**
Total Provision	**814**	**860**	**891**	**872**	**774**	**768**	**848**	**879**	**877**	**884**	**782**

Notes

[1] Viaduct Capital Limited went into receivership 13 May 2010.

[2] Rockforte Finance Limited went into receivership 10 May 2010.

[3] Vision Securities Limited went into recievorship 31 March 2010.

[4] Mutual Finance Limited went into recievorship 16 July 2010.

3. PROVISION – LOSS GIVEN DEFAULT (SCF)

Entity Name - South Canterbury Finance ("SCF")
Credit Rating - BB Negative Watch
DGS Status - Withdraw and replace complete / Accepted for extension.
Expected Date of Failure – August-10
Expected Reason for Failure – Lack of Equity / Liquidity / Credit Quality

June Update

KordaMentha contines to inspect SCF at the Crown's request. The scope of the inspection includes; a full discounted cash flow model of the expected loss to the Crown under receivership, the expected loss to the Crown under the potential "recapitalisation" proposals, and an audit of it debenture register (to speed up any payout that may be required). In addition, key "trip up" event are being monitored (liquidity, covenant compliance etc).

There are a number of parties currently considering the recapitalisation of SCF in varying ways. All interested parties are at different stages of development of their proposal. To avoid receivership, a recapitalisation proposal will require binding heads of Agreement by the 20th of August – this will allow the recapitalisation to be announced (subject to regulatory consents) on the 31st of August 2010 which will coincide with the release of SCF's 30 June 2010 full year and thereby avoid receivership.

SCF is currently operating with the benefit of a waiver SCF's Trustee in relation to a breach of its capital ratio.

SCF's Trustee waiver expires on 31 August 2010 and in the absence of an agreed recapitalisation proposal by that date, SCF's Trustee is expected to give notice of default on that date and SCF will enter receivership if this occurs. In addition, SCF is also expected to run out of cash on or about 31 August 2010.

Further compounding issues include the inability to raise debenture funding due to Alan and Jean Hubbard and "associated Hubbard entities" being under statutory management and the constant barrage of negative press surrounding SCF.

Internally, SCF appears to have accepted that with out a recapitalisation SCF will fail on or about the 31st of August 2010.

Recommendation

Based upon the information held by Treasury and the issues outlined above, it is considered probable that SCF will default under the existing Crown Guarantee on or about 31 August 2010 and therefore a provision is required.

Work is underway with KordaMentha to further refine the expected loss to the Crown under receivership and the "recapitalisation" proposals that are forming.

The quantum of the provision recommended (exclusive of the net effect of discounting cash flows) is $665m, being the Crown's Share of the loss given default of $559m plus an allowance for post acceleration interest of $106m.

South Canterbury Finance Limited

Liquidity[1] x's	Asset Quality[2] %	Income Margin[3] %	Capital Ratio[4] %	Related Party Exposure[5] %	Guaranteed Depositors[6] #	Month	Amount DGS	Non Gteed Deposits	Other Liabilities	Total Liabilities	Other assets	Cash & Liquid Assets	Net Loan Book	Total Assets	Loss-Given Default	Crown Loss-Given Default	Post Acceleration Interest	Provision Recommended
0.4	56	0.8	0.7	1,303.0	40,000	June	1,611	129	5	1,794	300	49	848	1,207	588	559	106	665
0.4	63	1.1	0.8	1,148.8	40,000	May	1,732	20	5	1,788	281	92	899	1,283	632	613	151	764
0.7	45	1.2	- 2.5	261.0	40,000	April	1,700	160	31	1,896	225	63	985	1,286	610	570	151	721
0.8	44	0.8	2.0	285.9	40,000	March	1,707	160	21	1,893	75	196	1,005	1,285	607	571	151	721
1.1	31	1.0	1.6	250.7	40,000	February	1,712	164	21	1,902	75	14	1,208	1,320	582	545	151	696
1.6	28	1.0	1.1		40,000	January	1,667	166	23	1,933	76	37	1,239	1,379	554	518	154	672
1.2	29	1.6	1.8		40,000	December	1,746	159	13	1,918	107	28	1,221	1,355	563	533	154	687
2	29	2.4	2.6		40,000	November	1,790	148	18	1,955	107	47	1,280	1,433	522	478	227	705
6	26	2.7	2.3		40,000	October	1,832	151	28	2,011	110	90	1,304	1,504	507	480	236	716

Notes
[1](Dec - Liquid assets + short term asset maturities + committed facilities as a multiple to short term liability maturities) (Oct to Nov - Liquid assets + 50% committed facilities as a percentage of guaranteed deposits)
[2]Impaired + past due + 75% Cap Interest + 50% restructured loans as a percentage of total loans
[3]Net margin: Annualised net-interest-income + Fee Income to gross loans
[4]Capital ratio methodology utilising the proposed capital framework for NBDTs
[5] Related Party exposure as % of Net Tier 1 Capital
[6] Total guaranted depositors is estimated at 40,000. Data set is incomplete.

3. PROVISION – LIQUIDITY HISTORY (SCF)

The table below outlines SCF's liquidity history, and illustrates their debenture and asset payment profiles.

South Canterbury Finance Limited

Weekly Liquidity Reporting

	Liquid assets				Financial assets maturity profile (excluding liquid assets)							Retail funding maturities								Re-investment			New funding	
Date	Bank	Other	Total	Undrawn committed facilities	At call	0 - 1 month	1-2 months	2-3 months	3-6 months	Other maturities	Total	At call	0 - 1 month	1-2 months	2-3 months	3-6 months	Other maturities	Total	Total wholesale maturites	Re-invested fund	Maturing funds	Re-investment rate	New call funding	New term funding
4/09/2009	92	1	93	100	135	101	88	68	148	908	1447	38	58	69	69	187	1428	1848	125			0.00		
11/09/2009	83	1	84	100	158	84	75	73	146	923	1460	42	64	67	68	184	1415	1841	125			0.00		
18/09/2009	68	1	69	100	134	104	78	88	134	919	1457	25	73	66	70	179	1419	1832	125			0.00		
25/09/2009	74	1	75	100	121	101	106	95	146	916	1486	25	79	70	60	180	1405	1819	125			0.00		
2/10/2009	70	1	71	100	151	131	83	83	124	918	1490	23	69	67	71	174	1385	1790	125			0.00		
9/10/2009	61	1	62	0	144	124	103	90	140	887	1487	22	73	64	69	177	1372	1776	125			0.00		
16/10/2009	59	1	59	0	164	102	98	71	167	883	1485	24	63	72	69	173	1360	1761	200			0.00		
23/10/2009	51	1	51	0	220	69	119	74	174	834	1490	23	81	57	71	179	1346	1757	200			0.00		
30/10/2009	28	1	28	0	127	176	122	70	152	866	1513	21	77	63	76	172	1360	1770	213	0	1	30.12	0	9
6/11/2009	56	1	57	0	134	190	117	65	154	866	1527	21	74	67	71	184	1364	1782	213	7	14	52.36	0	12
13/11/2009	56	1	56	0	113	204	74	72	148	940	1551	21	77	66	74	197	1355	1789	213	5	10	50.46	1	10
20/11/2009	52	1	52	0	126	177	62	70	137	980	1553	27	68	65	70	210	1343	1783	213	5	8	54.16	0	5
27/11/2009	51	1	52	0	122	80	77	94	186	994	1553	21	69	71	61	237	1324	1782	213	6	18	32.96	0	7
4/12/2009	36	1	37	0	109	88	112	66	244	955	1574	21	69	80	57	245	1388	1860	129	3	6	43.23	1	6
11/12/2009	37	1	37	0	142	92	78	64	257	957	1590	19	74	72	51	267	1367	1850	129	2	4	48.03	0	4
18/12/2009	31	1	31	0	148	83	82	78	268	946	1604	24	70	67	50	360	1296	1867	122	2	4	56.43	0	8
25/12/2009	31	1	31	0	148	83	91	87	286	952	1612	20	60	74	49	368	1289	1860	122	6	19	30.03	0	10
1/01/2010	11	1	11	0	130	66	91	87	286	952	1612	20	60	74	49	368	1289	1860	122	6	19	30.03	0	10
8/01/2010	17	1	17	0	146	103	102	179	197	880	1607	22	74	55	55	387	1261	1854	122	10	20	49.62	0	2
15/01/2010	26	1	26	0	132	121	83	213	247	884	1681	23	71	50	60	397	1268	1870	110	3	7	43.45	0	9
22/01/2010	33	1	33	0	144	108	87	199	257	880	1676	24	70	48	67	399	1265	1873	110	6	15	40.85	0	7
29/01/2010	43	1	44	0	140	134	129	98	274	913	1688	23	61	58	64	406	1263	1875	110	11	21	54.56	0	8
5/02/2010	79	1	80	0	199	126	181	50	279	856	1691	23	57	60	73	408	1257	1878	110	3	5	57.41	0	11
12/02/2010	116	1	116	0	207	105	193	27	271	856	1658	20	126	59	96	317	1259	1879	110	8	15	55.61	0	9
19/02/2010	120	1	121	0	216	104	198	49	246	824	1637	20	125	71	98	311	1255	1880	110	8	18	45.50	0	7
26/02/2010	115	1	115	0	217	104	198	49	246	824	1638	18	123	71	118	300	1219	1849	123	6	15	39.46	0	9
5/03/2010	46	1	46	0	300	139	83	48	245	823	1638	20	135	76	122	285	1144	1781	75	8	17	49.34	0	5
12/03/2010	55	1	56	0	199	99	196	64	247	832	1637	19	134	76	119	267	1158	1772	75	6	14	39.39	0	7
19/03/2010	48	1	48	0	196	99	196	63	247	832	1633	18	146	99	128	246	1132	1769	75	4	12	31.11	0	4
26/03/2010	48	1	49	0	194	102	187	66	249	820	1618	18	149	120	114	234	1130	1766	75	4	12	33.66	0	6
1/04/2010	34	1	35	0	196	105	178	62	258	828	1627	26	77	113	137	216	1214	1783	75	1	6	12.47	0	2
9/04/2010	38	1	39	0	194	101	173	62	255	826	1611	18	149	115	125	213	1134	1754	75	4	9	50.08	0	7
16/04/2010	46	1	47	0	191	103	174	59	252	823	1602	18	101	199	115	221	1111	1764	75	7	15	45.45	0	11
23/04/2010	38	1	39	0	196	99	171	69	249	810	1594	20	119	190	110	519	797	1755	75	8	24	33.68	0	6
30/04/2010	92	1	92	0	198	89	146	28	252	821	1533	18	130	190	98	508	809	1753	75	3	8	32.69	0	9
7/05/2010	86	1	87	0	197	93	153	21	254	815	1533	18	130	190	94	499	814	1745	75	9	30	30.86	0	9
14/05/2010	85	1	85	0	181	84	153	20	199	890	1527	35	121	172	89	491	821	1730	75	15	37	39.91	0	7
21/05/2010	80	1	81	0	81	58	151	22	189	1030	1531	36	117	168	83	485	837	1726	75	4	14	25.92	0	9
28/05/2010	66	1	67	0	67	32	162	25	72	1184	1542	39	106	153	83	467	862	1710	75	25	49	51.82	0	9
4/06/2010	93	1	93	0	93	167	29	23	75	1198	1585	37	110	139	79	459	879	1703	100	9	17	53.20	0	10
11/06/2010	89	1	90	0	90	178	24	23	76	1154	1545	40	105	137	63	440	885	1670	100	8	17	48.79	0	6
18/06/2010	68	1	69	0	69	175	27	20	92	1180	1563	40	82	125	53	395	973	1668	100	14	34	42.21	0	7
25/06/2010	53	1	54	0	54	149	28	20	92	1208	1551	28	77	133	36	349	1029	1652	100	16	37	42.46	0	6
2/07/2010	50	1	50	0	50	31	36	23	80	1297	1517	7	68	56	44	418	1060	1653	100	19	39	48.21	0	1
9/07/2010	37	1	37	0	37	24	38	25	90	1283	1497	26	64	49	258	374	870	1641	100	11	28	39.09	0	3
16/07/2010	33	1	34	0	34	26	30	29	84	1286	1489	25	62	45	258	373	869	1632	100	7	19	39.55	0	2
23/07/2010	30	2	31	0	31	33	27	28	88	1278	1485	23	59	35	266	373	860	1616	100	8	24	35.71	0	2
30/07/2010	27	1	28	0	28	45	29	15	88	1244	1449	22	56	45	252	373	859	1607	100	9	21	43.13	0	3
6/08/2010	20	1	21	0	21	30	26	14	90	1264	1445	20	53	44	250	373	857	1597	100	8	22	36.62	0	2

3. PROVISION – LOSS GIVEN DEFAULT (ANF)

Entity Name - Allied Nationwide Finance Limited ("ANF")
Credit Rating - BB-
DGS Status - Withdraw and Replace Complete / Not eligible for extension.
Expected Date of Failure - August-10
Expected Reason for Failure - Liquidity / Credit Quality

June Update

There have been no material changes in regard to the reported quality of ANF asset position, however the liquidity position continues to deteriorate.

An inspection of ANF has been completed by both Grant Thornton (Crown appointed) and McGrathNicol (Trustee Appointed) in the past two months. The scope of the inspections included liquidity, management control environment, equity, asset quality and reporting data quality.

The conclusions of the inspection reports were consistent with the original KordaMentha inspection report of August 2009. That is, ANF are in breach of a trust deed ratio (total liabilities to total tangible assets) that requires additional capital to be injected (to remedy the breach). In addition, ANF has a significant liquidity issue that should bring about its failure.

On the 3rd of August 2010 ANF's parent Allied Farmers Limited ("ANF") announced a partially underwritten $19m capital raising to repay its banking facility and provide additional support to ANF.

On the 6th of August Allied Nationwide Finance Limited 's Trustee announced that ANF had a breached a trust deed ratio (total liabilities to total tangible assets) and had 14 day to remedy the breach – or receivership will occur.

On the 11th of August ANF was downgraded by Standard and Poor's to CC from BB- due to the significant liquidity issue that it is facing and report breach of the trust deed.

To remedy this breach of the trust deed, ANF will be required to inject addition capital which is not considered likely as the capital raising of ANF parent (ANF) is not able to proceed while ANF's prospectus is off market.

ANF's parent Allied Farmers Limited ("ANF") have to date been unable to provide support to ANF beyond extending the credit support agreement by $5m to $10m due to the financial strain that it is under. ANF's banker (Westpac) is understood to be demanding the pay down of its facility with any surplus cash at the parent level.

Recommendation

Based upon the information held by Treasury and the issues outlined above, it is considered probable that ANF will default under the existing Crown guarantee on or about the 20th of August and therefore a provision is required.

** [Withheld under s.9(2)(b)(ii)]*

The quantum of the provision recommended (exclusive of the net effect of discounting cash flows) is [*] being the Crown's Share of the loss given default of [*] plus an allowance for post acceleration interest of [*]

Allied Nationwide Finance Limited

Liquidity[1] x's	Asset Quality[2] %	Income Margin[3] %	Capital Ratio[4] %	Related Party Exposure[5] %	Guaranteed Depositors #	Month	Amount DGS	Non Gteed Deposits	Other Liabilities	Total Liabilities	Other assets	Cash & Liquid Assets	Net Loan Book	Total Assets	Loss-Given Default	Crown Loss-Given Default	Post Acceleration Interest	Provision Recommended
0.6	40	10.5	0.1	-	4,558	June	142	3	5	153	3	5	103	118				
0.9	37	8.7	0.9	184.3	4,976	May	155	3	5	166	3	9	117	133				
1.5	40	9.0	2.3	37.9	5,690	April	190	3	4	202	3	29	128	160				
4.0	39	8.6	2.3	37.5	5,784	March	192	3	4	204	4	25	131	162				
3.7	37	7.6	2.5	34.7	5,851	February	192	3	4	204	-	21	138	165				
4.7	34	5.8	2.4		5,973	January	197	3	3	208	4	29	147	182				
7.5	34	5.4	2.4		6,122	December	202	3	3	212	4	27	151	184				
15.0	32	5.0	1.1		6,387	November	201	3	7	213	4	31	138	175				
16.0	32	5.2	1.6		6,323	October	204	3	6	215	4	28	139	177				

Notes

[1](Dec - Liquid assets + short term asset maturities + committed facilities as a multiple to short term liability maturities) (Oct to Nov - Liquid assets + 50% committed facilities as a percentage of guaranteed deposits)

[2]Impaired + past due + 75% Cap Interest + 50% restructured loans as a percentage of total loans

[3]Net margin: Annualised net-interest-income + Fee Income to gross loans

[4]Capital ratio methodology utilising the proposed capital framework for NBDTs

[5] Related Party exposure as % of Net Tier 1 Capital

3. PROVISION – LIQUIDITY HISTORY (ANF)

The table below outlines ANF's liquidity history, and illustrates their debenture and asset payment profiles.

Allied Nationwide Finance Limited

Weekly Liquidity Reporting

	Liquid assets				Financial assets maturity profile (excluding liquid assets)							Retail funding maturities								Re-investment			New funding	
Date	Bank	Other	Total	Undrawn committed facilities	At call	0 - 1 month	1-2 months	2-3 months	3-6 months	Other maturities	Total	At call	0 - 1 month	1-2 months	2-3 months	3-6 months	Other maturities	Total	Total wholesale maturites	Re-invested fund	Maturing funds	Re-investment rate	New call funding	New term funding
4/09/2009	31	4	35	0	47	18	5	8	15	81	174	6	6	9	9	16	159	206	1	1	2	58.82	-1	0
11/09/2009	36	0	36	0	37	28	8	4	14	82	174	6	7	8	10	15	160	206	1	1	1	67.86	0	0
18/09/2009	35	0	35	0	38	29	8	6	13	82	175	6	5	9	10	15	161	205	1	1	1	69.23	0	0
25/09/2009	33	0	33	0	37	29	8	8	11	83	176	6	8	8	9	14	160	205	1	1	1	58.73	0	0
2/10/2009	30	0	30	0	39	30	6	7	10	81	173	6	7	10	7	16	159	205	1	2	2	80.18	0	0
9/10/2009	34	0	34	0	38	32	7	6	11	82	174	6	8	9	6	17	160	206	1	1	2	80.45	0	1
16/10/2009	28	0	28	0	38	34	4	6	17	81	181	6	7	10	6	18	160	206	1	2	2	79.34	0	0
23/10/2009	29	0	29	0	36	34	7	3	17	83	179	6	7	10	5	21	158	206	1	1	2	77.90	0	0
30/10/2009	30	0	30	0	34	33	7	4	17	84	179	6	9	7	5	23	156	206	1	1	1	58.47	0	0
6/11/2009	35	0	35	0	37	31	7	2	14	78	171	6	8	7	5	25	152	203	1	2	3	61.79	0	-3
13/11/2009	34	0	34	0	40	30	7	2	16	78	173	6	9	6	5	28	150	203	1	1	1	64.62	0	0
20/11/2009	32	0	32	0	40	34	4	2	16	78	174	6	9	5	5	34	143	202	1	1	1	70.18	0	0
27/11/2009	29	0	29	0	35	33	3	2	17	83	174	6	7	5	5	70	108	200	1	1	4	29.41	0	-2
4/12/2009	31	0	31	0	35	34	2	4	19	78	171	6	6	6	5	81	96	199	1	1	2	53.78	0	-1
11/12/2009	29	0	29	0	39	30	2	4	18	78	171	6	5	5	5	86	91	198	1	1	2	32.26	0	-1
18/12/2009	25	0	25	0	39	29	3	5	18	82	175	5	5	5	5	87	90	197	1	1	2	43.51	0	0
25/12/2009	20	0	20	0	43	25	7	5	18	82	180	5	4	5	5	88	89	197	1	1	1	50.00	0	-1
1/01/2010	21	0	21	0	44	24	7	5	19	81	180	6	5	5	6	88	87	197	1	0	0	59.57	0	0
8/01/2010	23	0	23	0	38	22	8	3	18	87	176	6	5	5	7	87	87	197	1	1	2	77.12	0	0
15/01/2010	27	0	27	0	36	22	8	9	13	83	171	6	4	5	8	87	86	197	1	1	2	57.24	0	0
22/01/2010	27	0	27	0	36	24	9	8	13	83	173	5	3	5	8	87	87	196	1	1	1	65.85	0	0
29/01/2010	25	0	25	0	38	28	5	9	14	80	172	5	5	5	13	85	84	197	1	1	1	66.33	0	0
5/02/2010	29	0	29	0	38	28	3	9	13	78	169	5	5	6	15	71	94	195	1	1	2	56.67	0	-1
12/02/2010	29	0	29	0	32	29	4	8	13	84	169	5	5	8	14	70	94	196	1	1	1	74.44	0	1
19/02/2010	29	0	29	0	32	29	9	2	13	84	168	5	4	9	17	67	92	194	1	1	1	57.30	0	-2
26/02/2010	26	0	26	0	34	26	9	2	14	86	171	5	4	10	44	39	91	193	1	0	1	50.65	0	0
5/03/2010	28	0	28	0	36	25	9	5	11	84	170	5	5	12	41	33	97	193	1	1	1	78.81	0	0
12/03/2010	28	0	28	0	35	24	10	6	10	85	169	5	7	12	42	32	95	193	1	0	1	58.67	0	0
19/03/2010	27	0	27	0	36	30	3	7	9	84	169	5	8	13	41	32	94	193	1	1	1	42.98	0	0
26/03/2010	26	0	26	0	33	30	4	7	9	86	169	5	10	24	29	33	92	193	1	0	1	33.96	0	0
2/04/2010	22	0	22	0	32	33	7	4	10	86	171	5	9	38	16	34	90	191	1	1	3	51.27	0	-1
9/04/2010	23	0	23	0	31	33	7	4	10	84	169	5	11	42	9	63	60	190	1	1	2	36.32	0	-1
16/04/2010	22	0	22	0	35	27	6	4	17	80	168	5	12	41	9	65	57	189	1	1	2	46.29	0	-1
23/04/2010	24	0	24	0	36	25	7	3	17	79	166	5	13	39	9	65	57	188	1	2	3	56.38	0	-1
30/04/2010	31	0	31	0	29	26	5	3	20	78	162	5	36	16	8	63	56	185	1	1	2	32.11	0	-3
7/05/2010	31	0	31	0	30	28	4	3	22	68	155	5	40	10	10	61	57	183	1	2	4	52.30	0	-2
14/05/2010	29	0	29	0	29	28	4	3	21	70	154	5	40	8	13	59	57	181	1	1	3	30.15	0	-2
21/05/2010	26	0	26	0	29	29	3	3	22	70	155	5	38	9	14	57	56	179	1	2	4	38.29	0	-2
28/05/2010	9	0	9	0	27	28	3	2	21	70	152	5	15	9	15	59	57	159	1	5	25	19.00	0	-20
4/06/2010	3	0	3	0	31	24	3	2	21	69	151	5	9	10	14	58	55	151	1	0	7	0.00	0	-8
11/06/2010	1	0	1	0	24	24	3	4	20	73	147	4	8	12	13	56	54	148	1	1	3	21.73	0	-3
18/06/2010	2	0	2	0	25	23	3	4	23	69	147	4	8	13	12	56	54	147	1	1	2	35.85	0	0
25/06/2010	4	0	4	0	26	21	2	4	28	63	144	4	8	15	13	52	54	147	1	1	2	51.85	0	-1
2/07/2010	6	0	6	0	26	21	2	4	28	60	141	4	8	15	17	47	54	146	1	1	2	23.26	0	-1
9/07/2010	6	0	6	0	28	21	3	4	22	60	138	4	10	14	46	17	54	145	1	1	2	43.18	0	-1
16/07/2010	7	0	7	0	24	19	3	9	15	61	131	4	11	12	48	13	54	143	1	0	2	11.74	0	-2
23/07/2010	8	0	8	0	22	18	4	9	15	59	128	4	13	12	47	12	53	141	1	0	2	0.00	0	-2
30/07/2010	6	0	6	0	21	18	4	9	15	58	124	4	14	15	41	11	52	138	1	0	2	0.00	0	-4
6/08/2010	5		5	0	22	19	4	14	9	56	123	4	13	18	37	12	51	135	1	0	4	0.00		

[Next 6 pages withheld under s.9(2)(b)(ii)]

5. PROVISION – POST ACCELERATION INTEREST & DISCOUNTING

Cash flow projections for Investor Payout (including post acceleration interest) and Receiver Distributions

Cashflow forecasts are produced to enable the DMO to plan for the Crown to meet its cash obligations under the Guarantee Scheme, to inform the calculation of post acceleration interest liabilities for defaulting entities and to enable the provision for loss given default to be stated on a net present value basis. The process of forecasting cashflows is fraught with many uncertainties, this paper sets out the assumptions which underpin the forecast for the approval of the provisioning committee.

Investor Payout & Receiver Distribution Assumptions

The particular variables on which assumptions must be made are set out below:

Variable	Assumption
Which entities will default	The cash flow projection is based on the default of the entities for which provision has been made in the June accounts
The timing of any default	Default timing is based on key known triggers identified in provisioning papers – for instance, credit downgrades, liquidity walls, inability to renew prospectuses.
The claiming pattern of investors	Under the original deed covering investments made up to 31 Dec 2009, the Crown is liable for post acceleration interest in most cases until the date of repayment. The Crown requires a claim to be made to assess eligibility before investors can be paid out, therefore the Crown cannot impel investors to make a claim. It is therefore assumed that investors will fall into three categories - those who need the money immediately and will put in a claim early, - those who will claim when their investment was due to mature (as this was when they expected the money), and - those who will hold off claiming in the interest of continuing to earn high interest rates. The early claimers are expected to net off against the late claimers and thus on average the maturity profile of the entity is the best indicator of claiming pattern. Under the revised deed the Crown is able to limit the period that interest is payable, based on a reasonable period to submit a claim. The Interest calculation therefore assumed that investments made under the revised deed would be paid out 10 weeks post default and that investments under the original deed would be paid out on maturity date.
The amount of distribution from receivers	The loss given default per entity has already been calculated for provisioning. This includes the cost of receivership. Therefore the receiver payout is assumed to be the gross amount paid out by Treasury less the loss given default.
The timing of distributions	In SCF's case advice on big receiverships (greater than $1b) was sourced from PWC who advised that the total process could take 6 years, distribution was thus assumed to be spread evenly over the 5 years subsequent to default. For most the other entities in the provision the distribution pattern for National finance has been used as the model – the distribution took 3 years with the final payment being about 20% of the total.
Discounted cash flows	Cash flows of both payout to investors and distributions from receiverships have been discounted to present value using Government discount rates. The net effect is to increase the anticipated loss given default by $74m, due to the extended timeframe for distribution from receiverships exceeding the benefit gained from the spread of the timing of payout.

Departmental costs of Administering the Guarantees

In addition to the actual Crown cashflows for investor monies paid out and receiver distributions, there are likely to be some additional costs incurred for risk monitoring/management and for managing the payout process itself. These costs would be covered by the PLA. These costs are estimated at a further $2.25m for investigations and $10m for payout which is allocated across the years based on the payout pattern.

5. PROVISION – POST ACCELERATION INTEREST & DISCOUNTING

Timing Assumptions

The table below illustrates that projected cash flows for payouts and distributions from receiverships.

Retail Deposits Guarantee Scheme
Distibutions from Receivership
Timing Assumptions
For June 2010 accounts

Company Name (credit rating if available)	Default assumptions as at	Likely Timing For default
South Canterbury Finance Limited		Aug 2010
Allied Nationwide Finance Limited		Aug 2010
*		Aug 2010
Mutual Finance Ltd		Jul 2010
Cashflows per annum calculated		

Timeframe of % paid out by year

2010/11 %	2011/12 %	2012/13 %	2013/14 %
87%	9%	4%	1%
80%	17%	3%	
95%	5%		
95%	5%		

Proportion of receiver payout per year

2010/11 %	2011/12 %	2012/13 %	2013/14 %	2014/15 %
20%	20%	20%	20%	20%
40%	40%	20%		
40%	40%	20%		
40%	40%	20%		

Gross cashflows

Company Name (credit rating if available)	Total to be paid out incl interest $m	Expected amounts from receivership $m	Treasury Estimated loss-given default $m
South Canterbury Finance Limited	1,717		
Allied Nationwide Finance Limited	148		
*	6		
Mutual Finance Ltd	8		
Total cash flow	1,880	[redacted]	708
Net Present value of cashflows	1,866	[redacted]	
Discount (benefit)/cost	(13)	[redacted]	74
Loss Given Default post discounting			781

Payout per year

2010/11 $m	2011/12 $m	2012/13 $m	2013/14 $m
1,490	153	62	12
[redacted]			*
[redacted]			
[redacted]			
1,623	179	66	12
1,623	172	61	11

Receiver Distributions per year

2010/11 $m	2011/12 $m	2012/13 $m	2013/14 $m	2014/15 %
[redacted]				
[redacted]				
[redacted]				
[redacted]				
[redacted]				
[redacted]				

** [Withheld under s.9(2)(a)]*

6. METHODOLOGY

Information

In developing the recommended provision Treasury has relied primarily on information collected as part of the monitoring conducted by the Reserve Bank of New Zealand ("RBNZ"). That information includes but is not limited to monthly financial information which is to be reconciled with the annual and semi annual reports of the entities to ensure its accuracy. RBNZ are contracted by The Treasury to use this information to provide an assessment of the possible loss to the Crown in event of default of an entity.

The Treasury also uses additional information sourced directly from the entities covered by the Deposit Guarantee Scheme ("DGS"), Inspections (where these have been conducted) and from other market participants (Government Agencies, Banks, Professional Services Firms etc) in our assessment of the possible loss to the Crown in event of default of an entity.

Provisioning Recommendation

The provisioning recommendation made to the provisioning committee is made up of three components, **loss given default**, **post acceleration interest** and **net effect of discounting**.

To arrive at a **loss given default** for an entity, the RBNZ undertakes a loss given default assessment of the loan book to arrive at a discounted loan book value, which is then added together with other assets held by the entity (after discounting) to calculate the liquidated value of total assets. Total assets are then applied to the Total liabilities (including an allowance for "costs") to assess the equity shortfall (if any) and the Crown's loss under a liquidation scenario or loss given default.

The RBNZ model output is then reviewed by The Treasury to assess the appropriateness of the indicated loss given the additional information held by The Treasury, and adjustments are made as required. This process also includes arriving at an estimation of the expected timing of an entities default.

To arrive at an estimate of the Crown's **post acceleration interest** liability given the failure of an entity, the Treasury models the post acceleration interest liability using the date an entity is expected to fail, the level of guaranteed deposits, the terms of those deposits (term, interest rate, trust deed and Crown Deed of Guarantee provisions, etc) and the expected timing of depositor repayment.

The provisioning recommendation has been completed on the basis that post acceleration interest is payable, which is the case for the current and the amended and restated deed. Once the extension deed is on foot (post 12 October 2010) post acceleration interest is no longer payable.

The post acceleration interest model is then enhanced with a forecast of payout and receivers distributions. The cash outflows (post acceleration interest and payment of depositors) and the cash inflows (receivers distributions) are then discounted using GSF (risk free) discount rates so that the provision can be adjust for the **net effect of discounting**.

The provisioning recommendations are then presented to the provisioning committee to review and agree the appropriate level of the provision.

6. METHODOLOGY

Accounting Standards

The accounting issues and financial reporting standards that The Treasury has followed to establish this provision are as follows:

1. Initial recognition and measurement of the fair value of the guarantee at inception (IAS 39.9);
2. Recognition of premium received (IAS 18);
3. Measurement of a provision (NZIAS37:14 & NZIAS 37:36);
4. Triggering (recognition) of a provision (NZIAS37:14); and
5. Disclosures of the Crown's exposure (NZIAS 39, NZIFRS 7);

A detailed note on these was prepared by Ken Warren (i-manage 1247592), which included commentary on application of the financial reporting standards standards to our specific circumstances.