# 51st Annual Report 2010

Australian Defence Credit Union

# The Southern Cross

**The Crux constellation** is the smallest, yet most distinctive, of the 88 modern constellations. Its name is Latin for cross, and it is dominated by a cross-shaped asterism that is commonly known as the **Southern Cross**.

The Southern Cross comprises the red giant Gacrux and orange giant Juxta Crucem as well as three other major stars, which are blue-white in colour, Acrux, Mimosa and Delta Crucis.

Being a circumpolar constellation, Crux is easily visible from the southern hemisphere at practically any time of year. It is also visible near the horizon from tropical latitudes of the northern hemisphere for a few hours every night during the northern winter and spring.

Since the southern sky lacks an easily visible pole star, Acrux and Gacrux are commonly used to mark south. Tracing a line from Gacrux to Acrux and extending it for approximately 4.5 times the distance between the 2 stars leads to a point close to the Southern Celestial Pole.

Beginning in the colonial age, Crux became used as a national symbol by several southern nations. The brightest stars of Crux appear on the flags of Australia, Brazil, New Zealand, Papua New Guinea, and Samoa. They also appear on the flags of the Australian state of Victoria, the Australian Capital Territory and the Northern Territory.

The constellation was also used on the dark blue, shield-like patch worn by personnel of the U.S. Army's Americal Division, which was organized in the Southern Hemisphere, on the island of New Caledonia, and also the blue diamond of the U.S. 1st Marine Division, which fought on the Southern Hemisphere islands of Guadalcanal and New Britain.

As a highly distinctive asterism, Crux has great significance in the cultures of the southern hemisphere.

In Australia, the Southern Cross played a crucial role as symbol of the Eureka Stockade. In the Eureka Oath from Peter Lalor's famous speech in 1854 under the flag he proclaimed:

> *We swear by the Southern Cross to stand truly by each other and fight to defend our rights and liberties.*

In 1893, Australian poet Banjo Paterson wrote:

> *The English flag may flutter and wave,*
> *where the world wide oceans toss,*
> *but the flag the Australian dies to save,*
> *is the flag of the Southern Cross.*

The Southern Cross was written into the lyrics of Advance Australia Fair in 1901, *"Beneath our radiant Southern Cross"*, and the song was adopted as the Australian National Anthem in 1984.

**The Southern Cross inspired the creation of the ADCU logo.**

# Contents

# 2010 Directors' Report

**The Directors present their report on Australian Defence Credit Union Limited (the Credit Union) for the financial year ended 30 June 2010.**

# Corporate governance

This statement outlines the main corporate governance practices in place throughout the financial year.

## Legislative and regulatory requirements

The Credit Union is a company registered under the Corporations Act 2001.

The Credit Union is primarily regulated as:

- an Authorised Deposit Taking Institution by the Australian Prudential Regulatory Authority (APRA) (via Australian Prudential Standards and the Banking Act 1959),
- an Australian Financial Services licence holder by the Australian Securities and Investment Commission (ASIC) (via the Financial Services Regulatory Act 2001 and the Corporations Act 2001),
- a credit provider to consumers, by the Australian Securities and Investment Commission (ASIC), and
- a provider of designated services, by the Australian Transaction Reports and Analysis Centre (AUSTRAC).

The Credit Union's policy on corporate governance, to meet these regulatory requirements and establish best practice, is formulated by the Board of Directors based on the requirements and key principles of the Prudential Standard APS 510 Governance as they apply to the Credit Union.

## Role of the Board

The Board is responsible for the overall corporate governance of the Credit Union including formulating its strategic direction, approving and monitoring the business plan, creating policies, assessing risk, ensuring compliance, establishing and monitoring the achievement of the Credit Union's goals.

The Board has delegated responsibility for the operation and administration of the Credit Union to the Chief Executive Officer (CEO) and the Executive Management team.

## Composition of the Board

The names of the Directors and their qualifications are set out later in the Directors' Report.

The Constitution sets out the size and composition of the Board. The Board comprises seven independent non executive Directors. A Director must retire from office at the start of the third Annual General Meeting after the Director was last elected, and may stand for re-election should he or she re-nominate. The Board may appoint a new Director to fill a casual vacancy and the term of a Director so appointed will end at the start of the next Annual General Meeting.

## Board processes

To assist in the planning and execution of its responsibilities, the Board has established a number of Board Committees. They are the Executive Committee, Renewal Committee, Audit Committee, Risk Committee and Remuneration Committee. These committees have written charters and policies that are reviewed annually along with a range of plans. Through the committees, policies and plans, the Board has established a governance and risk management framework including a system of internal controls, business risk, compliance, financial and regulatory reporting. The significant outcomes of the committees' work are reviewed and endorsed by the full Board. The Board currently holds eleven scheduled meetings a year together with two strategic planning conferences, and approves via email or other correspondence 'out of session' items that require a more immediate response.

Typically a Board meeting would review the monthly and year to date financial results and key performance indicators, make decisions on resolutions and new policies, note progress on projects, discuss CEO and Executive Management's departmental reports and endorse Board Committee reports.

## Executive Committee

The Executive Committee's role is to plan, manage and co-ordinate the agendas and timetables of the Board meetings and strategic planning activities. This committee comprises the Chairman of the Board, the Deputy Chairman and Chief Executive Officer.

## Renewal Committee

The Renewal Committee's role is to maintain the Credit Union's Corporate Governance, Fit and Proper, Board Renewal and Performance Evaluation policies and initiate and conduct the procedures that flow from these policies. The committee comprises at least two Directors. The Chairman of the Renewal Committee is normally a senior Director. The Committee is assisted by the Manager, Human Resources & Premises.

## Audit Committee

The Audit Committee has specific responsibilities relating to policy development, financial accounting and reporting processes, internal and external audit processes, risk management (in conjunction with the Risk Committee), and whistleblower monitoring. The Audit Committee has free and unfettered access to senior management, the Internal Auditor, the External Auditor and the heads of all risk management functions. The committee comprises three Directors, assisted by the Internal Audit Manager.

## Risk Committee

The Risk Committee's role is to formulate the Credit Union's risk appetite and strategy, develop policies and plans to ensure the Credit Union's risk strategy is complied with, and to monitor compliance with those policies. The risk management areas overseen by the Committee include, but are not restricted to, market, liquidity, credit, strategic, funding and operational risk. The committee comprises three Directors assisted by the Head of Finance and Operations, the Head of Credit and the Compliance Manager.

## Remuneration Committee

The Remuneration Committee is responsible for overseeing the establishment and regular review of the Credit Union's Remuneration Policy, including assessment of the effectiveness of the policy. The committee is responsible for making annual recommendations to the Board on remuneration of the CEO, direct reports of the CEO and other persons whose activities may in the Remuneration Committee's opinion affect the financial soundness of ADCU, and any other person specified by APRA.

## Asset & Liability Committee (ALCO)

The ALCO meets at least monthly and has responsibility for managing and reporting credit, liquidity, market and capital risk exposure. It scrutinises operational reports and monitors exposures against limits determined by the Board.

## Operational Risk Management Committee (ORMC)

The ORMC meets at least monthly and is responsible for enabling Executive Management and the Board to implement an effective Operational Risk Management Framework and to ensure that the Board receives regular reporting and updates relating to operational risk management matters, thereby fulfilling the Board's oversight responsibilities in respect to operational risk management. The committee reviews, monitors, interrogates and reports to the Executive and Board on the information contained within the Credit Union's operational risk management system "WORMS" (Web-based Operational Risk Management System), with particular reference to KRI information.

## Strategic planning

The Board and Executive Management meet twice a year (December and May) to plan the strategic direction of the Credit Union by the establishment of long and medium term goals and objectives. The progression of these goals and objectives are reviewed through the course of the plan and are monitored throughout the year to ensure the Credit Union remains on track to deliver the best possible financial offering to our members.

## Ethical standards

All Directors, Managers and Staff are expected to act with the utmost integrity and objectivity, striving at all times to enhance the reputation and performance of the Credit Union.

## Conflicts of interest

The Directors and Executive Management must keep the Board informed of any interest that could potentially conflict with those of the Credit Union and declarations are made at the start of each Board and Board Committee meeting.

## Code of conduct

The Directors are expected to abide by the Credit Union's Code of Conduct as set out in the Corporate Governance Policy.

## Communications with members

Considerable information is available to members and potential members via the Credit Union's website www.adcu.com.au. Additionally, members receive a quarterly newsletter "Communiqué" advising of current activities and promotions, and our Member Contact Centre and all of our branches are there to assist with information and advice.

The Board encourages full participation of members at the Annual General Meeting to ensure a high level of accountability and identification with the Credit Union's strategic direction and performance. The members are requested to vote on Director appointments and aggregate remuneration of Directors as prescribed by the Constitution. Copies of the Constitution can be downloaded from the website, or are available to any member who so requests.

The Annual Report is distributed to all members who have elected to receive this document and posted on our website. The Board ensures that the Annual Report includes all relevant information about the operation of the Credit Union during the financial year, changes in the state of affairs and future developments, in addition to the other disclosures required by the Corporations Act 2001.

Directors (L to R):
Graham Weber; Clinton Thomas; John Wood (Chairman); John Brooks; Jane Spalding; Warren Thomas and Michael Pike.

## Office bearers

The names of Directors and Company Secretaries in office during the financial year were:

### John Wood

**Qualifications**

Fellow of Australian Institute of Company Directors

Fellow of the Australasian Mutuals Institute

Fellow Australian College of Defence and Strategic Studies

**Experience & Responsibilities**

36 years service and experience in Royal Navy and Royal Australian Navy

Consultant to Defence Industry

Member RAN Reserve

Credit Union Director for 13 years and Chairman from 2001

Chairman of Board and Chairman of Board Executive

Member of the Renewal and Remuneration Committee

### John Robert Brooks

**Qualifications**

Bachelor of Arts

Graduate of the Royal Air Force Staff College

Fellow of the Australian College of Defence and Strategic Studies

Member of the Australasian Mutuals Institute

Member of the Australian Institute of Company Directors

Graduate Diploma in Strategic Studies

**Experience & Responsibilities**

28 years with the Royal Australian Air Force (Logistics Branch)

Owner of Brooks Newsagency, Orange, NSW

Credit Union Director for 8 years

Chairman of the Audit Committee

### Michael Morrison Pike

**Qualifications**

Graduate RAN College and RAN Staff College

Graduate Joint Services Staff College

Fellow of the Australian Institute of Management

Fellow Corporate Directors' Association

Associate Fellow of the Australasian Mutuals Institute

Member of the Australian Institute of Company Directors

Graduate Diploma in Management

Graduate Diploma in Strategic Studies

Master of Management Economics (UNSW)

Diploma CD

**Experience & Responsibilities**

28 years service with Royal Australian Navy (Supply Branch)

Active Naval Reservist

Credit Union Director for 17 years

Chairman of the Renewal Committee

Member of the Audit Committee

Member of the Remuneration Committee

### Colonel Jane Maree Spalding

**Qualifications**

Bachelor of Social Science

Master of Arts

Master of Defence Studies

Graduate of the Royal Military College of Science (United Kingdom)

Graduate of the Australian Army Command and Staff College

Graduateship of the City and Guilds of London Institute

Member of the Australasian Mutuals Institute

Member of the Australian Institute of Management

Graduate Member of the Australian Institute of Company Directors

**Experience & Responsibilities**

27 years in the Australian Regular Army

Student, Centre for Defence and Strategic Studies

Credit Union Director for 3 years

Member of the Audit Committee

## Commodore Clinton William Thomas AM, CSC, RAN

**Qualifications**

Graduate RAN College and RAN Staff College

Member of the Australasian Mutuals Institute

Member of the Risk Management Institute of Australasia

Member of the Australian Institute of Project Management

Graduate Member of the Australian Institute of Company Directors

Diploma Applied Science (UNSW)

Diploma CD

Diploma of Government (Contract Management)

Advanced Diploma of Government (Strategic Procurement)

Advanced Diploma of Project Management

Graduate Diploma of Resource Management

Master of Management (Operations and Logistics) (MGSM)

**Experience & Responsibilities**

34 years in the Royal Australian Navy and Defence

Past Member of the Defence Audit Committee (3 years)

Past Chairman of RAN Relief Trust Fund (5 years)

Current Chairman of the RAN Australian Football Association (6 years)

Recently completed 3 years as Director General Supply Chain – Joint Logistics Command

Credit Union Director for 10 years

Chairman of the Risk Committee

## Warren Raymond Thomas

**Qualifications**

Accountancy Certificate

Associate Fellow of the Australasian Mutuals Institute

Graduate Member of the Australian Institute of Company Directors

**Experience & Responsibilities**

37 years in Dept of Defence, including Army service in Vietnam and 20 years in financial management in various Navy and Army Commands

President Cronulla RSL sub-branch

Board member Cronulla RSL Memorial Club

Credit Union Director for 14 years

Deputy Chairman

Chairman of Remuneration Committee

Member of the Executive and Risk Committees

Past Member of the Audit Committee (6 years as Chairman)

## Graham Anthony Weber

**Qualifications**

Member Australian Society of Certified Practising Accountants (CPA)

Bachelor of Commerce in Accounting

Member of the Australasian Mutuals Institute

**Experience & Responsibilities**

5 years in Accounting firms and advisory services

15 years in State and Commonwealth Agencies in Financial Management, Budgeting and performance reporting

Currently Director General – Budgets and Treasury, Defence Materiel Organisation

Credit Union Director since 12 November 2008

Member of the Risk Committee

## Ian Neville Doyle

**Qualifications**

Fellow of the National Institute of Accountants

Fellow of the Financial Services Institute of Australasia

Graduate Management Qualification - AGSM

Management Development Program - Mt. Eliza Australian Management College

Member of the Australasian Mutuals Institute

**Experience & Responsibilities**

Over 30 years experience in the Banking and Finance Industry

Chief Executive Officer

Company Secretary

## Fiorella Spagnolo

**Qualifications**

Bachelor of Commerce (Accountancy & Legal Studies)

Member Australian Society of Certified Practising Accountants (CPA)

Fellow of the Australasian Mutuals Institute

Member of the Risk Management Institution of Australasia

**Experience & Responsibilities**

Over 15 years experience in various senior management roles within the credit union industry

Founding Executive Officer of the Credit Union Financial Support System (CUFSS)

Prudential Supervisor for the NSW Financial Institutions Commissions (now APRA)

Head of Finance & Operations

Company Secretary

## Meetings attended

| | Board meetings | | Board Committee Meetings: Executive | | Audit | | Risk | | Renewal | | Remuneration | | Joint Risk/Audit | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Directors | H | A | H | A | H | A | H | A | H | A | H | A | H | A |
| John Wood | 11 | 10 | 12 | 12 | - | - | - | - | 4 | 4 | 3 | 3 | - | - |
| John Brooks | 11 | 10 | - | - | 6 | 6 | - | - | - | - | - | - | 1 | 1 |
| Michael Pike | 11 | 11 | - | - | 6 | 6 | - | - | 4 | 4 | 3 | 3 | 1 | 1 |
| Jane Spalding | 11 | 10 | - | - | 6 | 5 | - | - | - | - | - | - | 1 | 1 |
| Clinton Thomas | 11 | 11 | - | - | - | - | 7 | 7 | - | - | - | - | 1 | 1 |
| Warren Thomas | 11 | 11 | 12 | 11 | - | - | 7 | 7 | - | - | 3 | 3 | 1 | 1 |
| Graham Weber | 11 | 11 | - | - | - | - | 7 | 7 | - | - | - | - | 1 | 1 |

H: Number of meetings held that the Director was eligible to attend

A: Number of meetings attended

## Director benefits

Directors are required to make an annual declaration of any benefits or interests that may have occurred because of their association with the Credit Union. As at 30 June 2010, no Director has received or become entitled to receive any such benefit.

## Indemnity of Directors and Officers

The Credit Union has paid insurance premiums in respect of Directors' and Officers' liability and legal expense contracts. The Directors have not included details of the nature of the liabilities covered or the amount of the premium paid in respect of Directors' and Officers' liability and legal expense contracts, as such disclosure is prohibited under the insurance contract. No insurance cover has been provided for the benefit of the Credit Union's auditors, BDO Audit (NSW-VIC) Pty Ltd.

## Principal activities

The principal activities of the Credit Union during the year remain unchanged and were the raising of funds authorised by the Prudential Standards administered by APRA and the Banking Act 1959, and the application of those funds in providing financial accommodation to our members in the form of lending, savings, and insurance products.

As a Home Loan Provider under the Defence Home Ownership Assistance Scheme (DHOAS) the Credit Union has continued to experience sound growth in mortgage loans and associated products during 2009/2010.

## Operating and financial review

### Operating results

ADCU earned a total net profit after tax of $5.81m. This compares to $2.25m as at 30 June 2009. This increase in profitability was largely driven by the growth experienced in the preceding financial year 2008/09 as a result of ADCU's inclusion as a Home Loan Provider in DHOAS. The high level of growth has allowed the Credit Union to realise economies of scale. Despite the ongoing influence of the Global Financial Crisis adversely impacting on operating margins, ADCU was able to reduce its Expense to Income ratio to 66.4%.

During the financial year, ADCU continued to grow strongly, with total on and off balance sheet assets increasing by $120m (or 18%) to $786.5m. This growth continued to be predominately sourced from quality growth in the Credit Union's home loan portfolio both from DHOAS and the broader membership.

Throughout 2009/10 demand continued in the Banking & Financial Services market for deposit growth. Despite the competitive pressure, ADCU successfully grew deposits by $54m (or 12%) and this provided a stable base to fund our loan growth.

Non interest income continued to perform, increasing by $375k to $9m. This was mainly attributable to the continuing success in promoting our extensive range of good value insurance products to members, which has helped ADCU meet our commitment to providing products and services to meet all the financial needs of our members.

Over the past year, scale has allowed ADCU to maintain non interest expenses static. It is pleasing to note that the efficiencies associated with our recent growth are now visible and are directly contributing to the growth in our total member's equity.

## Dividends

No dividends have been paid or declared since the end of the financial year and no dividends have been recommended or provided for by the Directors of the Credit Union.

## Significant changes in State of Affairs

During the financial year the Credit Union created the Athena Trust. The Athena Trust is a securitisation vehicle which allows Australian Defence Credit Union to sell mortgage loans into it. The trust is independently administered by Perpetual Trustees in their role as trustee and by Cuscal Management Pty Ltd in their role as Manager. Westpac Banking Corporation Ltd provides a committed funding line to the trust. As part of the sale arrangement for assigned mortgages, the Credit Union is granted a service agreement for which it earns a fee.

## Regulatory snapshot

The largest legislative change for 2010 and 2011 is the implementation of the National Credit Code and National Consumer Credit Protection Act. This is a new national regime that will replace existing State-based Uniform Consumer Credit Codes and will create ASIC as regulator with powers to inspect and enforce requirements for greater consumer protection to ensure responsible lending.

The Board strongly supports the changes to lending and have worked closely with Management to ensure that the changes required for Phase 1 of the Act were completed by 30 June 2010. Additional changes to lending processes are on track to implement the Phase 2 requirements by 31 December 2010.

## Events occurring after balance date

Since the end of the financial year, the Directors have not become aware of any matters or circumstances that may significantly affect the operations or state of affairs of the Credit Union.

## Likely developments and results

No other matter, circumstance or likely development in the operations has arisen since the end of the financial year that has significantly affected or may significantly affect the:

- operations of the Credit Union;
- results of these operations; or
- state of affairs of the Credit Union;

in the financial years subsequent to this financial year.

## Auditors' independence

The auditors have provided the declaration of independence to the Board prescribed by the Corporations Act 2001 as set out on page 10.

## Board resolution

This report is signed in accordance with a formal resolution of the Board of Directors.

**John Wood**
Chairman
23 September 2010

**Warren Thomas**
Deputy Chairman

## Chairman's summary

As another successful financial year comes to an end, I would like to thank all our members for giving us the opportunity to continue working on your behalf to build a strong and sustainable Credit Union. Although the financial environment has remained a challenge for every organisation and the customers they serve, we are truly fortunate to have the ongoing and positive support of our members to help us ensure ADCU remains successful and its members well served.

At ADCU, we are committed to providing quality financial services to members based on the foundations of security and value. Well planned and executed management strategies ensured we maintained sound growth of our deposits and loan portfolio which delivered significant benefits of efficiency and scale which, in turn, contributed to a healthy increase in our revenue base. Whilst revenue grew, we prudently controlled our costs while, at the same time, we continued to reinvest in new services, competitive rates and added benefits to members. A completely reworked Visa product featuring some of the best rates in the market, a more convenient card activation process and a free Account Sweeping service were some of the ways ADCU invested its profits back into the organisation. This reinvestment of profits for the benefit of our members will continue to be the Credit Union's focus as we hold true to the industry slogan that "It all comes back to our members".

I would also like to take this opportunity to thank my fellow Directors, our Management team and all staff members. During a year of ongoing change and fluctuating market conditions, they have continued to meet their commitments and responsibilities in a highly professional manner and have delivered an excellent result for the Credit Union in a time of general uncertainty for the financial services industry.

**John Wood**
Chairman
23 September 2010

## Declaration of independence by Neville Sinclair to the Directors of Australian Defence Credit Union Limited

As lead auditor of Australian Defence Credit Union Limited for the year ended 30 June 2010, I declare that to the best of my knowledge and belief, there have been no contraventions of;

(i) the auditor independence requirements of the Corporations Act 2001 in relation to the audit, and

(ii) any applicable code of professional conduct in relation to the audit.

**Neville Sinclair**
Director, BDO Audit (NSW-VIC) Pty Ltd.
21 September 2010

## Directors' declaration

The Directors of Australian Defence Credit Union Limited declare that:

The financial statements comprising Balance Sheet, Income Statement, Statement of Changes in Equity, Statement of Cash Flows, accompanying notes and notes related thereto, are in accordance with the Corporations Act 2001, and:

(a) comply with Accounting Standards; and

(b) give a true and fair view of the financial position of the Credit Union as at 30 June 2010 and performance for the year ended on that date.

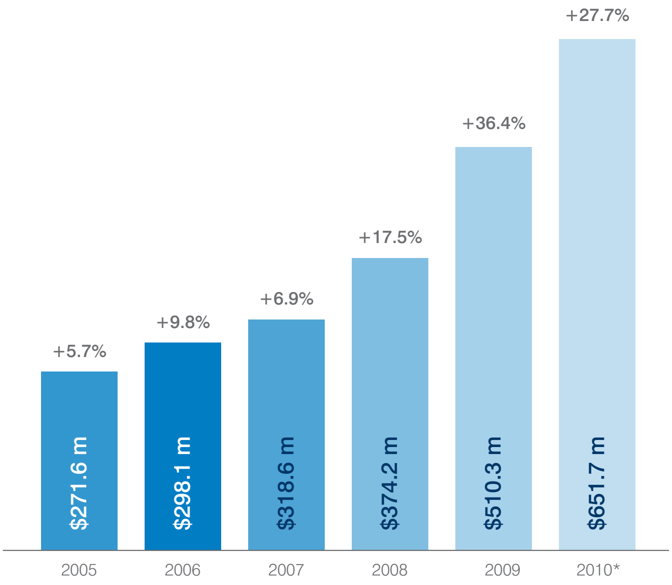
The company has included in the notes to the financial statements an explicit and unreserved statement of compliance with International Financial Reporting Standards.

In the Directors' opinion there are reasonable grounds to believe that the Credit Union will be able to pay its debts as and when they become due and payable.

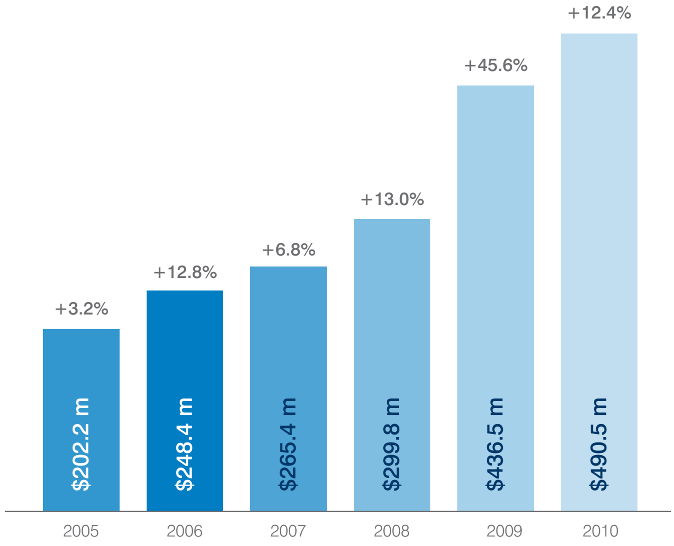
This declaration is made in accordance with a resolution of the Board of Directors.

**John Wood**
Chairman
23 September 2010

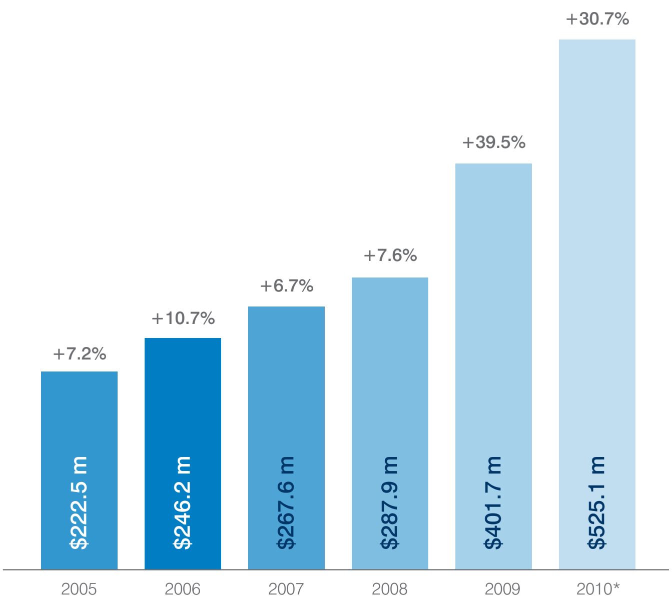
## Key Performance Measures



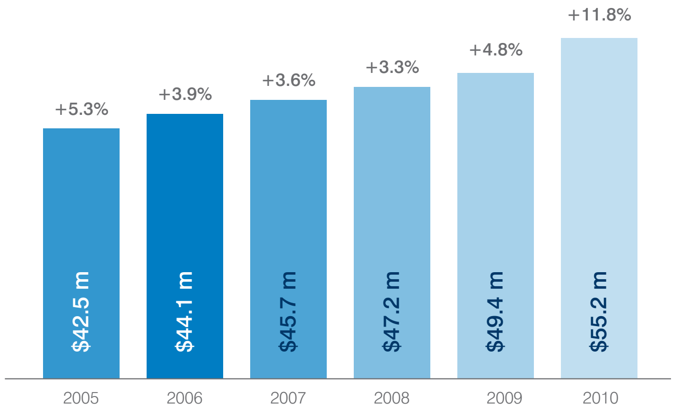

Balance Sheet Assets




Deposits




Net Balance Sheet Loans




Members Equity

* Includes $56,366,795 in loans securitised through Athena Trust

# 2010 Chief Executive's Report

Ian Doyle, CEO

**Despite the uncertainty and upheaval that continued in the financial industry throughout the year, ADCU again proved its resilience and core strength by delivering another year of strong performance.**

This achievement was not the result of any single person, product or strategy, but rather the culmination of all our dedicated staff delivering "many things done well" across the organisation in order to meet the needs of our members and serve the broader Defence community.

Over the past twelve months the Credit Union developed a combination of well balanced and well executed strategies to further augment our highly competitive product range and fulfil our commitment to providing financial services to members throughout their lives. These strategies spanned all areas of our organisation, including new product development, business processes, policies, human resources and technology, in order to strengthen the internal and external workings of the Credit Union and ultimately deliver the best service possible to our members.

Managing the Credit Union to this level of performance through this prolonged period of volatility continued to require significant operational focus from the Board and Management; however, we have continued to invest soundly and strategically to ensure sustainable growth in our business and earnings not only for the present, but for the medium-to-long term as well.

Some important steps that we have taken in support of the above over the past twelve months include:

## New products and services

A range of new products and services was introduced to members throughout the year to help them better manage their finances during these uncertain economic times. We completely rebuilt our credit card product and relaunched the *ADCU Low Rate Visa Card*, one of the most competitive products in the market today. With its low cost features and uniquely Defence design, members agreed it's the right product to help them save money through strong take-up of the new card.


Several other new services were rolled out including redesigned Member Statements providing easier to read and simpler account information and a new, more convenient Card Activation process offering members the option to activate their new credit or debit cards online or over the phone. We introduced EMV Chip technology to our new and reissued Credit and Debit Cards to increase card security for our members and launched the Account Sweeping feature which helps members manage the movement of their funds across multiple accounts.

## Our people and processes

At ADCU we recognise that our staff are our greatest asset in the way we do business and how we can best serve our members. We are committed to providing a work environment and culture that allows them to thrive by recognising their individual talents and skills and by fostering a team spirit supported by a strong commitment to training.

Much of this year's success came from behind-the-scenes projects aimed at better engaging staff, increasing efficiency and providing a challenging and rewarding environment where our employees can make a difference. In the past year we launched the *Knowledge Centre*, a new online system to help the organisation manage information and procedures, the *Electronic Learning Management System* (ELMS), an online training and development system as well as a new Debt Management module to alleviate time consuming administrative duties around the management of overdue accounts.

These new tools are making it easier and quicker for staff across the country to access the information they need and complete the necessary training so they can spend more time focussing on serving members and adding value in more meaningful ways.

## Prudential standards and regulation

As an Authorised Deposit Taking Institution (ADI), ADCU continues to operate under strict regulations and monitoring imposed by the Australian Securities & Investments Commission (ASIC) and the Australian Prudential Regulatory Authority (APRA). ADCU strictly adheres to these prudential requirements and regulations.

We also operate under, and comply with, the following:

- Mutual Banking Code of Practice, which came into effect on 1 July 2009 which addresses the fair and ethical treatment of all our members and transparency in our dealings with members, whilst focusing on high customer service standards.

- National Privacy Principles, which ensures protection of member's privacy.
- Trade Practices Act 1974, which ensures safeguards for consumer rights, together with fair and ethical trading.
- Uniform Consumer Credit Code (UCCC) legislation, that regulates credit provided to personal borrowers. This was replaced by the new National Credit Act from 1 July 2010.
- Financial Services Reform Act 2001, which regulates the provision of financial services and conduct in relation to financial products.
- Anti-Money Laundering and Counter-Terrorism Financing Act 2006, which is aimed at preventing and detecting money laundering and terrorism financing and imposes requirements relating to customer identification, due diligence and maintenance of an AML/CTF Program.

High priority is given to compliance and corporate governance within the Credit Union and compliance with our policies and procedures is continually under review by our internal and external audit process. We have reinforced our compliance focus and process with the introduction of a sophisticated online compliance framework and reporting system to ensure we maintain the highest level of corporate governance.

## Financial education

A career in the ADF offers members an opportunity to save for the future, provided goals are put in place early. To this end, ADCU continued to run a host of financial education initiatives for our members to help them grow their personal wealth and create financial stability. Education topics have included Budgeting, Pre-deployment Planning, Buying a Motor Vehicle, Understanding Credit, as well as many others, and will continue to be a priority as the need for good financial management only continues to grow.

## Supporting our communities

As we've done throughout our 51 year history, ADCU played an active role in Defence life across Australia over the past year. ADCU supported a wide range of activities and organisations through sponsorships, donations and spirited participation at events from Rockingham to Enoggera and at virtually every base in between. As with previous years, we worked with the national and many state Returned & Services Leagues to show our support and help further their cause including raising funds through ANZAC Badge sales.




We are extremely proud of our mutual structure and the benefits it provides to our members in the form of competitive interest rates, fairer fees, great products, services and our Relationship Reward. Our mutuality is a strength that differentiates us from the big banks and enables us to give back to our members. As a keen supporter of the Credit Union movement, we were proud to be an active participant in the first awareness-building campaign created by Abacus on behalf of the industry and will continue to do so as the campaign takes hold.

Finally, I would like to thank you, our members, and our Board of Directors for your on-going support this year and for the years ahead.

**Ian Doyle**
Chief Executive Officer
23 September 2010

1. (L to R): Andrew Moebus, Regional Manager Hume, Derek Robson (AM), RSL National Secretary, Rear Admiral Ken Doolan (AO (retired)), RSL National President
2. (L to R): Andrew Moebus, Regional Manager Hume, Mickey Michaelis, Treasurer RSL ACT & RSL National Project Officer
3. (L to R): Annette Mulliner, Asst State Secretary & Financial Control Manager RSL NSW, Don Rowe, State President RSL NSW, Ann Roach, Regional Manager Inner Sydney, Chris Perrin, State Secretary RSL NSW
4. (L to R): Nola Edwards, Regional Manager WA, Bill Gaynor (OAN RFD), State President RSL WA, Saxon Norgard, Christ Church Grammar School, Conrad Scott, Cadet Coordinator

Executive Team (L to R):
Fiorella Spagnolo, Head of Finance and Operations; Ian Doyle, Chief Executive Officer; Bob McGregor, Head of Credit; Sloan Dinning, Marketing Manager; Mike Lanzing, Head of Business Development.


# 2010 Independent Auditor's Report

To the members of Australian Defence Credit Union Limited

## Report on the complete set of financial statements

We have audited the accompanying complete set of financial statements of Australian Defence Credit Union Limited, which comprises the statement of financial position as at 30 June 2010, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year ended on that date, a summary of significant accounting policies, other explanatory notes and the directors' declaration for consolidated entity comprising the company and the entities it controlled at the year's end or from time to time during the financial year.

## Directors' responsibility for the complete set of financial statements

The directors of the Credit Union are responsible for the preparation and fair presentation of the complete set of financial statements in accordance with Australian Accounting Standards (including the Australian Accounting Interpretations) and the *Corporations Act 2001*. This responsibility includes establishing and maintaining internal controls relevant to the preparation and fair presentation of the complete set of financial statements that is free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances. In Note 1, the directors also state, in accordance with Accounting Standard AASB 101 *Presentation of Financial Statements*, that compliance with the Australian equivalents to International Financial Reporting Standards ensures that the complete set of financial statements, comprising the financial statements and notes, complies with International Financial Reporting Standards.

## Auditor's responsibility

Our responsibility is to express an opinion on the complete set of financial statements based on our audit. We conducted our audit in accordance with Australian Auditing Standards. These Auditing Standards require that we comply with relevant ethical requirements relating to audit engagements and plan and perform the audit to obtain reasonable assurance whether the complete set of financial statements is free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the complete set of financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the complete set of financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the complete set of financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the complete set of financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

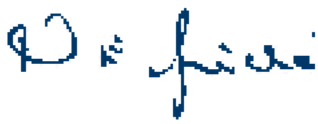
## Independence

In conducting our audit, we have complied with the independence requirements of the *Corporations Act 2001*. We confirm that the independence declaration required by the *Corporations Act 2001* provided to the directors of Australian Defence Credit Union Limited, would be in the same terms if provided to the directors at the time that this auditor's report was made.

## Auditor's opinion

In our opinion

a. the complete set of financial statements of Australian Defence Credit Union Limited is in accordance with the *Corporations Act 2001*, including:
   i. giving a true and fair view of the company's and consolidated entity's financial position as at 30 June 2010 and of its performance for the year ended on that date; and
   ii. complying with Australian Accounting Standards (including the Australian Accounting Interpretations) and the *Corporations Regulations 2001*: and
b. the complete set of financial statements also complies with International Financial Reporting Standards as disclosed in Note 1.



**Neville Sinclair**
Director, BDO Audit (NSW-VIC) Pty Ltd.
24 September 2010

## Statement of Comprehensive Income for the year ended 30 June 2010

| | Note | 2010 $ | 2009 $ |
|---|---|---|---|
| Interest revenue | 2.a | 43,320,731 | 41,208,555 |
| Interest expense | 2.c | 20,640,219 | 22,873,464 |
| **Net interest income** | | 22,680,512 | 18,335,091 |
| Fee commission and other income | 2.b | 9,009,790 | 8,635,885 |
| | | 31,690,302 | 26,970,976 |
| Less | | | |
| **Non interest expenses** | | | |
| Impairment losses on loans receivable from members | 2.d | 1,561,586 | 1,693,716 |
| Fee and commission expenses | | 2,387,702 | 2,822,478 |
| General administration | | | |
| - Employees compensation and benefits | | 10,597,621 | 10,778,966 |
| - Depreciation and amortisation | 2.e | 788,732 | 850,325 |
| - Information technology | | 1,898,402 | 1,702,322 |
| - Office occupancy | 2.f | 856,933 | 844,764 |
| - Other administration | | 2,605,989 | 2,607,806 |
| Other operating expenses | | 2,735,438 | 2,662,372 |
| Total non interest expenses | | 23,432,403 | 23,962,749 |
| **Profit before income tax** | | 8,257,899 | 3,008,227 |
| Income tax expense | 3 | 2,446,275 | 758,607 |
| **Profit after income tax** | | **5,811,624** | **2,249,620** |

## Statement of Changes In Member Equity for the year ended 30 June 2010

| | Capital Reserve $ | Reserve for Credit Losses $ | Retained Earnings $ | Total $ |
|---|---|---|---|---|
| Total as at 1 July 2008 | **79,110** | **1,060,545** | **46,032,859** | **47,172,514** |
| Profit for the year | – | – | 2,249,620 | 2,249,620 |
| Transfer to reserve for credit losses in the year | – | – | – | – |
| Transfer to capital account on redemption of shares | 6,176 | – | (6,176) | – |
| **Total as at 30 June 2009** | **85,286** | **1,060,545** | **48,276,303** | **49,422,134** |
| Profit for the year | – | – | 5,811,624 | 5,811,624 |
| **Transfers to (from) reserves** | | | | |
| Transfer to reserve for credit losses in the year | – | – | – | – |
| Transfer to capital account on redemption of shares | 5,982 | – | (5,982) | – |
| **Total as at 30 June 2010** | **91,268** | **1,060,545** | **54,081,945** | **55,233,758** |

# Statement of Financial Position as at 30 June 2010

| | Note | 2010 $ | 2009 $ |
|---|---|---|---|
| **Assets** | | | |
| Cash | 4 | 13,520,374 | 1,064,624 |
| Receivables from financial institutions | 5 | 107,500,000 | 101,500,000 |
| Receivables | 6 | 2,331,429 | 2,600,071 |
| Loans to members | 7.a | 525,122,557 | 401,732,045 |
| Available for sale investments | 9 | 907,154 | 907,154 |
| Property, plant and equipment | 10 | 694,205 | 895,702 |
| Taxation assets | 11 | 848,110 | 771,222 |
| Intangible assets | 12 | 809,163 | 847,643 |
| **Total assets** | | 651,732,992 | 510,318,461 |
| **Liabilities** | | | |
| Short term borrowings | 13 | 96,366,795 | 16,912,377 |
| Deposits from members | 14 | 490,496,935 | 436,465,871 |
| Creditor accruals and settlement accounts | 15 | 7,283,645 | 6,861,597 |
| Taxation liabilities | 16 | 1,957,145 | 199,395 |
| Provisions | 17 | 394,714 | 457,087 |
| **Total liabilities** | | 596,499,234 | 460,896,327 |
| **Net assets** | | **55,233,758** | **49,422,134** |
| **Members' equity** | | | |
| Capital reserve account | 18 | 91,268 | 85,286 |
| General reserve for credit losses | 19 | 1,060,545 | 1,060,545 |
| Retained earnings | | 54,081,945 | 48,276,303 |
| **Total members' equity** | | **55,233,758** | **49,422,134** |

Table of other notes to accounts

# Statement of Cash Flows for the year ended 30 June 2010

| | Note | 2010 $ | 2009 $ |
|---|---|---|---|
| **Operating activities** | | | |
| **Revenue inflows** | | | |
| Interest received | | 42,493,022 | 41,709,166 |
| Fees and commissions | | 8,413,036 | 7,391,196 |
| Dividends | | 113,373 | 561,696 |
| Other income | | 440,310 | 595,081 |
| **Revenue outflows** | | | |
| Interest paid | | (20,738,286) | (22,000,586) |
| Suppliers and employees | | (21,013,509) | (21,457,822) |
| Income taxes paid | | (765,413) | (581,866) |
| Net cash from revenue activities | 32.b | 8,942,533 | 6,216,865 |
| **Inflows (outflows) from other operating activities** | | | |
| Increase in member loans (net movement) | | (125,050,198) | (115,493,523) |
| Increase in member deposits and shares (net movement) | | 55,653,542 | 134,897,412 |
| Increase in deposits to other financial institutions (net) | | (6,000,000) | (32,000,000) |
| **Net cash from operating activities** | | **(66,454,123)** | **(6,379,246)** |
| **Investing activities** | | | |
| **Inflows** | | | |
| Proceeds on sale of investments in shares | | – | – |
| Proceeds on sale of property, plant and equipment | | 5,578 | 144,000 |
| **Less: Outflows** | | | |
| Purchase of investments in shares | | – | (156) |
| Purchase of property plant and equipment | | (279,339) | (289,863) |
| Purchase of intangible assets | | (270,784) | (193,505) |
| **Net cash from investing activities** | | **(544,545)** | **(339,524)** |
| **Financing activities** | | | |
| **Inflows (outflows)** | | | |
| Increase in borrowings (net movement) | | 81,279,795 | (913,000) |
| **Net cash from financing activities** | | **81,279,795** | **(913,000)** |
| Total net cash increase/(decrease) | | 14,281,127 | (7,631,770) |
| Cash at beginning of year | | (760,753) | 6,871,017 |
| **Cash at end of year** | 32.a | **13,520,374** | **(760,753)** |

# 1. Statement of Accounting Policies

This financial report is prepared for Australian Defence Credit Union Limited as a group comprising the Credit Union and the Athena Trust, an entity deemed under the Accounting Standards to be controlled by the Credit Union, for the year ended the 30th June 2010. The report was authorised for issue on 23rd September 2010 in accordance with a resolution of the Board of Directors. The financial report is presented in Australian dollars. The financial report is a general purpose financial report which has been prepared in accordance with Australian equivalents to International Financial Reporting Standards (AIFRS), other authoritative pronouncements of the Australian Accounting Standards Board, Urgent Issues Group Interpretations and the Corporations Act 2001. Compliance with Australian equivalents to International Financial Reporting Standards (AIFRS) ensures the financial statements and notes comply with the International Financial Reporting Standards (IFRS).

## a. Basis of measurement

The financial statements have been prepared on an accruals basis, and are based on historical costs, which do not take into account changing money values or current values of non current assets [except for real property and available for sale investments which are stated at fair value]. The accounting policies are consistent with the prior year unless otherwise stated.

## b. Loan to members

### (i) Basis of recognition

All loans are initially recognised at fair value, net of loan origination fees and inclusive of transaction costs incurred. Loans are subsequently measured at amortised cost. Any difference between the proceeds and the redemption amount is recognised in the income statement over the period of the loans using the effective interest method.

Loans to members are reported at their recoverable amount representing the aggregate amount of principal and unpaid interest owing to the Credit Union at balance date, less any allowance or provision against impairment for debts considered doubtful. A loan is classified as impaired where recovery of the debt is considered unlikely as determined by the Board of Directors.

### (ii) Interest earned

**Term loans** – interest is calculated on the basis of the daily balance outstanding and is charged in arrears to a member's account on the last day of each month.

**Overdraft** – interest is calculated initially on the basis of the daily balance outstanding and is charged in arrears to a member's account on the last day of each month.

**Credit cards** – interest is calculated initially on the basis of the daily balance outstanding and is charged in arrears to a member's account each month, on cash advances and purchases in excess of the payment due date. Purchases are granted up to 55 days interest free until the due date for payment.

**Non accrual loan interest** – whilst still legally recoverable, interest is not brought to account as income where the Credit Union is informed that the member has deceased, or, where a loan is impaired.

### (iii) Loan origination fees and discounts

Loan establishment fees and discounts are initially deferred as part of the loan balance, and are brought to account as income over the expected life of the loan as interest revenue.

### (iv) Transaction costs

Transaction costs are expenses which are direct and incremental to the establishment of the loan. These costs are initially deferred as part of the loan balance, and are brought to account as a reduction to income over the expected life of the loan, and included as part of interest revenue.

### (v) Fees on loans

The fees charged on loans after origination of the loan are recognised as income when the service is provided or costs are incurred.

### (vi) Net gains and losses

Net gains and losses on loans to members to the extent that they arise from the partial transfer of business or on securitisation, do not include impairment write downs or reversals of impairment write downs.

## c. Loan impairment

### (i) Specific and collective provision for impairment

A provision for losses on impaired loans is recognised when there is objective evidence that the impairment of a loan has occurred. Estimated impairment losses are calculated on either a portfolio basis for loans of similar characteristics, or on an individual basis. The amount provided is determined by management and the Board to recognise the probability of loan amounts not being collected in accordance with terms of the loan agreement. The critical assumptions used in the calculation are as set out in Note 8. Note 20 details the credit risk management approach for loans.

The APRA Prudential Standards require a minimum provision to be maintained, based on specific percentages on the loan balance which are contingent upon the length of time the repayments are in arrears. This approach is used to assess the collective provisions for impairment.

An assessment is made at each balance sheet date to determine whether there is objective evidence that a specific financial asset or a group of financial assets is impaired. Evidence of impairment may include indications that the borrower has defaulted, is experiencing significant financial difficulty, or where the debt has been restructured to reduce the burden to the borrower.

### (ii) Reserve for credit losses

In addition to the above specific provision, the Board has recognised the need to make an allocation from retained earnings to ensure there is adequate protection for members against the prospect that some members will experience loan repayment difficulties in the future. The reserve is based on estimation of potential risk in the loan portfolio based upon:

- the level of security taken as collateral; and
- the concentration of loans taken by employment type.

### (iii) Renegotiated loans

Loans which are subject to renegotiated terms which would have otherwise been impaired do not have the repayment arrears diminished and interest continues to accrue to income. Each renegotiated loan is retained at the full arrears position until the normal repayments are reinstated and brought up to date and maintained for a period of 6 months.

## d. Bad debts written off (direct reduction in loan balance)

Bad debts are written off from time to time as determined by management and the Board of Directors when it is reasonable to expect that the recovery of the debt is unlikely. Bad debts are written off against the provisions for impairment, if a provision for impairment had previously been recognised. If no provision had been recognised, the write-offs are recognised as expenses in the income statement.

## e. Property, plant and equipment

Property, plant and equipment are depreciated on a straight line basis so as to write off the net cost of each asset over its expected useful life to the Credit Union. The useful lives are adjusted if appropriate at each reporting date. Estimated useful lives as at the balance date are as follows:

- Leasehold improvements - 10 years.
- Plant and equipment - 3 to 7 years.
- Assets less than $300 are not capitalised.

## f. Receivables from other financial institutions

Term deposits with other financial institutions are unsecured and have a carrying amount equal to their principal amount. However, the Government Guarantee protects the first $1 million deposited with each Financial Institution. Interest is paid on the daily balance at maturity. All deposits are in Australian currency.

The accrual for interest receivable is calculated on a proportional basis of the expired period of the term of the investment. Interest receivable is included in the amount of receivables in the balance sheet.

## g. Equity investments and other securities

Investments in shares are classified as available for sale financial assets where they do not qualify for classification as loans and receivables, or investments held for trading.

Investments in shares which do not have a ready market and are not capable of being reliably valued are recorded at the lower of cost or recoverable amount.

Realised net gains/losses on available for sale financial assets taken to the profit and loss account comprise gains/losses on disposal only.

All investments are in Australian currency.

## h. Member deposits

### (i) Basis for measurement

Member savings and term investments are quoted at the aggregate amount of money owing to depositors.

### (ii) Interest payable

Interest on savings is calculated either on the daily balance and posted to the accounts periodically, or on maturity of the term deposit. Interest on savings is brought to account on an accrual basis in accordance with the interest rate terms and conditions of each savings and term deposit account as varied from time to time. The amount of the accrual is shown as part of amounts payable.

## i. Borrowings

All borrowings are initially recognised at fair value, net of transaction costs incurred. Borrowings are subsequently measured at amortised cost. Any difference between the proceeds (net of transaction costs) and the redemption amount is recognised in the income statement over the period of the loans and borrowings using the effective interest method.

## j. Provision for employee benefits

Provision is made for the Credit Union's liability for employee benefits arising from services rendered by employees to balance date. Employee benefits expected to be settled within one year, have been measured at their nominal amount.

Other employee benefits payable later than one year have been measured at the present value of the estimated future cash outflows to be made for those benefits discounted using national government bond rates.

Provision for long service leave is on a pro-rata basis from commencement of employment with the Credit Union based on the present value of its estimated future cash flows.

Annual leave is accrued in respect of all employees on pro-rata entitlement for part years of service and leave entitlement due but not taken at balance date. Annual leave is reflected as part of the sundry creditors and accruals.

Contributions are made by the Credit Union to an employee's superannuation fund and are charged to the income statement as incurred.

## k. Leasehold on premises

Leases where the lessor retains substantially all the risks and rewards of ownership of the net asset are classified as operating leases. Payments made under operating leases (net of incentives received from the lessor) are charged to the income statement on a straight-line basis over the period of the lease.

## l. Income tax

The income tax expense shown in the income statement is based on the profit before income tax adjusted for any non tax deductible, or non assessable items between accounting profit and taxable income. Deferred tax assets and liabilities are recognised using the balance sheet liability method in respect of temporary differences arising between the tax bases of assets or liabilities and their carrying amounts in the financial statements. Current and deferred tax balances relating to amounts recognised directly in equity are also recognised directly in equity.

Deferred tax assets and liabilities are recognised for all temporary differences between carrying amounts of assets and liabilities for financial reporting purposes and their respective tax bases at the rate of income tax applicable to the period in which the benefit will be received or the liability will become payable. These differences are presently assessed at 30%.

Deferred tax assets are only brought to account if it is probable that future taxable amounts will be available to utilise those temporary differences. The recognition of these benefits is based on the assumption that no adverse change will occur in income tax legislation; and the anticipation that the Credit Union will derive sufficient future assessable income and comply with the conditions of deductibility imposed by the law to permit an income tax benefit to be obtained.

## m. Intangible assets

Items of computer software which are not integral to the computer hardware owned by the Credit Union are classified as intangible assets.

Computer software is amortised over the expected useful life of the software. These lives range from 2 to 5 years.

## n. Goods and Services Tax

As a financial institution the Credit Union is input taxed on all income except for income from commissions and some fees. An input taxed supply is not subject to Goods and Services Tax (GST) collection, and similarly the GST paid on related or apportioned purchases cannot be recovered. As some income is charged GST, the GST on purchases are generally recovered on a proportionate basis. In addition certain prescribed purchases are subject to reduced input tax credits (RITC), of which 75% of the GST paid is recoverable.

Revenue, expenses and assets are recognised net of the amount of GST. To the extent that the full amount of the GST incurred is not recoverable from the Australian Tax Office (ATO), the GST is recognised as part of the cost of acquisition of the asset or as part of an item of the expense.

Receivables and payables are stated with the amount of GST included where applicable GST is collected. The net amount of GST recoverable from, or payable to, the ATO is included as a current asset or current liability in the balance sheet. Cash flows are included in the cash flow statement on a gross basis. The GST components of cash flows arising from investing and financing activities which are recoverable from, or payable to, the ATO are classified as operating cash flows.

## o. Impairment of assets

At each reporting date the Credit Union assesses whether there is any indication that individual assets are impaired. Where impairment indicators exist, recoverable amount is determined and impairment losses are recognised in the income statement where the asset's carrying value exceeds its recoverable amount. Recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purpose of assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. Where it is not possible to estimate recoverable amount for an individual asset, recoverable amount is determined for the cash-generating unit to which the asset belongs.

## p. Accounting estimates and judgements

Management have made critical accounting estimates when applying the Credit Union's accounting policies with respect to the impairment provisions for loans - refer Note 8.

## q. New or emerging standards

Certain new accounting standards and interpretations have been published that are not mandatory for 30 June 2010 reporting periods. The company's assessment of the impact of these new standards and interpretations is set out in the table below.

| AASB reference | Nature of change | Application date | Impact on initial application |
|---|---|---|---|
| AASB 9<br>Issued DEC 2009<br>Financial Instruments | Amends the requirements for classification and measurement of financial assets. | Periods beginning on or after 1 January 2013. | Due to the recent release of these amendments and that adoption is only mandatory for the 30 June 2014 year end, the entity has not yet made an assessment of the impact of these amendments. |

## 2. Income statement

| | 2010 $ | 2009 $ |
|---|---|---|
| **a. Analysis of interest revenue** | | |
| **Interest revenue on assets carried at amortised cost** | | |
| Cash – deposits at call | 240,892 | 535,634 |
| Receivables from financial institutions | 5,262,596 | 5,731,605 |
| Loans to members | 37,817,243 | 34,941,316 |
| **Total interest revenue** | **43,320,731** | **41,208,555** |
| **b. Fee, commission and other income** | | |
| **Fee and commission revenue** | | |
| Fee income on loans – other than loan origination fees | 1,763,215 | 2,030,398 |
| Other fee income | 4,545,564 | 3,935,796 |
| Insurance commissions | 1,479,132 | 856,590 |
| Other commissions | 625,125 | 601,041 |
| **Total fee and commission revenue** | **8,413,036** | **7,423,825** |
| **Other income** | | |
| Dividends received on available for sale assets | 113,373 | 561,696 |
| Bad debts recovered | 478,677 | 475,866 |
| Gain on disposal of assets | | |
| – Property, plant and equipment | 4,212 | 142,482 |
| – Intangibles | – | – |
| Miscellaneous revenue | 492 | 32,017 |
| **Total fee commission and other income** | **9,009,790** | **8,635,885** |
| **c. Interest expenses** | | |
| **Interest expense on liabilities carried at amortised cost** | | |
| Short term borrowings | 2,533,516 | 2,281,777 |
| Deposits from financial institutions | – | – |
| Deposits from members | 18,106,703 | 20,591,687 |
| **Total interest expense** | **20,640,219** | **22,873,464** |
| **d. Impairment losses** | | |
| **Loans and advances** | | |
| Increase in provision for impairment | 44,660 | 158,806 |
| Bad debts written off directly against profit | 1,516,926 | 1,534,910 |
| **Total impairment losses** | **1,561,586** | **1,693,716** |
| **e. Other prescribed disclosures** | | |
| General administration – depreciation expense includes: | | |
| – plant and equipment | 306,363 | 386,175 |
| – leasehold improvements | 173,107 | 163,693 |
| – amortisation of software | 309,262 | 300,457 |
| | **788,732** | **850,325** |

| | 2010 $ | 2009 $ |
|---|---|---|

### f. General administration – office occupancy costs include:

| | | |
|---|---|---|
| Property operating lease payments | **856,933** | **844,764** |

### g. Other operating expenses include:

| | | |
|---|---|---|
| Auditor's remuneration (excluding GST) | | |
| – Audit fees | 98,100 | 98,100 |
| – Other services – taxation | 4,800 | 4,500 |
| – Other services – compliance | 3,000 | 3,000 |
| – Other services – other | 10,000 | 5,000 |
| | **115,900** | **110,600** |
| Loss on disposal of assets | | |
| – property, plant and equipment | – | – |
| | – | – |

## 3. Income tax expense

The prima facie tax payable on profit is reconciled to the income tax expense in the accounts as follows:

| | | |
|---|---|---|
| **Profit** | **8,257,899** | **3,008,227** |
| Prima facie tax payable on profit before income tax at 30% | 2,477,370 | 902,468 |
| Add tax effect of expenses not deductible | 15,862 | 13,547 |
| Less | | |
| – Investment allowance | 3,206 | – |
| – Franking rebate | 34,012 | 168,509 |
| – Over provision in prior year | 9,739 | (11,101) |
| **Total income tax expense in income statement** | **2,446,275** | **758,607** |

## 4. Cash

| | | |
|---|---|---|
| Cash on hand | 1,077,497 | 1,064,624 |
| Deposits at call | 12,442,877 | – |
| | **13,520,374** | **1,064,624** |

## 5. Receivables from financial institutions

| | | |
|---|---|---|
| Deposits with industry bodies - Cuscal (refer Note 29) | 36,000,000 | 54,500,000 |
| Deposits with other societies | – | – |
| Deposits with banks | 71,500,000 | 47,000,000 |
| | **107,500,000** | **101,500,000** |

| | 2010 $ | 2009 $ |
|---|---|---|

## 6. Receivables

| | | |
|---|---|---|
| Interest receivable on deposits with other financial institutions | 1,356,856 | 417,318 |
| Prepayments | 257,616 | 390,965 |
| GST Receivable | – | – |
| Sundry debtors and settlement accounts | 716,957 | 1,791,788 |
| | **2,331,429** | **2,600,071** |

## 7. Loans to members

### a. Amount due comprises:

| | | |
|---|---|---|
| Overdrafts and revolving credit | 25,867,710 | 22,302,659 |
| Term loans | 444,099,653 | 380,484,498 |
| Term loans held by the Athena Trust | 56,366,795 | – |
| **Subtotal** | 526,334,158 | 402,787,157 |
| Less: | | |
| Unamortised loan origination fees | 293,821 | 181,992 |
| Unearned Income | – | – |
| **Subtotal** | 526,040,337 | 402,605,165 |
| Less: | | |
| Provision for impaired loans (Note 8) | 917,780 | 873,120 |
| | **525,122,557** | **401,732,045** |

### b. Credit quality – security held against loans

| | | |
|---|---|---|
| Secured by mortgage over real estate held in Athena trust | 56,366,795 | – |
| Secured by mortgage over real estate | 316,461,676 | 258,530,326 |
| Partly secured by goods mortgage | 96,491,453 | 96,779,555 |
| Wholly unsecured | 57,014,234 | 47,477,276 |
| | **526,334,158** | **402,787,157** |

It is not practicable to value all collateral as at the balance date due to the variety of assets and condition. A breakdown of the quality of the residential mortgage security on a portfolio basis is as follows:

| | | |
|---|---|---|
| Security held as mortgage against real estate is on the basis of: | | |
| – loan to valuation ratio of less than 80% | 191,624,027 | 155,383,866 |
| – loan to valuation ratio of more than 80% but mortgage insured | 108,678,645 | 87,124,511 |
| – loan to valuation ratio of more than 80% and not mortgage insured | 16,159,004 | 16,021,949 |
| **Total** | **316,461,676** | **258,530,326** |

Where the loan value is less than 80% there is a 20% margin to cover the costs of any sale, or potential value reduction.

| | 2010 $ | 2009 $ |
|---|---|---|

## c. Concentration of loans

The values discussed below include on balance sheet values and off balance sheet undrawn facilities as described in Note 25.

| | 2010 $ | 2009 $ |
|---|---|---|
| (i) Loans to individual or related groups of members which exceed 10% of reserves in aggregate | – | – |
| **Total** | – | – |

(ii) Loans to members are concentrated to individuals employed in the Australian Defence industry.

(iii) Geographical concentrations

Loans have been made to individuals in the Defence Forces throughout Australia. There are no concentrations of borrowers in any state or region.

(iv) Loans by purpose

| | 2010 $ | 2009 $ |
|---|---|---|
| **Loans to natural persons** | | |
| Residential loans and facilities | 316,381,401 | 256,370,057 |
| Personal loans and facilities | 152,870,037 | 145,776,354 |
| Business loans and facilities | 715,925 | 640,746 |
| Loans held by the Athena Trust | 56,366,795 | – |
| | **526,334,158** | **402,787,157** |
| **Loans to corporations** | – | – |

During the year, the Credit Union transferred mortgage loans to the Athena Trust under a securitisation arrangement.

Under the arrangements the Credit Union bears no credit risk in respect of these loans. The risks and rewards of ownership to which the entity remains exposed are the interest rate risk arising from the prepayment of the loans, and the Credit Union is the ultimate beneficiary of the trust net assets on winding up. Whilst these transfers satisfied all prudential requirements to obtain the benefits of capital relief, under the Accounting Standards the Athena Trust is deemed to be controlled by the Credit Union, and as a consequence these loans have continued to be disclosed as assets on the Statement of Financial Position for the consolidated group.

The carrying amounts of the assets held in the Athena trust are stated above in Note 7, and the associated liabilities are set out in Note 13.

The Credit Union receives a fee from the Manager of the Athena Trust as consideration for managing the loan portfolio on behalf of the trust.

| | 2010 $ | 2009 $ |
|---|---|---|

## 8. Provision on impaired loans

### a. Total provision comprises

| | 2010 $ | 2009 $ |
|---|---|---|
| Collective provisions | 917,780 | 873,120 |
| Individual specific provisions | – | – |
| **Total Provision** | **917,780** | **873,120** |

### b. Movement in the provision for impairment

| | 2010 $ | 2009 $ |
|---|---|---|
| Balance at the beginning of year | 873,120 | 714,314 |
| Add (deduct): | | |
| Transfers from (to) income statement | 44,660 | 158,806 |
| Bad debts written off provision | – | – |
| **Balance at end of year** | **917,780** | **873,120** |

Details of credit risk management is set out in Note 20.

### c. Impaired loans written off

| | 2010 $ | 2009 $ |
|---|---|---|
| Amounts written off against the provision for impaired loans | – | – |
| Amounts written off directly to expense | 1,516,926 | 1,534,910 |
| Total bad debts | **1,516,926** | **1,534,910** |
| Bad debts recovered in the period | 478,677 | 475,866 |
| | **1,038,249** | **1,059,044** |

### d. Analysis of loans that are impaired or potentially impaired by class

In the note below:

– carrying Value is the amount recorded on the Balance Sheet;

– impaired loans value is the 'on balance sheet' loan balances which are past due by 90 days or more;

– provision for impairment is the amount of the impairment provision allocated to the class of impaired loans.

| | 2010 Carrying value $ | 2010 Value of impaired loans $ | 2010 Provision for impairment $ | 2009 Carrying value $ | 2009 Value of impaired loans $ | 2009 Provision for impairment $ |
|---|---|---|---|---|---|---|
| Loans to members | | | | | | |
| Mortgages held by Athena Trust | 56,366,795 | – | – | – | – | – |
| Mortgages | 316,461,676 | – | – | 258,530,326 | – | – |
| Personal | 127,637,977 | 708,463 | 360,655 | 121,954,172 | 806,693 | 387,159 |
| Credit cards and overdrafts | 25,867,710 | 860,458 | 557,125 | 22,302,659 | 712,566 | 485,961 |
| Total to natural persons | **526,334,158** | **1,568,921** | **917,780** | **402,787,157** | **1,519,259** | **873,120** |
| Corporate borrowers | – | – | – | – | – | – |
| **Total** | **526,334,158** | **1,568,921** | **917,780** | **402,787,157** | **1,519,259** | **873,120** |

Past due value is the 'on balance sheet' loan balances which are past due by 90 days or more.

It is not practicable to determine the fair value of all collateral as at the balance date due to the variety of assets and condition.

## e. Analysis of loans that are impaired or potentially impaired based on age of repayments outstanding

| | 2010 | | 2009 | |
|---|---|---|---|---|
| **Non impaired loans** | Carrying value $ | Provision $ | Carrying value $ | Provision $ |
| In advance & up to 30 days in arrears | 522,973,810 | – | 399,894,860 | – |
| 31 to 90 days in arrears | 1,791,427 | – | 1,373,038 | – |
| **Impaired loans** | | | | |
| 90 to 180 days in arrears | 403,421 | 161,369 | 535,528 | 214,211 |
| 181 to 270 days in arrears | 231,849 | 139,110 | 230,307 | 138,184 |
| 271 to 365 days in arrears | 65,083 | 52,066 | 30,475 | 24,380 |
| Over 365 days in arrears | 8,110 | 8,110 | 10,384 | 10,384 |
| Overlimit facilities over 14 days | 860,458 | 557,125 | 712,565 | 485,961 |
| **Total** | **526,334,158** | **917,780** | **402,787,157** | **873,120** |

The impaired loans are generally not secured against residential property. Some impaired loans are secured by bill of sale over motor vehicles or other assets of varying value. It is not practicable to determine the fair value of all collateral as at the balance date due to the variety of assets and condition.

## f. Loans with repayments past due but not regarded as impaired

There are loans with a value of $0 past due which not considered to be impaired as the value of related security over residential property is in excess of the loan due. It is not practicable to determine the fair value of all collateral as at the balance date due to the variety of assets and condition.

Loans with repayments past due but not impaired are in arrears as follows:

### Loans members

| | 1–3 Months | 3–6 Months | 6–12 Months | > 1 Year | Total |
|---|---|---|---|---|---|
| **2010** | | | | | |
| Mortgage secured | 488,045 | – | – | – | 488,045 |
| Personal loans | 1,303,382 | – | – | – | 1,303,382 |
| Credit cards and overdrafts less than 14 days | 237,164 | – | – | – | 237,164 |
| **Total** | **2,028,591** | – | – | – | **2,028,591** |
| **2009** | | | | | |
| Mortgage secured | – | – | – | – | – |
| Personal loans | 1,373,038 | – | – | – | 1,373,038 |
| Credit cards and overdrafts less than 14 days | 103,245 | – | – | – | 103,245 |
| **Total** | **1,476,283** | – | – | – | **1,476,283** |

| | 2010 $ | 2009 $ |
|---|---|---|

### g. Loans renegotiated

Some loans that were previously past due or impaired, have been renegotiated by the Credit Union and are no longer regarded as impaired. Details of these loans are:

| **Value of loans renegotiated during the year and not now regarded as impaired** | | |
|---|---|---|
| Book value of the renegotiated loans at balance date | **176,473** | **210,131** |
| Book value of these loans which are well secured | – | – |
| Book value of these loans which are not well secured | **176,473** | **210,131** |

Well secured loans are secured by registered mortgage over real estate.

### h. Key assumptions in determining the provision for impairment

In the course of the preparation of the annual report the Credit Union has determined the likely impairment loss on loans that have not maintained repayments in accordance with the loan contract, or where there is other evidence of potential impairment such as industrial restructuring, job losses or economic circumstances. In identifying the impairment likely from these events the Credit Union is required to estimate the potential impairment using the length of time the loan is in arrears and the historical losses arising in past years. Given the relatively small number of impaired loans, the circumstances may vary for each loan over time resulting in higher or lower impairment losses. An estimate is based on the period of impairment.

| Period of impairment | % of balance |
|---|---|
| Up to 90 days | 0 |
| 91 days to 180 days | 40 |
| 181 days to 270 days | 60 |
| 271 days to 365 days | 80 |
| Over 365 days | 100 |

| | 2010 $ | 2009 $ |
|---|---|---|

## 9. Available for sale investments

| **Shares in unlisted companies – at cost** | | |
|---|---|---|
| – Cuscal Limited | 907,154 | 907,154 |
| **Total value of investments** | **907,154** | **907,154** |

### Disclosures on shares held at cost

#### Cuscal Limited

The shareholding in Cuscal is measured at cost as its fair value could not be measured reliably. This company was created to supply services to the member credit unions and does not have an independent business focus. These shares are held to enable the Credit Union to receive essential banking services – refer to Note 29. The shares are not able to be traded and are not redeemable.

The financial reports of Cuscal record net tangible asset backing of these shares exceeding their cost value. Based on the net assets of Cuscal, any fair value determination on these shares is likely to be greater than their cost value, but due to the absence of a ready market and restrictions on the ability to transfer the shares, a market value is not able to be determined readily.

The Credit Union is not intending, nor able to, dispose of these shares.

| | 2010 $ | 2009 $ |
|---|---|---|

## 10. Property, plant and equipment

### a. Fixed assets

| | 2010 $ | 2009 $ |
|---|---|---|
| **Plant and equipment - at cost** | 4,835,184 | 4,644,029 |
| Less: provision for depreciation | 4,415,968 | 4,139,413 |
| | 419,216 | 504,616 |
| **Capitalised leasehold improvements at cost** | 1,817,950 | 1,760,939 |
| Less: provision for amortisation | 1,542,961 | 1,369,853 |
| | 274,989 | 391,086 |
| | **694,205** | **895,702** |

### b. Movement in the assets balances during the year were:

| | 2010 Plant & equipment $ | 2010 Leasehold improvements $ | 2010 Total $ | 2009 Plant & equipment $ | 2009 Leasehold improvements $ | 2009 Total $ |
|---|---|---|---|---|---|---|
| Opening balance | 504,616 | 391,086 | 895,702 | 757,983 | 398,330 | 1,156,313 |
| Purchases | 222,328 | 57,010 | 279,338 | 132,809 | 157,055 | 289,864 |
| Revaluation increase | – | – | – | – | – | – |
| Less | | | | | | |
| Assets disposed | 1,365 | – | 1,365 | – | 607 | 607 |
| Depreciation charge | 306,363 | 173,107 | 479,470 | 386,176 | 163,692 | 549,868 |
| Revaluation decrease | – | – | – | – | – | – |
| Impairment loss | – | – | – | – | – | – |
| **Balance at the end of the year** | **419,216** | **274,989** | **694,205** | **504,616** | **391,086** | **895,702** |

## 11. Taxation assets

| | 2010 $ | 2009 $ |
|---|---|---|
| Deferred tax assets | **848,110** | **771,222** |
| Deferred tax assets comprise: | | |
| - Accrued expenses not deductible until incurred | 31,882 | 24,000 |
| - Provisions for impairment on loans | 275,334 | 261,936 |
| - Provisions for employee benefits | 304,925 | 330,819 |
| - Depreciation on fixed assets and intangible assets | 147,822 | 99,869 |
| - Deferred fees (less transaction costs) on loan origination | 88,147 | 54,598 |
| | **848,110** | **771,222** |

| | 2010 $ | 2009 $ |
|---|---|---|

## 12. Intangible assets

| | 2010 $ | 2009 $ |
|---|---|---|
| Computer software | 2,901,810 | 2,631,027 |
| Less provision for amortisation | 2,092,647 | 1,783,384 |
| | **809,163** | **847,643** |
| **Movement in the assets balances during the year were:** | | |
| Opening balance | 847,643 | 955,659 |
| Purchases | 270,782 | 193,505 |
| Less | | |
| Assets disposed | – | 1,064 |
| Depreciation charge | 309,262 | 300,457 |
| **Balance at the end of the year** | **809,163** | **847,643** |

## 13. Short term borrowings

| | 2010 $ | 2009 $ |
|---|---|---|
| Borrowings from Westpac through the Athena Trust | 56,366,795 | – |
| Loans from other ADIs | 40,000,000 | 15,087,000 |
| Overdraft | – | 1,825,377 |
| | **96,366,795** | **16,912,377** |

There were no defaults on interest and capital payments on these liabilities in the current or prior year.

## 14. Deposit

| | 2010 $ | 2009 $ |
|---|---|---|
| Member deposits | | |
| - at call | 210,667,129 | 220,448,216 |
| - term | 261,234,896 | 180,924,663 |
| Deposits from other financial institutions - term | 18,500,000 | 35,000,000 |
| Member withdrawable shares | 94,910 | 92,992 |
| | **490,496,935** | **436,465,871** |

There were no defaults on interest and capital payments on these liabilities in the current or prior year.

**Concentration of member deposits**

| | 2010 $ | 2009 $ |
|---|---|---|
| (i) Significant individual member deposits which in aggregate represent more than 10% of the total liabilities; | – | – |
| (ii) Member deposits at balance date were received from individuals employed principally in the Australian Defence industry. | – | – |

## 15. Creditor accruals and settlement accounts

| | 2010 $ | 2009 $ |
|---|---|---|
| Annual leave | 621,702 | 645,644 |
| Creditors and accruals | 825,172 | 941,560 |
| Interest payable on borrowings | 239,947 | 102,015 |
| Interest payable on deposits | 3,822,222 | 3,920,291 |
| Sundry creditors | 1,774,602 | 1,252,087 |
| | **7,283,645** | **6,861,597** |

| | 2010 $ | 2009 $ |
|---|---:|---:|

## 16. Taxation liabilities

| | 2010 $ | 2009 $ |
|---|---:|---:|
| Current income tax liability | **1,957,145** | **199,395** |
| **Current income tax liability comprises:** | | |
| Liability for income tax in current year | 2,527,324 | 781,935 |
| Less installments paid in current year | 570,179 | 582,540 |
| **Balance – current year** | **1,957,145** | **199,395** |

## 17. Provisions

| | 2010 $ | 2009 $ |
|---|---:|---:|
| Long service leave | 394,714 | 457,087 |
| Provisions – other | – | – |
| **Total provisions** | **394,714** | **457,087** |

## 18. Capital reserve account

| | 2010 $ | 2009 $ |
|---|---:|---:|
| Balance at the beginning of the year | 85,286 | 79,110 |
| Transfer from retained earnings on share redemptions | 5,982 | 6,176 |
| Balance at the end of year | **91,268** | **85,286** |

Share redemption

The accounts represent the amount of redeemable preference shares redeemed by the Credit Union since 1 July 1999. The law requires that the redemption of the shares be made out of profits. Since the value of the shares has been paid to members in accordance with the terms and conditions of the share issue, the account represents the amount of profits appropriated to the account.

## 19. General reserve for credit losses

| | 2010 $ | 2009 $ |
|---|---:|---:|
| General reserve for credit losses | 1,060,545 | 1,060,545 |
| Other reserve for credit losses | – | – |
| | **1,060,545** | **1,060,545** |

**General reserve for credit losses**

This reserve records amount previously set aside as a General provision and is maintained to comply with the Prudential Standards set down by APRA

| | 2010 $ | 2009 $ |
|---|---:|---:|
| Balance at beginning of year | 1,060,545 | 1,060,545 |
| Add: increase (decrease) transferred from retained earnings | – | – |
| Balance at end of year | **1,060,545** | **1,060,545** |

## 20. Financial risk management objectives and policies

### Introduction

The Board has endorsed a policy of compliance and risk management to suit the risk profile of the Credit Union.

The Credit Union's risk management focuses on the major areas of market risk, credit risk and operational risk. Authority flows from the Board of Directors to the Risk Committee and from there to the Audit Committee which are integral to the management of risk. The main elements of risk governance are as follows:

**Board:** This is the primary governing body. It approves the level of risk which the Credit Union is exposed to and the framework for reporting and mitigating those risks.

**Risk Committee:** This is a key body in the control of risk. The committee comprises three Directors assisted by the Head of Finance and Operations, the Head of Credit and the Compliance Manager. The Risk Committee does not form a view on the acceptability of risks but instead reviews risks and controls that are used to mitigate those risks. This includes the identification, assessment and reporting of risks. Regular monitoring is carried out by the Risk Committee through a monthly review of operational reports. The Risk Committee confirms whether risks are within the parameters outlined by the Board.

The Risk Committee carries out a regular review of all operational areas to ensure that operational risks are being properly controlled and reported. It also ensures that contingency plans are in place to achieve business continuity in the event of serious disruptions to business operations.

The Risk Committee monitors compliance with the framework laid out in policy on a quarterly basis and reports in turn to the Board, where actual exposures to risks are measured against prescribed limits.

**Audit Committee:** Its key role in risk management is the assessment of the controls that are in place to mitigate risks. The Audit Committee considers and confirms that the significant risks and controls are to be assessed within the internal audit plan. The Audit Committee receives the internal audit reports on assessment and compliance with the controls, and provides feedback to the Risk Committee for their consideration.

**Asset & Liability Committee (ALCO):** This committee of senior management meets at least monthly and has responsibility for managing and reporting credit, liquidity, market and capital risk exposure. It scrutinises operational reports and monitors exposures against limits determined by the Board.

**Operational Risk Management Committee (ORMC):** This committee of senior management meets at least monthly and is responsible for enabling Executive Management and the Board to implement an effective Operational Risk Management Framework and to ensure that the Board receives regular reporting and updates relating to operational risk management matters, thereby fulfilling the Board's oversight responsibilities in respect of operational risk management. The committee reviews, monitors, interrogates and reports to the Executive and Board on the information contained within the Credit Unions operational risk management system "WORMS", with particular reference to KRI information.

**Head of Finance and Operations and Head of Credit:** These positions have responsibility for ensuring timely production of information for the Risk Committee and ensuring that instructions passed down from the Board via the Risk Committee are implemented.

**Internal Audit:** Internal audit has responsibility for implementing the controls testing and assessment as required by the Audit Committee.

Key risk management policies encompassed in the overall risk management framework include:

- the overarching Risk Management Policy;
- Liquidity Management Plan;
- Capital Risk Management Plan;
- Market Risk Management Plan;
- Funding Plan;
- Credit Risk Management Policy;
- Collections Policy;
- Operational Risk Management Policy, which has a number of related documents, including the Compliance Program, AML/CTF Program, Data Risk Management Policy and other operational risk management policy documents.

The Credit Union has undertaken the following strategies to minimise the risks arising from financial instruments:

### A. Market risk

The objective of the Credit Union's market risk management is to manage and control market risk exposures in order to optimise risk and return.

Market risk is the risk that changes in interest rates, foreign exchange rates or other prices and volatilities will have an adverse effect on the Credit Union's financial condition or results. The Credit Union is not exposed to currency risk, and other significant price risk. The Credit Union does not trade in the financial instruments it holds on its books. The Credit Union is exposed only to interest rate risk arising from changes in market interest rates.

The management of market risk is the responsibility of the ALCO, which reports directly to the Board.

#### Interest rate risk

Interest rate risk is the risk of variability of the fair value of future cash flows arising from financial instruments due to the changes in interest rates.

Most banks are exposed to interest rate risk within their treasury operations. The Credit Union does not have a treasury operation and does not trade in financial instruments.

#### Interest rate risk in the banking book

The Credit Union is exposed to interest rate risk in its banking book due to mismatches between the repricing dates of assets and liabilities.

In the banking book the most common risk the Credit Union faces arises from fixed rate assets and liabilities. This exposes the Credit Union to the risk of sensitivity should interest rates change.

This risk is not considered sufficiently significant to warrant the use of derivatives to mitigate it.

#### Method of managing risk

The Credit Union manages its interest rate risk by the use of a value at risk VaR model. An independent review of the interest rate risk profile is conducted on a quarterly basis by Protecht Advisory Pty Ltd, an independent risk management consultancy company. The Board monitors interest rate risk through the management reporting process.

#### Value at Risk (VaR)

The Credit Union's exposure to market risk is measured and monitored using the VaR methodology of estimating potential losses. VaR is a technique which estimates the potential losses that could occur on risk positions taken due to movements in market rates and prices over a specified time period to a given level of confidence. VaR is calculated using historical simulations, movements in market rates and prices, a 99.5 per cent confidence level and taking into account historical correlations between different markets and rates.

Although the use of the VaR model calculates the interest rate sensitivity on the banking book, this is not reflected in the Pillar 1 capital requirement.

The Credit Union's exposure to banking book interest rate risk is not expected to change materially in the next year and existing capital requirements are considered to be an accurate measurement of capital needed to mitigate interest rate risk.

### B. Liquidity risk

Liquidity risk is the risk that the Credit Union may encounter difficulties raising funds to meet commitments associated with financial instruments, e.g. borrowing repayments or member withdrawal demands. It is the policy of the Board of Directors that treasury maintains adequate cash reserves and committed credit facilities so as to meet the member withdrawal demands when requested.

The Credit Union manages liquidity risk by:

- continuously monitoring actual daily cash flows and longer term forecasted cash flows;
- monitoring the maturity profiles of financial assets and liabilities;
- maintaining adequate reserves, liquidity support facilities and reserve borrowing facilities;
- monitoring the prudential liquidity ratio daily; and
- transferring loans to the Athena trust or to the Integris securitisation scheme when there are insufficient liquid funds to meet loan demand (See Note 32).

The Credit Union has a longstanding arrangement with the industry liquidity support scheme Credit Union Financial Support Services (CUFSS) which can access industry funds to provide support to the Credit Union should this be necessary.

The maturity profile of the financial liabilities, based on the contractual repayment terms are set out in Note 22.

### C. Credit risk

Credit risk is the risk that members, financial institutions and other counterparties will be unable to meet their obligations to the Credit Union which may result in financial loss. Credit risk arises principally from the Credit Union's loan book and investment assets.

The method of managing credit risk is by way of strict adherence to the credit assessment policies before the loan is approved and close monitoring of defaults in the repayment of loans thereafter on a weekly basis. The Credit Policy has been endorsed by the Board to ensure that loans are only made to members that are creditworthy (capable of meeting loan repayments).

The Credit Union has established policies over the:

- credit assessment and approval of loans and facilities covering acceptable risk assessment and security requirements;
- limits of acceptable exposure to individual borrowers, non mortgage secured loans, commercial lending and concentrations to geographic and industry groups considered at high risk of default;
- reassessing and review of the credit exposures on loans and facilities;
- establishing appropriate provisions to recognise the impairment of loans and facilities;
- debt recovery procedures; and
- review of compliance with the above policies.

A regular review of compliance is conducted as part of the internal audit scope.

**Past due and impaired**

A financial asset is past due when the counterparty has failed to make a payment when contractually due. As an example, a member enters into a lending agreement with the Credit Union that requires interest and a portion of the principle to be paid every month. On the first day of the next month, if the agreed repayment amount has not been paid, the loan is past due. Past due does not mean that a counterparty will never pay, but it can trigger various actions such as renegotiation, enforcement of covenants, or legal proceedings. Once the past due exceeds 90 days the loan is regarded as impaired, unless other factors indicate the impairment should be recognised sooner.

Daily reports monitor the loan repayments to detect delays in repayments. For loans where repayments are doubtful, external consultants are engaged to conduct recovery action once the loan is over 90 days in arrears. The exposure to loss arise predominantly with personal loans and facilities not secured by registered mortgage over real estate.

If evidence of impairment exists, the estimated recoverable amount of the asset is determined and any impairment loss, based on the net present value of future anticipated cash flows, is recognised in the income statement. In estimating these cash flows, management makes judgements about a counterparty's financial situation and the net realisable value of any underlying collateral.

In addition to specific provisions against individually significant financial assets, the Credit Union makes collective assessments for each financial asset portfolio segmented by similar risk characteristics.

Balance sheet provisions are maintained at a level that management deems sufficient to absorb probable incurred losses in the Credit Union's loan portfolio from homogenous portfolios of assets and individually identified loans.

A provision for incurred losses is established on all past due loans after a specified period of repayment default where it is probable that some of the capital will not be repaid or recovered. Specific loans and portfolios of assets are provided against depending on a number of factors including changes in a counterparty's industry and identified structural weaknesses or deterioration in cash flows.

The provisions for impaired and past due exposures relate to the loans to members.

Past due value is the 'on balance sheet' loan balances which are past due by 90 days or more.

Details are as set out in Note 8.

**Bad debts**

Amounts are written off when collection of the loan or advance is considered to be remote. All write-offs are on a case by case basis, taking account of the exposure at the date of the write-off.

On secured loans, the write-off takes place on ultimate realisation of collateral value, or from claims on any lenders mortgage insurance.

A reconciliation in the movement of both past due and impaired exposure provisions is provided in Note 8.

**Collateral securing loans**

A sizeable portfolio of the loan book is secured on residential property in Australia. Therefore, the Credit Union is exposed should the property market be subject to a decline.

The risk of losses from the loans undertaken is primarily reduced by the nature and quality of the security taken. Note 7.b describes the nature and extent of the security held against the loans held as at the balance date.

### Concentration risk – individuals

Concentration risk is a measurement of the Credit Union's exposure to an individual counterparty (or group of related parties). If prudential limits are exceeded as a proportion of the Credit Union's regulatory capital a large exposure is considered to exist. No capital is required to be held against these but the APRA must be informed. APRA may impose additional capital requirements if it considers the aggregate exposure to all loans over the 10% capital benchmark to be higher than acceptable.

The aggregate value of large exposure loans is set out in Note 7. The Credit Union holds no significant concentrations of exposures to members. Concentration exposures to counterparties are closely monitored with annual reviews being prepared for all exposures over 5 per cent of the capital base.

The Credit Union's policy on exposures of this size is to insist on an initial Loan to Valuation ratio (LVR) of no more than 80 per cent and bi-annual reviews of compliance with this policy are conducted.

### Concentration risk – industry

The Credit Union has a concentration in the retail lending for members who comprise employees and family in the Defence industry. This concentration is considered acceptable on the basis that the Credit Union was formed to service these members, and the employment concentration is not exclusive. Should members leave the industry the loans continue and other employment opportunities are available to the members to facilitate the repayment of the loans. The details of the geographical and industry concentrations are set out in Note 7.

### Credit risk – liquid investments

Credit risk is the risk that the other party to a financial instrument will fail to discharge their obligation resulting in the Credit Union incurring a financial loss. This occurs when a debtor fails to settle their obligations owing to the Credit Union.

The credit policy is that investments are only made to institutions that are credit worthy based on the assessment of independent credit rating agencies. The risk of losses from liquid investments is reduced by the nature and quality of the financial institutions used and limits to the concentration and amount of individual investments with an institution.

There is a concentration of credit risk with respect to investment receivables with the placement of investments with Cuscal; a company set up to support member credit unions and which has a AA- rating.

### External credit assessment for institution investments

The Credit Union uses the ratings of reputable ratings agencies to assess the credit quality of all investment exposure, where applicable, using the credit quality assessment scale in APRA prudential guidance AGN 112.

## D. Operational risk

Operational risk is the risk of loss to the Credit Union resulting from deficiencies in processes, personnel, technology and infrastructure, and from external factors other than credit, market and liquidity risks. Operational risks in the Credit Union relate mainly to those risks arising from a number of sources including legal compliance, business continuity, data infrastructure, outsourced services failures, fraud, and employee errors.

The Credit Union's objective is to manage operational risk so as to balance the avoidance of financial losses through the implementation of controls, whilst avoiding procedures which inhibit innovation and creativity. These risks are managed through the implementation of polices and systems to monitor the likelihood of the events and minimise the impact. Systems of internal control are enhanced through:

- the segregation of duties between employee duties and functions, including approval and processing duties;
- documentation of the policies and procedures, employee job descriptions and responsibilities, to reduce the incidence of errors and inappropriate behavior;
- implementation of the whistleblowing policy to promote a compliant culture and awareness of the duty to report exceptions by staff;
- education of members to review their account statements and report exceptions to the Credit Union promptly;
- effective dispute resolution procedures to respond to member complaints;
- effective insurance arrangements to reduce the impact of losses;
- contingency plans for dealing with the loss of functionality of systems or premises or staff.

### Fraud

Fraud can arise from member card PINs and internet passwords being compromised where not protected adequately by the member. It can also arise from other systems failures. The Credit Union has systems in place which are considered to be robust enough to prevent any material fraud. However, in common with all retail banks, fraud is potentially a real cost to the Credit Union. Fraud losses have arisen from card skimming, internet password theft and false loan applications.

### IT systems

The worst case scenario would be the failure of the Credit Union's core banking and IT network suppliers to meet customer obligations and service requirements. The Credit Union has outsourced the IT systems management to an Independent Data Processing Centre (IDPC) which is owned by a collection of credit unions. This organisation has the experience in-house to manage any short-term problems and has a contingency plan to manage any related power or systems failures. Other network suppliers are engaged on behalf on the Credit Union by the industry body Cuscal to service the settlements with other financial institutions for direct entry, ATM & Visa cards and BPAY etc.

A full disaster recovery plan is in place to cover medium to long-term problems which is considered to mitigate the risk to an extent such that there is no need for any further capital to be allocated.

## E. Capital management

The capital levels are prescribed by Australian Prudential Regulation Authority (APRA). Under the APRA prudential standards capital is determined in three components:

- credit risk;
- market risk (trading book);
- operational risk.

The market risk component is not required as the Credit Union is not engaged in a trading book for financial instruments.

### Capital resources

### Tier 1 capital

The vast majority of Tier 1 capital comprises:

- retained profits;
- realised reserves.

### Tier 2 capital

Tier 2 capital consists of capital instruments that combine the features of debt and equity in that they are structured as debt instruments, but exhibit some of the loss absorption and funding flexibility features of equity. There are a number of criteria that capital instruments must meet for inclusion in Tier 2 capital resources as set down by APRA.

Tier 2 capital generally comprises a general reserve for Credit Losses. The level of the capital ratio can be affected by growth in the Credit Union's asset base relative to growth in reserves and by changes in the mix of assets.

To manage the Credit Union's capital the Credit Union reviews the ratio monthly and monitors major movements in the asset levels. Policies have been implemented to require reporting to the Board and the regulator if the capital ratio falls below the documented trigger levels. Further, a 3 year capital budget projection of the capital levels is maintained annually to address how strategic decisions or trends may impact on the capital level.

### Pillar 2 capital on operational risk

This capital component was introduced as from the 1 January 2008 and coincided with changes in the asset risk weightings for specified loans and liquid investments. Previously no operational charge was prescribed.

The Credit Union uses the Standardised approach which is considered to be most suitable for its business given the small number of distinct transaction streams. The Operational Risk Capital Requirement is calculated by mapping the Credit Union's three year average net interest income and net non-interest income to the Credit Union's various business lines.

It is considered that the Standardised approach accurately reflects the Credit Union's operational risk other than for the specific items set out below.

### Internal capital adequacy management

The Credit Union manages its internal capital levels for both current and future activities through a combination of the various committees. The outputs of the individual committees are reviewed by the Board in its capacity as the primary governing body. The capital required for any change in the Credit Union's forecasts for asset growth, or unforeseen circumstances, is assessed by the Board. The Finance Department then updates the forecast capital resources models produced and the impact upon the overall capital position of the Credit Union is reassessed.

The Credit Union is also able to transfer loans to the Athena trust and the Integris securisation vehicle, to assist with capital management.

## 21. Categories of financial instruments

The following information classifies the financial instruments into measurement classes.

| | Note | 2010 $ | 2009 $ |
|---|---|---|---|
| **FINANCIAL ASSETS** - carried at amortised cost | | | |
| Cash | 4 | 13,520,374 | 1,064,624 |
| Receivables | | 2,331,429 | 2,411,889 |
| Receivables from financial institutions | 5 | 107,500,000 | 101,500,000 |
| Loans to members | 7 & 8 | 468,755,762 | 401,732,045 |
| Loans held by Athena Trust | | 56,366,795 | – |
| **Total loans and receivables carried at amortised cost** | | **648,474,360** | **506,708,558** |
| Available for sale investments - carried at cost | 9 | 907,154 | 907,154 |
| Available for sale investments - carried at fair value | | – | – |
| Total available for sale investments | | 907,154 | 907,154 |
| **Total financial assets** | | **649,381,514** | **507,615,712** |
| **FINANCIAL LIABILITIES** | | | |
| Short term borrowings | 13 | 40,000,000 | 16,912,377 |
| Creditors | | 6,661,943 | 6,359,946 |
| Deposits from other institutions | | 18,500,000 | 35,000,000 |
| Securitisation Facility – Athena Trust | | 56,366,795 | – |
| Deposits from members | 14 | 471,996,935 | 401,465,871 |
| **Total carried at amortised cost** | | **593,525,673** | **459,738,194** |
| **Total financial liabilities** | | **593,525,673** | **459,738,194** |

## 22. Maturity profile of financial assets and liabilities

Monetary assets and liabilities have differing maturity profiles depending on the contractual term, and in the case of loans the repayment amount and frequency. The table below shows the period in which different monetary liabilities held will mature and be eligible for renegotiation or withdrawal. Financial liabilities are at the undiscounted values (including future interest expected to be paid). Accordingly these values will not agree to the balance sheet.

| 2010 | Within 1 month $000 | 1 – 3 months $000 | 3 – 12 months $000 | 1 – 5 years $000 | After 5 years $000 | No maturity $000 | Total $000 |
|---|---|---|---|---|---|---|---|
| **ASSETS** | | | | | | | |
| Cash | 13,520 | – | – | – | – | – | 13,520 |
| Advance to financial institutions | 26,822 | 22,009 | 62,775 | – | – | – | 111,606 |
| Loans & advances | 6,215 | 12,430 | 50,668 | 224,822 | 561,750 | – | 855,885 |
| Loans & advances – Athena Trust | 461 | 923 | 3,811 | 20,750 | 92,505 | – | 118,450 |
| **Total Financial Assets** | **47,018** | **35,362** | **117,254** | **245,572** | **654,255** | – | **1,099,461** |
| **LIABILITIES** | | | | | | | |
| Borrowings | 10,077 | 20,200 | 10,487 | – | – | – | 40,764 |
| Creditors | 2,600 | – | – | – | – | – | 2,600 |
| Deposits from other financial institutions | 1,001 | 15,672 | 2,046 | – | – | – | 18,719 |
| Deposits from members | 287,017 | 107,093 | 84,321 | 1,247 | – | – | 479,678 |
| **On Balance Sheet** | **300,695** | **142,965** | **96,854** | **1,247** | – | – | **541,761** |
| Undrawn commitments | 60,459 | – | – | – | – | – | 60,459 |
| **Total Financial Liabilities** | **361,154** | **142,965** | **96,854** | **1,247** | – | – | **602,220** |

| 2009 | Within 1 month $000 | 1 – 3 months $000 | 3 – 12 months $000 | 1 – 5 years $000 | After 5 years $000 | No maturity $000 | Total $000 |
|---|---|---|---|---|---|---|---|
| **ASSETS** | | | | | | | |
| Cash | 1,065 | – | – | – | – | – | 1,065 |
| Advance to financial Institutions | 28,024 | 17,092 | 43,054 | 16,637 | – | – | 104,807 |
| Loans & advances | 4,721 | 9,442 | 44,667 | 183,674 | 422,610 | – | 665,114 |
| Loans & advances – Athena Trust | – | – | – | – | – | – | – |
| **Total Financial Assets** | **33,810** | **26,534** | **87,721** | **200,311** | **422,610** | – | **770,986** |
| **LIABILITIES** | | | | | | | |
| Borrowings | 9,303 | 6,471 | – | – | – | – | 15,774 |
| Creditors | 2,440 | – | – | – | – | – | 2,440 |
| Deposits from other financial institutions | 20,320 | 15,185 | – | – | – | – | 35,505 |
| Deposits from members | 264,523 | 97,767 | 42,748 | 1,750 | – | 93 | 406,881 |
| **On Balance Sheet** | **296,586** | **119,423** | **42,748** | **1,750** | – | 93 | **460,600** |
| Undrawn commitments | 40,397 | – | – | – | – | – | 40,397 |
| **Total Financial Liabilities** | **336,983** | **119,423** | **42,748** | **1,750** | – | **93** | **500,997** |

## 23. Interest rate change of profile of financial assets and liabilities

Financial assets and liabilities have conditions which allow interest rates to be amended either on maturity (term deposits and term investments) or after adequate notice is given (loans and savings). The table below shows the respective value of funds where interest rates are capable of being altered within the prescribed time bands, being the earlier of the contractual repricing date, or maturity date.

| 2010 | Within 1 month $000 | 1 – 3 months $000 | 3 – 12 months $000 | 1 – 5 years $000 | After 5 years $000 | Non interest bearing $000 | Total $000 |
|---|---|---|---|---|---|---|---|
| **ASSETS** | | | | | | | |
| Cash | 12,443 | – | – | – | – | 1,077 | 13,520 |
| Receivables | – | – | – | – | – | 2,331 | 2,331 |
| Advances to other financial institutions | 26,500 | 21,500 | 59,500 | – | – | – | 107,500 |
| Loans & advances | 408,035 | 2,761 | 19,454 | 39,717 | – | – | 469,967 |
| Loans & advances – Athena Trust | 56,367 | – | – | – | – | – | 56,367 |
| Investments | – | – | – | – | – | 907 | 907 |
| **Total Financial Assets** | **503,345** | **24,261** | **78,954** | **39,717** | **0** | **4,315** | **650,592** |
| **LIABILITIES** | | | | | | | |
| Borrowings - Securitisation facility | 56,367 | – | – | – | – | – | 56,367 |
| Borrowings - other ADIs | 10,000 | 20,000 | 10,000 | – | – | – | 40,000 |
| Creditors | – | – | – | – | – | 6,662 | 6,662 |
| Deposits from other financial institutions | 1,000 | 15,500 | 2,000 | – | – | – | 18,500 |
| Deposits from members | 285,367 | 104,672 | 80,727 | 1,136 | – | 95 | 471,997 |
| **On Balance Sheet** | **352,734** | **140,172** | **92,727** | **1,136** | – | **6,757** | **593,526** |
| Undrawn commitments | 60,459 | – | – | – | – | – | 60,459 |
| **Total Financial Liabilities** | **413,193** | **140,172** | **92,727** | **1,136** | **0** | **6,757** | **653,985** |

| 2009 | Within 1 month $000 | 1 – 3 months $000 | 3 – 12 months $000 | 1 – 5 years $000 | After 5 years $000 | Non interest bearing $000 | Total $000 |
|---|---|---|---|---|---|---|---|
| **ASSETS** | | | | | | | |
| Cash | – | – | – | – | – | 1,065 | 1,065 |
| Receivables | – | – | – | – | – | 2,412 | 2,412 |
| Advances to other financial institutions | 28,000 | 17,000 | 42,000 | 14,500 | – | – | 101,500 |
| Loans & advances | 353,518 | 2 | 36,531 | 12,736 | – | – | 402,787 |
| Investments | – | – | – | – | – | 907 | 907 |
| **On Balance Sheet** | **381,518** | **17,002** | **78,531** | **27,236** | – | **4,384** | **508,671** |
| Undrawn commitments | – | – | – | – | – | – | – |
| **Total Financial Assets** | **381,518** | **17,002** | **78,531** | **27,236** | – | **4,384** | **508,671** |
| **LIABILITIES** | | | | | | | |
| Borrowings | 10,912 | 6,000 | – | – | – | – | 16,912 |
| Creditors | – | – | – | – | – | 6,360 | 6,360 |
| Deposits from other financial institutions | 20,000 | 15,000 | – | – | – | – | 35,000 |
| Deposits from members | 261,093 | 94,624 | 44,110 | 1,546 | – | 93 | 401,465 |
| **On Balance Sheet** | **292,005** | **115,624** | **44,110** | **1,546** | – | **6,453** | **459,738** |
| Undrawn commitments | 40,397 | – | – | – | – | – | 40,397 |
| **Total Financial Liabilities** | **332,402** | **115,624** | **44,110** | **1,546** | – | **6,453** | **500,135** |

## 24. Fair value of financial assets and liabilities

Fair value has been determined on the basis of the present value of expected future cash flows under the terms and conditions of each financial asset and financial liability.

Significant assumptions used in the determining the cash flows are that the cash flows will be consistent with the contracted cash flows under the respective contracts.

The information is only relevant to circumstances at balance date and will vary depending on the contractual rates applied to each asset and liability, relative to market rates and conditions at the time. No assets are held regularly traded by the Credit Union, and there is no active market to assess the value of the financial assets and liabilities.

The values reported have not been adjusted for the changes in credit ratings of the assets.

The calculation reflects the interest rate applicable for the remaining term to maturity not the rate applicable to original term

| | 2010 Fair value $ | 2010 Carrying value $ | 2010 Variance $ | 2009 Fair value $ | 2009 Carrying value $ | 2009 Variance $ |
|---|---|---|---|---|---|---|
| **FINANCIAL ASSETS** | | | | | | |
| Cash | 13,520,374 | 13,520,374 | – | 1,064,624 | 1,064,624 | – |
| Advances to other financial institutions | 108,216,994 | 107,500,000 | 716,994 | 102,722,306 | 101,500,000 | 1,222,306 |
| Receivables (1) | 2,073,813 | 2,073,813 | – | 2,411,889 | 2,411,889 | – |
| Loans & advances | 467,917,786 | 468,755,762 | (837,976) | 401,103,988 | 401,732,045 | (628,057) |
| Loans & advances – Athena Trust | 56,366,795 | 56,366,795 | – | – | – | – |
| Investments | 907,154 | 907,154 | – | 907,154 | 907,154 | – |
| **Total Financial Assets** | 649,002,916 | 649,123,898 | (120,982) | 508,209,961 | 507,615,712 | 594,249 |
| **FINANCIAL LIABILITIES** | | | | | | |
| Borrowings | 40,144,938 | 40,000,000 | 144,938 | 15,145,165 | 15,087,000 | 58,165 |
| Securitisation facility | 56,366,795 | 56,366,795 | – | – | – | – |
| Deposits from other financial institutions | 18,540,755 | 18,500,000 | 40,755 | 35,027,053 | 35,000,000 | 27,053 |
| Deposits from members | | | | | | |
| - Call | 210,762,039 | 210,762,039 | – | 220,554,937 | 220,554,937 | – |
| - Term | 261,763,297 | 261,234,896 | 528,401 | 181,639,192 | 180,924,663 | 714,529 |
| Creditors (1) | 6,661,943 | 6,661,943 | – | 6,359,946 | 6,359,946 | – |
| **Total Financial Liabilities** | 594,239,767 | 593,525,673 | 714,094 | 458,726,293 | 457,926,546 | 799,747 |

(1) For these assets and liabilities the carrying value approximates fair value.

Assets where the fair value is lower than the book value have not been written down in the accounts of the Credit Union on the basis that they are to be held to maturity, or in the case of loans, all amounts due are expected to be recovered in full.

The fair value estimates were determined by the following methodologies and assumptions:

### Liquid assets and receivables from other financial institutions

The carrying values of cash and liquid assets and receivables due from other financial institutions redeemable within 12 months approximate their fair value as they are short term in nature or are receivable on demand.

### Loans and advances

The carrying value of loans and advances is net of unearned income and both general and specific provisions for doubtful debts.

For variable rate loans, (excluding impaired loans) the amount shown in the balance sheet is considered to be a reasonable estimate of fair value. The fair value for fixed rate loans is calculated by utilising discounted cash flow models (i.e. the net present value of the portfolio future principal and interest cash flows), based on the period to maturity of the loans. The discount rates applied were based on the current applicable rate offered for the average remaining term of the portfolio.

The fair value of impaired loans was calculated by discounting expected cash flows using a rate which includes a premium for the uncertainty of the flows.

### Deposits from members

The fair value of call and variable rate deposits, and fixed rate deposits repricing within 12 months, is the amount shown in the Balance Sheet. Discounted cash flows were used to calculate the fair value of other term deposits, based upon the deposit type and the rate applicable to its related period maturity.

### Short term borrowings

The carrying value of payables due to other financial institutions approximate their fair value as they are short term in nature and reprice frequently.

## 25. Financial commitments

| | 2010 $ | 2009 $ |
|---|---|---|
| **a. Outstanding loan commitments** | | |
| The loans approved but not funded | **20,648,987** | **16,512,348** |
| **b. Loan redraw facilities** | | |
| The loan redraw facilities available | **21,793,332** | **4,909,317** |
| **c. Undrawn loan facilities** | | |
| Loan facilities available to members for overdrafts and line of credit loans are as follows: | | |
| Total value of facilities approved | 43,891,494 | 41,277,252 |
| Less: Amount advanced | 25,874,962 | 22,302,257 |
| Net undrawn value | **18,016,532** | **18,974,995** |
| These commitments are contingent on members maintaining credit standards and ongoing repayment terms on amounts drawn. | | |
| **Total Financial Commitments** | **60,458,851** | **40,396,660** |
| **d. Computer expenditure commitments** | | |
| The costs committed under contracts with Ultradata are as follows: | | |
| Not later than 1 year | 885,328 | 699,139 |
| Later than 1 year but not 2 years | 1,277,118 | 996,048 |
| Later than 2 years but not 5 years | – | – |
| Later than 5 years | – | – |
| | 2,162,446 | 1,695,187 |
| **e. Lease expense commitments for operating leases on property occupied by the Credit Union** | | |
| Not later than 1 year | 530,265 | 646,258 |
| Later than 1 year but not later than 5 years | 1,060,531 | 2,595,032 |
| Later than 5 years | – | – |
| | **1,590,796** | **3,241,290** |

The operating leases are in respect of property used for providing branch services to members. There are no contingent rentals applicable to leases taken out. The terms of the leases are for between 2 to 5 years and options for renewal are usually obtained for a further 3 years.

There are no restrictions imposed on the Credit Union so as to limit the ability to undertake further leases, borrow funds or issue dividends

## 26. Standby borrowing facilities

The Credit Union has a borrowing facility with Credit Union Services Corporation (Australia) Limited (Cuscal) of:

| | Gross<br>$ | Current borrowing<br>$ | Net available<br>$ |
|---|---|---|---|
| **2010** | | | |
| Committed loan facility - Cuscal | 25,000,000 | – | 25,000,000 |
| Loan facility - other | 60,000,000 | 40,000,000 | 20,000,000 |
| Overdraft facility | 5,000,000 | – | 5,000,000 |
| **TOTAL STANDBY BORROWING FACILITIES** | **90,000,000** | **40,000,000** | **50,000,000** |
| **2009** | | | |
| Loan facility | 25,000,000 | – | 25,000,000 |
| Overdraft facility | 5,000,000 | 1,825,377 | 3,174,623 |
| **TOTAL STANDBY BORROWING FACILITIES** | **30,000,000** | **1,825,377** | **28,174,623** |

Withdrawal of the loan facility is subject to the availability of funds at Cuscal.

Cuscal holds an equitable mortgage charge over all of the assets of the Credit Union as security against loan and overdraft amounts drawn under the facility arrangements.

## 27. Contingent liabilities

### Liquidity Support Scheme

The Credit Union is a member of the Credit Union Financial Support Scheme Limited (CUFSS) a Company limited by guarantee, established to provide financial support to member credit unions in the event of a liquidity or capital problem. As a member, the Credit Union is committed to maintaining 3.2% of the total assets as deposits with Cuscal Limited.

Under the terms of the Industry Support Contract (ISC), the maximum call for each participating credit union would be 3.2% of the credit union's total assets (3% under loans and facilities and 0.2% under the cap on contributions to permanent loans). This amount represents the participating Credit Union's irrevocable commitment under the ISC. At the balance date there were no loans issued under this arrangement.

## 28. Disclosures on Key Management Persons

### a. Remuneration of Key Management Persons [KMP]

*Key management persons* are those persons having authority and responsibility for planning, directing and controlling the activities of the credit union, directly or indirectly, including any Director (whether executive or otherwise) of that credit union. *Control* is the power to govern the financial and operating policies of a credit union so as to obtain benefits from its activities.

**KMP** have been taken to comprise the Directors and the 2 members of the Executive Management responsible for the day to day financial and operational management of the Credit Union.

The aggregate Compensation of **KMP** during the year comprising amounts paid or payable or provided for was as follows:

| | 2010<br>KMP<br>$ | 2009<br>KMP<br>$ |
|---|---|---|
| (a) short-term employee benefits | 727,708 | 690,616 |
| (b) post-employment benefits – superannuation contributions | 61,849 | 61,975 |
| (c) other long-term benefits | – | – |
| (d) termination benefits | – | – |
| (e) share-based payment | – | – |
| **Total** | **789,557** | **752,591** |

In the above table, remuneration shown as short term benefits means (where applicable) wages, salaries and social security contributions, paid annual leave and paid sick leave, profit-sharing and bonuses, value of fringe benefits received, but excludes out of pocket expense reimbursements.

All remuneration to Directors was approved by the members at the previous Annual General Meeting of the Credit Union. The amount approved for 2010 was $260,000. [2009 $202,500].

| | 2010 $ | 2009 $ |
|---|---|---|
| **b. Loans to KMP** | | |
| (i) The aggregate value of loans to Directors and other KMP as at balance date amounted to | **748,821** | **820,291** |
| (ii) The total value of revolving credit facilities to Directors and other KMP, as at balance date amounted to | 18,000 | 38,000 |
| Less amounts drawn down and included in (i) | 17,662 | – |
| **Net balance available** | **338** | **38,000** |
| (iii) During the year the aggregate value of loans disbursed to KMP amounted to: | | |
| Revolving credit facilities | – | – |
| Personal loans | – | – |
| Term loans | – | 1,187,500 |
| | – | **1,187,500** |
| (iv) During the year the aggregate value of revolving credit facility limits granted or increased to KMP amounted to: | – | – |
| (v) Interest and other revenue earned on Loans and revolving credit facilities to KMP | **43,810** | **46,082** |

The Credit Union's policy for lending to KMP is that all loans are approved and deposits accepted on the same terms and conditions which applied to members for each class of loan or deposit with the exception of personal loans to KMP who are not Directors.

There are no loans which are impaired in relation to the loan balances with KMP or their close family relatives.

There are no benefits or concessional terms and conditions applicable to KMP or their close family members.

Other transactions between related parties include deposits from KMP are:

| | 2010 $ | 2009 $ |
|---|---|---|
| Total value term and savings deposits from KMP | 701,128 | 278,393 |
| Total Interest paid on deposits to KMP | 7,199 | 8,009 |

The Credit Union's policy for receiving deposits from KMP is that all transactions are approved and deposits accepted on the same terms and conditions which applied to members for each type of deposit.

## c. Transactions with other related parties

Other transactions between related parties include deposits from related entities or close family members of KMP.

The Credit Union's policy for receiving deposits from related parties is that all transactions are approved and deposits accepted on the same terms and conditions which applied to members for each type of deposit.

There are no benefits paid or payable to the close family members of the KMP.

There are no service contracts to which KMP or their close family members are an interested party.

## 29. Economic dependency

The Credit Union has an economic dependency on the following suppliers of services.

### a. Cuscal Limited

Cuscal is an Approved Deposit Taking Institution registered under the *Corporations Act 2001* and the Banking Act. This entity:

(i) provides the license rights to Visa card in Australia and settlement with Bankers for ATM, Visa card and cheque transactions, direct entry transactions, as well as the production of Visa and Redicards for use by members;

(ii) provides treasury and money market facilities to the Credit Union. The Credit Union has invested a portion of its liquid assets with Cuscal to maximise return on funds, and to comply with the Liquidity Support Scheme requirements.

### b. First Data Corporation

This entity operates the computer network used to link Redicards and Visa cards operated through Reditellers and other approved ATM suppliers to the Credit Union's EDP Systems.

### c. Ultradata Australia Pty Limited

This entity provides and maintains the application software utilised by the Credit Union.

### d. Transaction Solutions Limited

This entity operates the computer facility on behalf of the Credit Union in conjunction with other credit unions. The Credit Union has a management contract with the company to supply computer support staff and services to meet the day to day needs of the Credit Union and compliance with the relevant Prudential Standards.

## 30. Superannuation liabilities

The Credit Union contributes to the CUE Super Plan for the purpose of superannuation guarantee payments and payment of other superannuation benefits on behalf of employees. The plan is administered by an independent corporate trustee.

The Credit Union has no interest in the superannuation plan (other than as a contributor) and is not liable for the performance of the plan, or the obligations of the plan.

## 31. Securitisation

The Credit Union has an arrangement with Integris Securitisation Services Pty Limited whereby it acts as an agent to promote and complete loans on their behalf, for on sale to an investment trust. The Credit Union also manages the loans portfolio on behalf of the trust. The Credit Union bears no risk exposure in respect of these loans. The Credit Union receives a management fee to recover the costs of on-going administration of the processing of the loan repayments and the issue of statements to the members.

The Credit Union is able to assign mortgage secured loans to Integris at the book value of the loans, subject to acceptable documentation criteria. During the year the Credit Union assigned loans to Integris. These loans qualify for de-recognition on the basis that the assignment transfers all the risks and rewards to Integris; there are no residual benefits to the Credit Union. The Credit Union receives a management fee to recover the costs of on-going administration of the processing of the loan repayments and the issue of statements to the members.

In addition to Integris, the Credit Union operates and assigns mortgages to the Athena trust. The trust is independently administered by Perpetual Trustees in their role as trustee and by Cuscal Management Pty Ltd in their role as Manager. Westpac Banking Corporation Ltd provides a committed funding line to the trust. As part of the sale arrangement for assigned mortgages, the Credit Union is granted a service agreement for which it earns a fee.

The amount of securitised loans under management as at 30 June 2010 is $191,206,315 (2009: $156,407,196). Of this $56,366,795 is held by the Athena trust and $134,839,520 is held within the Integris securitisation vehicle.

| | 2010 $ | 2009 $ |
|---|---|---|

## 32. Notes to cash flow statement

### a. Reconciliation of cash

Cash includes cash on hand, and deposits at call with other financial institutions and comprises:

| | 2010 $ | 2009 $ |
|---|---|---|
| Cash on hand | 1,077,497 | 1,064,624 |
| Deposits at call | 12,442,877 | – |
| Bank overdraft | – | (1,825,377) |
| **Total cash** | **13,520,374** | **(760,753)** |

### b. Reconciliation of cash from operations to accounting profit

The net cash increase/(decrease) from operating activities is reconciled to the profit after tax

| | 2010 $ | 2009 $ |
|---|---|---|
| Profit after income tax | 5,811,624 | 2,249,620 |
| **Add (Deduct):** | – | – |
| Bad debts written off | 1,516,926 | 1,534,910 |
| Depreciation expense | 788,732 | 851,215 |
| Loss on sale of assets | – | – |
| (Decrease) in Amortised fees on loans | 111,829 | (58,801) |
| Increase in provisions for staff leave | (86,315) | 220,833 |
| Increase in provision for income tax | 1,757,750 | 199,998 |
| Increase in provision for loans | 44,660 | 158,806 |
| Increase in accrued expenses | 21,544 | 99,330 |
| Increase in interest payable | (98,069) | 872,878 |
| Increase in unearned income | – | – |
| (Gain) on sale of assets | (4,212) | (142,482) |
| Decreases in prepayments | 133,349 | (360,167) |
| Decreases in sundry receivables | (38,859) | 87,199 |
| Decreases in deferred tax assets | (76,888) | (23,257) |
| Decrease in other assets | | |
| Accrued taxes-GST payable | – | (32,629) |
| (Increase) in interest receivable | (939,538) | 559,412 |
| **Net cash from revenue activities** | **8,942,533** | **6,216,865** |

## 33. Corporate information

The Credit Union is a company limited by shares, and is registered under the Corporations Act 2001.

The address of the registered office is:
Level 8, 1 York Street, Sydney NSW 2000.

The address the principal place of business is:
Level 8, 1 York Street, Sydney NSW 2000.

The nature of the operations, and its principal activities are the provision of deposit taking facilities and loan facilities to the members of the Credit Union.

# Images index

The images on pages 2 to 21 are courtesy of the Australian Government Department of Defence www.defence.gov.au

## Page 2

The second of two A25 Blackhawks lands on the aft flight deck, 3 spot, of HMAS KANIMBLA in preparation for Exercise Olgeta Warrior 2009.

## Page 12

Australian Defence Force celebrating Australia Day in the streets of Melbourne.

## Page 16

Australian Super Hornet, aircraft number A44-203 taxis on the flight line at Naval Air Station, Lemoore, California, USA.

## Page 21

A soldier from the 3rd Royal Australian Regiment Battalion Group stands guard outside a building at a village near Gleno.

## Page 41

Australian flag waving at the Commonwealth Games Melbourne.

## Contact information


**Australian Defence Credit Union**

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Commodore Clinton William Thomas AM, CSC, RAN

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Ian Doyle

**Auditors**

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Australian Defence Credit Union


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