Churches' Mutual Credit Union

Contact Name and Details	Mr Doug Swanney, Connexional Secretary Email swanneyd@methodistchurch.org.uk
Status of Paper	Final
Action Required	Decision
Draft Resolution	4/1. The Council agrees to become a partner to the Churches' Mutual Credit Union with those being eligible for membership set out in para 14 and the Council's financial support set out in para. 13.2 a) and b).
Alternative Options to Consider, if Any	None

Summary of Content

Subject and Aims	Credit Union Membership for Methodist Presbyters and Deacons
Main Points	Benefits of CMCU Strategic Fit Loan Products / Savings Accounts Regulation Key Priorities Key Risks Funding Requirements Corporate Deposits and Deferred Shares Methodist Church Involvement Financial input Methodist Membership of the CMCU
Background Context	The Church of England has asked the Methodist Church, as a covenant partner, if it would be interested in participating as a partner in the CMCU. Our understanding is that for regulatory reasons it will be much more straightforward to be a founding partner than to join later on. The View of the SRC is set out in paper MC/14/3

Executive Summary

1. A Credit Union for Clergy and Church employees.

1.1 Churches' Mutual Credit Union (CMCU) will be a savings and loans cooperative. Members save regularly and build up a pool of savings from which loans are made to those wishing to borrow. There are now 350 credit unions in the United Kingdom serving more than 1,000,000 members. Credit Unions are 'mutuals' owned and controlled by their members.

2. The Vision for CMCU.

2.1 Clergy are an ideal group to form a mutual society. They live on modest and relatively fixed incomes throughout their working life. They often need to borrow for major purchases such as cars, and need to save for retirement when they lose the benefit of job-related accommodation. Those who do not inherit property need to fund a property with a mortgage. This mix of savers and borrowers lends itself well to the credit union business model. The Short-Term vision (first 4 years) for CMCU is to build a sustainable business by concentrating membership recruitment amongst clergy and church employees who can transact with the credit union through payroll deduction thereby keeping operating costs to a minimum.

2.2 The Medium Term vision (years 5-8) for CMCU is to extend membership to all active church members thereby extending the reach, scope and scale of the business.

2.3 The Long-Term vision is to encourage membership from parishes and other church charities as 'corporate members'. Provided trustees are prepared to join CMCU and stand as guarantors of loans to their church, the credit union will be able to function as a cheap source of finance for mission.

2.4 In summary CMCU will provide a vehicle to enable the Church and church members to recycle their financial resources for the benefit of each other and the mission of the Church. Additionally it will raise the profile and brand image of credit unions and so reinforce the current drive by churches to support and strengthen the credit union sector.

3. The Benefits of CMCU.

3.1 CMCU will offer the following advantages:

- A discounted Car Loan scheme
- Household Loans to meet everyday needs
- Tax efficient savings accounts (ISAs)
- A Regular Savers Account to help members build their personal assets
- A Save as You Earn scheme

3.2 Collectively the Church of England (CoE) and the other participant Churches are a major 'employer' of people who tend to sign up for one or two decades, or a lifetime, of service for the most part on reliable but fixed and modest incomes. The financial challenges for clergy households reliant on the stipend can be considerable, with little spare income to deal with emergencies or make larger purchases.

3.3 An occupational credit union enables members, through the effortless mechanism of payroll deduction, to save even very small amounts on a regular basis. By virtue of being saving members, whenever the need to borrow arises, members are entitled to apply for a loan at a fair interest rate knowing that CMCU fully understands their financial circumstances.

3.4 CMCU will enable the participant Churches, without long-term subsidy, to make available this financial management tool to their entire 'workforce' at a minimal cost to themselves.

4. Strategic Fit: Common Tenure.

4.1 A new form of tenure for CoE clergy office holders took effect from February 2011. Common tenure provides for additional employment rights, including rest breaks, annual leave and a statement of terms and conditions, but it also emphasises clergy financial independence. CMCU can support this process, as it is legally obliged to:

- Promote thrift amongst its members by encouraging them into the savings habit.
- Offer loans at a *fair* and *reasonable* rate of interest.
- Educate its members in the wise use of money and their financial affairs.

Additionally it will:

- Contribute towards the economic regeneration of the wider community and help raise the profile and image of credit unions.

4.2 Whilst incumbents will continue to have formal legal ownership of the parsonage, upon retirement, many will have to find alternative accommodation in the wider market. Recent consultations around clergy retirement housing and pensions have been given new urgency by the banking crisis and have highlighted the need for clergy to plan for their retirement needs throughout their working lives. CMCU is actively examining the potential (once sufficient lending capital and reserves are in place) to offer mortgages for retirement housing.

4.3 This project has also arisen because of a desire of the Church Commissioners to provide their car loan scheme through another organisation. *The transfer of the vehicle loan scheme underpins this business plan and is critical to the success of CMCU.*

5. **Loan Products.**

5.1 Our Vehicle Loans will assist members wanting to purchase a car or other mode of transport and we will offer these at a discounted rate of 5.54% APR. Around 20 loans are granted each month in a scheme currently run by the Church Commissioners. The average loan is £7,000 and the total loan book is worth nearly £3.6m. Write offs are just 0.2%.

5.2 Our Household Loan at 9.38% APR (average loan size £4,500) could be used to fund other larger purchases including home improvements and educational courses. Around 10% of the loan repayment is allocated to a savings account to encourage members to develop the saving habit, put them in control of their finances and reduce their need to borrow in the future. In some circumstances a household loan can be used to help borrowers rationalise and consolidate their credit commitments, by re-ordering their finances at lower rates of interest and thus reduce their current credit spend. Other smaller loans at higher rates of interest will also be offered.

6. **Savings Accounts.**

6.1 CMCU will offer instant access, limited access and tax efficient savings accounts. A supporters' bond will be offered during the first three months of operation which will require a minimum investment of £2,000. Some ISAs will be lump sum deposits and a Regular Savers (Instant Access) Account will prove attractive for those who want to make regular payments in the knowledge that they can withdraw their savings at a moment's notice. The target dividend for all of these accounts varies from 0.5% to 2.5%.

6.2 After CMCU has been trading for an initial start-up period the aim is to apply to the FCA/PRA for permission to offer interest-bearing accounts. This will enable the credit union to pay a guaranteed return for ISAs and bond accounts and a smaller return for instant access accounts. *Capitalisation through shares is a critical success factor if CMCU is to meet the demand for car loans that are currently being granted at a rate of one per day.*

7. Regulation.

7.1 Credit unions are authorised by the Prudential Regulation Authority (PRA) and regulated by the Financial Conduct Authority (FCA). Deposits are protected by the Financial Services Compensation Scheme (FSCS). CMCU members can also seek redress through the Financial Ombudsman Scheme. This is a time of opportunity for credit unions with the passage of a Legislative Reform Order in January 2012 liberalising the legal context within which CMCU will be able to work. CMCU can take advantage of the new rules including:

- Attracting investment from corporate members, through the purchase of deferred shares to support CMCU's initial capitalisation.
- Offering a new range of interest-bearing accounts.
- Liberalising the 'common bond' to enable, in addition to clergy, a wide range of different categories of member to join CMCU, including Church Charities as corporate members and employees of the Ecclesiastical Insurance Group (EIG). In due course, it is envisaged all active members of the participant churches will be able to join.

8. Key priorities.

8.1 The key priorities for CMCU during its first year of operation are to:

- Ensure the smooth transfer of the Car Loan scheme from the Church Commissioners.
- Attract sufficient savings and other investment (eg deferred shares) to meet the capital requirements of the Car Loan scheme.
- Maximise recruitment of payroll deduction members within the common bond.
- Attract further investment from church organisations and grant funders.
- Develop systems and controls to reduce the risks associated with offering new interest-bearing accounts.
- Create back office functions that keep the cost per loan low.
- Encouraging participation and involvement in the affairs of CMCU.

9. Key Risks.

Table 1: **Key Risks, Impact and Mitigation.**		
Risk	Impact	Mitigation
Insufficient capital to meet the demand for car loans.	• **Slower than anticipated loan book growth** • **Reduced levels of income** • **Financial self-sufficiency would be delayed.** • **Turned away, potentially disgruntled members.**	• **Focus on recruitment and encourage ISA transfers.** • **Quickly raise funds by offering a limited issue Founder Members Bond.** • **Open savings accounts two months before loans are offered.** • **Raise deferred shares.** • **Encourage corporate deposits.**
Insufficient funding to 'pump prime' CMCU during its first 2-3 years of operation.	• **Inability to meet FCA/PRA thresholds leading to non-authorisation.** • **Reduced operational capacity with fewer loans being offered delaying financial self-sufficiency.** • **Lack of investment in back office systems, leading to a more costly and less efficient member service.**	• **Offer a range of investment options such as deferred shares and corporate deposits.** • **Produce an investment prospectus to show the benefit of supporting CMCU.** • **Approach more Dioceses for interest free loans and / or grant support.**

10. Funding requirements.

Based on the Variables in **Table 3** (overleaf), a viable credit union can be achieved for approximately £260k grant (plus £20k in kind support for premises), £400k in deferred shares, and corporate deposits. These projections demonstrate that CMCU could be financially sustainable within three years,

(See **Table 2**).

Table 2: **Balance Sheet**						
	Start-up	Year 1	Year 2	Year 3	Year 4	Year 5
Members						
	21	**1,021**	**1,970**	**2,871**	**3,478**	**4,304**
Assets						
Tangible assets	**£40,000**	**£32,000**	**£24,000**	**£16,000**	**£8,000**	**£0**
Current assets						
Loans to individuals	**£0**	**£1,605,268**	**£3,566,590**	**£5,628,034**	**£7,249,505**	**£8,629,042**
Bad debt provision	**£0**	**-£29,941**	**-£76,752**	**-£138,337**	**-£205,238**	**-£279,163**
Cash at bank	**£577,280**	**£590,150**	**£496,106**	**£458,302**	**£562,051**	**£1,163,218**
Total assets	£617,280	£2,197,477	£4,009,944	£5,964,000	£7,614,319	£9,513,097
Liabilities						
Individuals' savings	**£29,400**	**£1,429,400**	**£2,954,925**	**£4,422,037**	**£5,495,050**	**£6,972,457**
Corporate deposits	**£0**	**£300,000**	**£650,000**	**£1,100,000**	**£1,550,000**	**£1,800,000**
Net assets	*£587,880*	*£468,077*	*£405,019*	*£441,963*	*£569,268*	*£740,640*
Credit union capital						
Reserves	**£187,880**	**£68,077**	**£5,019**	**£41,963**	**£169,268**	**£340,640**
Deferred shares	**£400,000**	**£400,000**	**£400,000**	**£400,000**	**£400,000**	**£400,000**
Total capital	*£587,880*	*£468,077*	*£405,019*	*£441,963*	*£569,268*	*£740,640*
Ratios						
Solvency	**-**	**154%**	**136%**	**135%**	**139%**	**136%**
Liquidity	**-**	**41%**	**17%**	**10%**	**10%**	**17%**
Capital / assets ratio	**-**	**21%**	**10%**	**7%**	**7%**	**8%**
Bad debt	**-**	**2%**	**2%**	**2%**	**3%**	**3%**
Corporate deposits	**-**	**17%**	**18%**	**20%**	**22%**	**21%**
Operating costs	**-**	**8%**	**6%**	**5%**	**5%**	**5%**

Table 3: Variables						
	Start-up	Year 1	Year 2	Year 3	Year 4	Year 5
Total potential members	**21**	**50,000**	**50,000**	**50,000**	**50,000**	**50,000**
Penetration rate	**0%**	**2%**	**2%**	**2%**	**1.5%**	**2%**
Staffing FTE	**1**	**1.7**	**1.7**	**1.7**	**1.9**	**2**
Marketing costs per member	**£1,000**	**£10**	**£10**	**£5**	**£5**	**£5**
Grants required	**£260,000**	**£0**	**£0**	**£0**	**£0**	**£0**
Deferred shares required	**£400,000**	**£0**	**£0**	**£0**	**£0**	**£0**
Deferred shares dividend	**0.5%**	**0.5%**	**0.5%**	**0.5%**	**0.5%**	**0.5%**
Other dividends	**1.75%**	**1.75%**	**1.75%**	**1.75%**	**2%**	**2.25%**
Return on CU investments	**1%**	**1%**	**1%**	**1%**	**1%**	**1%**
Average saving per saving member	**£2,000**	**£2,000**	**£2,000**	**£2,000**	**£2,000**	**£2,000**
% of members saving	**70%**	**75%**	**77%**	**79%**	**81%**	**70%**
Inflation rate	**3%**	**3%**	**3%**	**3%**	**3%**	**3%**

11. Corporate Deposits and Deferred Shares

11.1 During the first five years of operation the demand for loan capital to fund car loans is predicted to be higher than the value of shares held by CMCU. This additional lending capital will be raised through corporate deposits and deferred shares.

11.2 The business model seeks to raise £1.8m of corporate deposits so it can meet demand for loans and FCA/PRA liquidity requirements. There are currently millions of pounds of parish cash deposits with CCLA earning 0.5%, CMCU will offer a better rate so it is anticipated most of the corporate deposits will come from Parishes. If the depositor's turnover is under £6.5m, the balance sheet is not worth more than £3.26m and the number of employees does not exceed 50, they will generally be covered by the Financial Services Compensation Scheme (FSCS). There is capacity within the model to take additional corporate deposits if liquidity becomes a problem but equally, if CMCU raises more than £400k in deferred shares, less corporate deposits will be required.

11.3 Deferred shares cannot be withdrawn. These are not covered by the FSCS and, in the event of CMCU being wound up, would only be repaid after all other shareholders and creditors. For this reason they count as reserves and help to improve CMCU's capital to assets ratio. It is essential that this ratio is above 5% so that the credit union can exercise greater flexibility in terms of offering higher value and longer-term loans. A capital to assets ratio of 5% is required if CMCU is to offer variable dividends or interest bearing shares.

11.4 Deferred shares will attract a target dividend of 0.5% and corporate deposit holders a target dividend of 1%.

12. Methodist Church involvement

12.1 The Church of England has asked the Methodist Church, as a covenant partner, if it would be interested in participating as a partner in the CMCU. Our understanding is that for regulatory reasons it will be much more straightforward to be a founding partner than to join later on.

12.2 There would be two aspects to this – financial input and inclusion of certain Methodists within the defined group that is eligible for membership.

13. **Financial Input**

13.1 The Church of England has made it clear that this is not the primary reason for inviting the MCB's involvement. Whilst Methodist participation is not dependent on it, clearly some form of financial commitment would demonstrate a shared sense of ownership and would provide a legal stake.

13.2 After some discussion with the President of the CMCU, the following are recommended:-

a) A non-returnable grant of £30,000 towards the set up costs of the CMCU. Although the set up costs of £260,000 are covered, there is no margin for comfort at all and this additional £30,000 would provide a little more room for manoeuvre, particularly if the initial forecast levels of business are not achieved. This grant could be paid from the CPF outside of the budget.

b) An investment in deferred shares of £100,000. As outlined in the Executive Summary above, these count as reserves and help to improve CMCU's capital to assets ratio. It is essential that this ratio is above 5% so that the credit union can exercise greater flexibility in terms of offering higher value and longer-term loans. A capital to assets ratio of 5% is required if CMCU is to offer variable dividends or interest bearing shares, so boosting this from the currently committed £400,000 would significantly boost the opportunities for growth. Deferred shares will attract a target dividend of 0.5% but are not covered so would be lost of CMCU went into liquidation. These would be held as an asset on the Methodist Council balance sheet, so could be invested from the Epworth Fund which is generally held as being used to support new and innovative work.

14. **Methodist Membership of the CMCU**

14.1 It is important that membership of this union does not undermine the valuable work carried out by local credit unions. Membership of this union must not in any way serve to detract attention from local credit unions, neither must it in any way encourage people join a national credit union at the expense of leaving or ignoring more local Unions. To that end it is proposed to limit Methodist membership to a more restrictive group than would be the case for Anglicans and to make it available only to those who are required to be itinerant.

14.2 Methodist Admission to membership of the Credit Union would be restricted to;

presbyters and deacons in Full Connexion with the Conference,
those who are recognised and regarded as being in Full Connexion with the Conference.

14.3 The Common bond qualifications for membership for Anglicans will be as follows;

Admission to membership of the Credit Union is restricted to:

a) an individual who is associated with other individuals through being a baptised member of the Anglican Churches of Great Britain or the Church of Scotland and;

   i) is ordained or in training for ordination, or;
   ii) is a lay-person licensed to minister, or;
   iii) is a trustee of an Anglican Church or Charity, or;
   iv) is a trustee of a Church of Scotland Church or Charity

b) a body corporate, an individual in his/her capacity as a partner in a partnership, an individual in his/her capacity as a member of the governing body, if the body corporate, partnership or unincorporated association is;

   i) an Anglican Church or Charity
   ii) a Church of Scotland Church or Charity

c) an individual who is employed by an employer in the following group:

   i) Anglican Churches and Charities
   ii) Church of Scotland Churches and Charities

d) an individual who is employed by the following employer:

   i) Ecclesiastical Insurance Group (EIG) plc

e) an individual who is a member of the same household as, and is a relative of, an individual who is a member of the credit union and falls directly within a common bond specified above

*****RESOLUTION**

4/1. The Council agrees to become a partner to the Churches' Mutual Credit Union with those being eligible for membership set out in para 14 and the Council's financial support set out in para 13.2 a) and b).