RESERVE BANK OF NEW ZEALAND
TE PŪTEA MATUA

# Review of mortgage bond collateral standards

## PART C

## Draft Practice Guide

November 2017

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## Part C: RMO Draft Practice Guide

1. Part C provides technical detail on the proposed implementation of Residential Mortgage Obligations (RMOs). While Part C contains no specific questions, the Reserve Bank welcomes responses on any part of this document.

2. The information in Part C also describes key determinants with regard to the behaviour of the RMO Valuation Model.

### 5.1 Key technical definitions

3. Model legal documentation would be developed at a later date based on the final RMO standard. The definitions in Part C would be used as a basis for model legal documentation. A glossary of selected terms is included at the end of this document.

#### 5.1.1 Eligible securities

4. In general, a Residential Mortgage Trust (RMT) may issue AA-Notes, AB-Notes and Capital-Notes denominated in New Zealand dollars on the Closing Date, would list all securities issued in a public market place and would maintain a register of noteholders.

5. All classes of RMO notes would be lodged and settled in NZClear.

6. The minimum Aggregate Initial Investment Amount for a given series of notes would be NZD 100 million. All note purchases would exceed a parcel size of NZD 1,000 and be in multiples of NZD 1,000 thereafter.

*AA-Notes*

7. AA-Notes would have the following characteristics:
   - 7.1 Initial Invested Amount would be between 20% and 45% of Aggregate Initial Invested Amount.
   - 7.2 Soft-bullet maturity date would be between one and two years from the Closing Date.
   - 7.3 Coupon payments would be based on a fixed rate and would be quarterly frequency.
   - 7.4 Principal payments would be trapped in the Trapped Principal Account and paid at the AA-Note soft bullet maturity date. Any AA-Note Invested Amount not paid back at AA-note soft-bullet maturity date would thereafter be paid on a pass-through basis.
   - 7.5 Principal payments would not be subject to a pro-rata trigger.
   - 7.6 AA-Notes are not callable.
   - 7.7 AA-Notes may be issued up to two times after their initial issuance.

*AB-Notes*

8. AB-Notes would have the following characteristics:
   - 8.1 Initial Invested Amount would be equal to Aggregate Initial Invested Amount less AA-Note Initial Invested Amount less Capital-Note Initial Invested Amount.
   - 8.2 Coupon payments would be either fixed or floating and would be quarterly frequency. Floating coupon payments would be based on a floating rate of OIS3m + spread.
   - 8.3 Principal payments would be made on a pass-through basis.

8.4 Principal payments may be subject to a pro-rata trigger.
8.5 AB-Notes are callable.
8.6 AB-Notes may not be issued again after their initial issuance.

*Capital-Notes*

9. Capital-Notes would have the following characteristics:
   9.1 Initial Invested Amount would be between 10% and 35% of Aggregate Initial Invested Amount.
   9.2 Coupon payments would be based on a floating rate of OIS3m + spread and would be quarterly frequency.
   9.3 The spread paid on Capital-Note coupons is currently modelled with a cap of three times the spread paid on AB-Notes.
   9.4 Principle payments would be made on a pass-through basis.
   9.5 Principle payments may be subject to a pro-rata trigger.
   9.6 Capital-Notes are not callable.
   9.7 Capital-Notes may not be issued again after their initial issuance.

*Coupons*

10. Coupons are paid:
    10.1 when the Stated Amount of the note is positive at the start of the period. If the Stated Amount for a note becomes positive after having been zero, then coupon payments would resume.
    10.2 based on the principal outstanding at the start of the period.
    10.3 in arrears with a quarterly frequency.
    10.4 on the Distribution Date.
    10.5 with actual/365 day-count basis.
    10.6 with no ex-coupon period.

11. Unpaid coupons:
    11.1 accumulate, except when the Stated Amount is zero, and can be paid at a future Distribution Date.
    11.2 do not accrue interest.

*Step-up coupon rate*

12. On the first Distribution Date that a call option is not exercised when there is the right to do so, the coupon rate on all outstanding notes would increase by a minimum of 0.25% pa for each note class. The coupon step-up amount would be specified ahead of the Cut-Off date.

*Call Option*

13. The majority of Capital-Note holders have the right to exercise the notional-based call at any Distribution Date where the mortgage loan pool notional is less than 10% of the initial mortgage pool notional.

14. If exercised, the Originator would pay to the RMT the fair market value of each mortgage loan, and the Originator would regain control of the mortgage loans after the settlement

date. The fair market value must not be less than all current period accrued coupon and outstanding principal amounts plus all senior costs, swap payments and breakage costs.

*Waterfalls*

15. Four waterfalls are used to distribute funds at Distribution Dates: termination, charge-off, interest, and principal. A stylised diagram of the waterfalls is shown in section 5.3.

16. No note classes would receive principal payments in excess of the Initial Invested Amount.

*Termination Waterfall*

17. The termination waterfall is run when a call option is exercised, at legal final maturity, when a RMT Capital Centre is liquidated by majority note holder vote, or when principal outstanding across all note classes is less than $1 per note class. The termination waterfall distributes the following amounts:
    - 17.1 Scheduled interest payments.
    - 17.2 Net receivable swap amounts.
    - 17.3 Scheduled principal payments.
    - 17.4 Prepayments.
    - 17.5 Trapped Principal Balance.
    - 17.6 Principal recoveries.
    - 17.7 Interest recoveries.
    - 17.8 Liquidity Reserve Balance.
    - 17.9 Capital Reserve Balance.
    - 17.10 Trust Reserve Balance.
    - 17.11 Fair market value for the sale of the Mortgage Loan Pool.

18. Payment at each Distribution Date would be made in the following order of priority:
    - 18.1 Taxes, fees and expenses.
    - 18.2 Swap payments and breakage costs.
    - 18.3 Current and unpaid coupon payments to AA-Notes and AB-Notes on a pari passu basis in proportion to their coupon payments due.
    - 18.4 Reimburse carry-over charge-offs to AA-Notes and AB-Notes on a pari passu basis in proportion to their carry-over charge-offs.
    - 18.5 Principal payments to AA-Notes.
    - 18.6 Principal payments to AB-Notes.
    - 18.7 Conditional current and unpaid coupon payments to Capital-Notes.
    - 18.8 Conditional reimburse carry-over charge-offs to Capital-Notes.
    - 18.9 Conditional principal payments to Capital-Notes.
    - 18.10 Unit Holder or Charity.

19. Following running of the Termination Waterfall, the RMT would have no obligation to make any future payments to any note classes.

*Charge-off Waterfall*

20. The charge-off waterfall allocates mortgage loan write-offs. Mortgage loans are to be written off based on NZ IFRS 9 definitions.

21. Before charging-off any note, mortgage loan write-offs are reduced by:

21.1 Drawing from the Principal Deficiency Ledger until the balance is zero.
21.2 Drawing from the Capital Reserve until the balance is zero.
21.3 Drawing from the Trust Reserve Account balance until the balance is zero.

22. The Principal Deficiency Ledger captures over collateralisation. An example where this may occur is when a loan write-off generates a Capital Reserve draw of equal size. Once the defaulted loan is worked-out, a recovery amount would also be paid through the principal waterfall, which creates over collateralisation. This creation of an excess of RMT assets over liabilities means that loan write-offs in future periods may be offset by drawing from the Principal Deficiency Ledger.

23. A Capital Centre is eligible to draw on the Trust Reserve Account when the Capital Reserve Balance of the Capital Centre is zero.

24. When a RMT has multiple Capital Centres that are eligible to draw from the Trust Reserve Account, the available funds in the Trust Reserve Account would be applied pro-rata to each Capital Centre based on the outstanding principal for each note series.

25. Thereafter, Notes would be charged-off in the following order of priority:
25.1 Capital-Notes.
25.2 AB-Notes and AA-Notes on a pari passu basis in proportion to their Stated Amount. For AA-Notes, the Stated Amount is reduced by the Trapped Principal Balance.

*Interest Waterfall*

26. The interest waterfall distributes the following cash flows:
26.1 Scheduled interest payments (including delayed interest payments).
26.2 Swap net receivable swap amounts.
26.3 Principal draw.
26.4 Liquidity Reserve draw.

27. Interest Payments would be made in the following order of priority:
27.1 RMT taxes.
27.2 Senior fees.
27.3 Trustee Fee.
27.4 Security Trustee.
27.5 Trust Manager.
27.6 Registrar.
27.7 Paying Agent.
27.8 Servicer.
27.9 Back-up Servicer.
27.10 Swap payments and breakage costs.
27.11 Current and unpaid coupon payments to AA-Notes and AB-Notes on a pari passu basis in proportion to their coupon payments due.
27.12 Replenishment of any Principal draws.
27.13 Replenishment of any Liquidity Reserve draws.
27.14 Reimburse carry-over charge-offs to AA-Notes and AB-Notes on a pari passu basis in proportion to their carry-over charge-offs.
27.15 Reimburse carry-over charge-offs for Capital-Notes.
27.16 Current and unpaid coupon payments to Capital-Notes.
27.17 Capital Reserve deposit.

27.18 Trust Reserve deposit.

*Principal Draw*

28. If there are insufficient funds to pay taxes, senior fees, swap payments and break costs and AA- and AB-Note current and unpaid coupons in full, a principal draw would be made to cover this liquidity shortfall. This principal draw is made even if the Stated Amount of either AA- or AB-Notes is zero.

29. A carry-over Principal Draw would be replenished until the Principal Draw balance returns to zero.

*Liquidity Reserve Draw*

30. Following a Principal Draw, if there are insufficient funds to pay taxes, senior fees, swap payments and break costs and AA- and AB-Notes current and unpaid coupons in full, a Liquidity Reserve draw would be made to cover this liquidity shortfall. This Liquidity Reserve draw is made even if the Stated Amount of either AA- or AB-Notes is zero.

31. The Liquidity Reserve balance would be reimbursed when the balance is less than 1.0% of the initial mortgage loan pool balance.

*Principal Waterfall*

32. The Principal waterfall distributes the following cashflows:
    32.1 Scheduled Principal Payments.
    32.2 Principal prepayments.
    32.3 Trapped Principle Balance.
    32.4 Principal and interest recoveries.
    32.5 Principal Draw replenishment.
    32.6 Charge-off reimbursements.
    32.7 Capital Reserve draw.
    32.8 Trust Reserve draw.

33. Principal payments would be made with the following order of priority:
    33.1 AA-Note.
    33.2 AB-Note.
    33.3 Capital Note.
    33.4 Unit Holder/Charity.

*Trapped Principal Account*

34. The Trapped Principal Account would collect principal payments for the AA-Note class and would be invested into RMT eligible liquidity assets. At the AA-Note soft bullet maturity date, the balance of this account would be paid into the Principal Waterfall. After the AA-Note soft bullet maturity date, no funds would enter this account, unless the mortgage loan pool is subsequently replenished and new AA-Notes are issued.

*Pro-rata Trigger*

35. Principal payments would automatically and permanently change from sequential to pro-rata if the conditions following are met:
    35.1 AA-Notes have been paid back in full.
    35.2 Aggregate outstanding principal is less than 20% of the Aggregate Initial Invested Amount.
    35.3 Aggregate outstanding principal is less than double the amount of Capital-Note Initial Invested Amount.
    35.4 There are no Capital-Note carry-over charge-offs.

36. Pro-rata means all note classes rank pari passu for principal payments, with the Unit Holder or Charity continuing to rank below note holders for principal payments.

*Credit Enhancement*

37. The Liquidity Reserve would have the following characteristics:
    37.1 On Closing Date, the Liquidity Reserve balance would be equal to 1.0% of the initial mortgage loan pool balance.
    37.2 The Liquidity Reserve balance would be invested in RMT eligible liquidity assets.

38. The Capital Reserve would have the following characteristics:
    38.1 The Capital Reserve balance would be zero on Closing Date.
    38.2 The Capital Reserve balance would be invested in RMT eligible liquidity assets.
    38.3 The Capital Reserve balance would be capped for each RMT Capital Centre at 1% of Aggregate Initial Invested Amount.
    38.4 Amounts above the 1% cap are transferred to the Trust Reserve.

39. The Trust Reserve would have the following characteristics:
    39.1 The Trust Reserve balance would be invested in RMT eligible liquidity assets.
    39.2 The Trust Reserve Account is paid out via the Termination Waterfall if the RMT is wound-up.

### 5.1.2 Eligible Loans

40. RMO notes are secured against a pool of residential mortgage loans (mortgage loan pool). The eligible loan criteria determine the loans that may enter the mortgage loan pool.

*Nature of Mortgages*

41. The mortgage pool holds loans originated by a single Originator. The mortgage loan pool consists of residential mortgage loans that:
    41.1 are secured on residential properties located in New Zealand.
    41.2 are not secured by unimproved bare residential land.
    41.3 are first-ranking mortgages.
    41.4 comply in all respects with New Zealand law.
    41.5 are structured to be fully amortised by a stated loan maturity of no more than 360 calendar months.
    41.6 are repayable in periodic payment streams with payment frequency no longer than monthly.
    41.7 are advanced and are repayable in New Zealand dollars.
    41.8 are advanced to New Zealand residents.

41.9 are not in-arrears on a monthly basis, are not in default, and have never been in default or been restructured.

*Moderate Balance Principle*

42. The Moderate Balance Principle would reduce any mismatch risks consistently that can arise from interest income and coupon payment divergence, open positions from existing interest rate or total return swaps, as well as extension risks.

43. The Moderate Balance Principle refers to the following principles:
    43.1 At any distribution date, the sum of scheduled interest payments generated by the mortgage loan pool and any receipts from swaps have to be equal or higher than the coupons required to pay each class of notes.
    43.2 At the issuance date, the notional amount of fixed-rate mortgage loans in the pool has to be equal or higher than the notional amount of fixed rate notes issued.
    43.3 The maturity of fixed rate loans must be equal or close to the maturity of fixed rate notes issued. Any accountable scheduled principal on mortgage loans is due and collectable within a period of 30 days before any fixed rate note payment date.

44. Any residual liquidity risks that can arise from pre-payments even if the Moderate Balance Principle is applied will be mitigated through a Principal draw or a Liquidity Reserve draw respectively.

*Portfolio Limits*

45. The mortgage loan pool would adhere to the following concentration limits:

| Limit Type | Pool-Level * | Loan-Level |
|---|---|---|
| Interest-only loan ratio | <= 20.0% | - |
| Investment loan ratio | <= 20.0% | - |
| Fixed-rate loan ratio | >= 45.0% | - |
| Remaining loan term ratio | <= 240 months | <= 360 months |
| Loan seasoning ratio | >= 720 calendar days | >= 90 calendar days |
| Borrower concentration ratio | Top 10 / 50 Obligors <= 5.0% / <= 15.0%<br>Number of loans >= 500 | Principal amount<br>outstanding <= $1million |

* Weighted by mortgage loan outstanding balance including undrawn balances

46. Remaining loan term is the time from the Cut-Off Date to the stated maturity of the loan.

47. Loan seasoning is the time from the date the mortgage begins accruing interest to the date of the latest received payment.

48. The borrower concentration ratio is the ratio of:
    48.1 borrower unit mortgage loan outstanding balance including undrawn balances, to
    48.2 the total mortgage pool outstanding balance including undrawn balances.

49. The mortgage loan pool would adhere to the following indexed loan to value criteria:
    49.1 The notional weighted indexed loan to value ratio would be less than or equal to 60% when calculated with loan level data.
    49.2 Each loan within the mortgage pool would have indexed loan to value ratio of less than or equal to 80%.

49.3 No more than 50% of mortgage pool loan notional would have an indexed loan to value ratio of less than or equal to 60%.

49.4 No more than 30% of mortgage pool loan notional would have an indexed loan to value ratio of between 60% and 70%.

49.5 No more than 30% of mortgage pool loan notional would have an indexed loan to value ratio of between 70% and 80%.

50. Indexed loan-to-value ratio is defined as the ratio of:

50.1 the current mortgage loan outstanding balance including undrawn balances, to

50.2 the value of underlying collateral at the time of origination, unless the value had been updated based on an independent valuation.

*Replenishment*

51. The mortgage loan pool can be replenished either once or twice after Cut-Off Date. The Issuer must make any Replenishment Date(s) publically available before the Closing Date.

52. At each Replenishment Date:

52.1 The RMT would issue AA-Notes only.

52.2 AA-Notes would be issued via auction in the same manner as the initial note issuance.

52.3 The mortgage loan pool must increase by the same amount as AA-Note Invested Amount.

52.4 The portfolio of loans added to the loan pool must match the credit quality standard of the better of:

52.4.1 the eligible loan criteria, or

52.4.2 the credit quality of the existing portfolio as at the last reporting date, measured against the eligible loan criteria limit types.

52.5 The Moderate Balance Principal must still be adhered to by the Mortgage Loan Pool including any new loans added to it.

*Transfer of Mortgage Loan Pool and rights*

53. On the Assignment Date, the RMT would take equitable assignment of the mortgage loans in the mortgage loan pool. The Security Trustee would hold at the Closing Date irrevocable power of attorney to perfect the title of all mortgage loans in the mortgage loan pool. Circumstances where the RMT may choose to perfect the title include:

53.1 When the Originator is the Servicer and there is a servicer default event.

53.2 When the Originator is the Swap Counterparty and fails to make full payment.

53.3 When the Originator falls below a BBB+ rating, or equivalent rating, issued by more than one external credit rating agency.

53.4 When the Originator is in administration.

### 5.1.3 Risk retention

54. At Closing Date, the Originator will hold 100% of Capital-Notes issued. The Originator may not sell any of the Capital-Notes other than to the RMT after a call option has been exercised and all AB-Notes principal has been repaid in full.

### 5.1.4 Repo-eligibility

55. The Reserve Bank will assess applications for repo-eligibility of RMO notes based on criteria outlined in the RMO rule book.

56. Any change to the RMO rule book will not affect the repo-eligibility status of existing RMO notes, including AA-Notes issued under replenishment.

57. RMO note issuance subsequent to any changes to the RMO Rule Book will have to comply with the changes to the RMO rule book.

58. The Reserve Bank will only consider applications for repo-eligibility of AA-Notes and AB-Notes. Capital-Notes will not be considered for repo eligibility.

59. The Reserve Bank will only consider applications for repo-eligibility for notes issued by RMTs under the RMO model legal documentation.

60. Mortgage Bonds other than RMO or Covered Bonds issued in New Zealand dollars would not be repo-eligible securities after the transition period ends.

*Haircuts*

61. The haircuts for AA-Notes and AB-Notes will be based on
    - 61.1 the Reserve Bank’s calculation of the notes’ Weighted Average Life (WAL)
    - 61.2 the proportion of notes in that issuance that was placed in the market
    - 61.3 the notes being pledged are listed and are quoted
    - 61.4 secondary market activity has been observable.

62. The share of RMO notes issued and retained would determine the actual haircut applied.

63. Market placement means notes are sold
    - 63.1 via an auction process at arm’s length to a third-party
    - 63.2 this third party is legally and financially independent from the Originator
    - 63.3 this third party is neither directly nor indirectly controlled by the Originator
    - 63.4 this third party is not a subsidiary of the Originator.

64. Private placements and over the counter trades would not qualify as market placements.

65. Eligible parties would be informed of the haircuts applying to their RMO-series of notes. The haircuts for series of RMO would otherwise be available from the RBNZ website.

*Listed and quoted*

66. Listed and quoted means that the Originator of each note class would make available daily bid and offer quotes for each RMO note class for each series on issue.

*Base fee and risk premium*

67. The base fee and risk premium (if applicable) will be paid at the 1st business day of each month based on the principal outstanding.

**5.1.5 Information disclosure**

68. An Originator would have to certify through the information memorandum that there is no information withheld.

*Central data repository*

69. All data in relation to RMO will be delivered, stored and serviced through a central data repository. The provider of the data repository services will make relevant data available to interested parties or the public.

70. Loan-level data for the mortgage pool may only be delivered using the loan-level template format provided as part of model legal documentation.

71. If an Originator agrees to provide information additional to the information memorandum or offering circular, the information would be made available to all parties and all relevant data would be made available via the central data repository.

*Initial disclosure requirements*

72. At the day of offering a new series of notes and updating this information immediately and as required before the Closing Date the RMT will make the following information available:
    - 72.1 mortgage performance history data for each of the mortgage loan products in the mortgage pool on a monthly basis for the preceding five years for loans that met the Eligible Loan Criteria at origination and were based on similar origination standards.
    - 72.2 mortgage performance history data split by mortgage loan product type for their:
        - 72.2.1 Constant prepayment rate (CPR).
        - 72.2.2 Delinquency rates split into current, 0-30 days, 31-60 days, 61-90 days, 91+ days.
        - 72.2.3 Default rates.
        - 72.2.4 Realised loss rates.
        - 72.2.5 Detail of any material change in underwriting standards implemented.
    - 72.3 Prospectus and Information Memorandum.
    - 72.4 Name of RMT.
    - 72.5 Name of Security Trustee.
    - 72.6 Name of Originator.
    - 72.7 Name of Servicer.
    - 72.8 Name of Back-up Servicer.
    - 72.9 Name of Unit Holder.
    - 72.10 Name of Charity.

72.11 Name of swap counterparty and swap details, including initial swap notional size, fixed leg rate, floating leg spread, floating leg benchmark rate, floating leg payment frequency and fixed leg payment frequency.
72.12 Term sheet, including for each note class: Initial Invested Amount, issue price, ISIN, and coupon rates and spreads.
72.13 Important dates (Closing Date, Cut-Off date, legal final maturity).
72.14 Details of the number of AA-Note replenishments and the intended dates.
72.15 Details of initial share of market placement and retention of the notes.
72.16 Loan-level data for the mortgage pool based on the loan level template format.
72.17 Summary of the mortgage loan products included in the mortgage loan pool, including any special features that may affect the cash flows to investors, such as the ability for the mortgagor to skip payments and capitalise the missed payment.
72.18 The Originator’s verification process for the:
72.18.1.1 mortgagor’s application details
72.18.1.2 mortgagor’s ability to repay the loan
72.18.1.3 valuation of the collateral.
72.19 Relevant information in relation to the moderate balance principle requirements of eligible loans and eligible securities’ maturities and maximum invested amounts.

*Ongoing disclosure requirements*

73. The stratified or aggregate data would be provided for the latest month and period to date since Cut-Off Date:
73.1 delinquency rates split into current, 0-30 days, 31-60 days, 61-90 days, 91+ days.
73.2 mortgage loan scheduled principal payments.
73.3 mortgage loan prepayments.
73.4 mortgage loan scheduled interest payments.
73.5 principal recovery amount net of recovery cost.
73.6 interest recovery amount net of recovery cost.
73.7 default amount (mortgage balance and number of loans).
73.8 loss given default rate for loans that received final recovery amounts.

*Notes*

73.9 Initial Invested Amount, current Invested Amount, Stated Amount and Bond Factor.
73.10 Principal paid to each note class.
73.11 Trapped Principal Account deposit and balance.
73.12 Coupon paid to each note class, including for each note class:
73.12.1 the coupon rate separated into the OIS3M rate and spread, or the fixed rate.
73.12.2 the payment amount required for full payment of current coupon.
73.12.3 any current period and carry-over unpaid coupon amount.
73.13 Charge-off amount for each note class.
73.14 Carry-over charge-off for each note class.

*Triggers*

73.15 Current pool factor relative to the threshold for principal pro-rata payment
73.16 Current pool factor relative to the threshold for notional-based call option
73.17 Information if the notional-based call option has been exercised
73.18 Current ratings of the servicer and the swap provider relative to rating triggers
73.19 Current assessment of any other third party relative to documented requirements.

*Credit Enhancement*

73.20 Principal Draw amount.
73.21 Principal Draw replenishment.
73.22 Unreimbursed Principal Draw balance.
73.23 Liquidity Reserve balance.
73.24 Liquidity Reserve balance as a percentage of initial mortgage loan pool balance.
73.25 Liquidity Reserve draw amount.
73.26 Liquidity Reserve replenished amount.
73.27 Capital Reserve balance amount.
73.28 Capital Reserve balance amount as a percentage of initial pool balance.
73.29 Capital Reserve draw amount.
73.30 Capital Reserve deposit amount.
73.31 RMT Reserve Account balance.
73.32 RMT Reserve Account draw.
73.33 RMT Reserve Account deposit.

*Swaps*

73.34 Name of swap counterparty.
73.35 Swap notional size.
73.36 Frequency of fixed leg payments.
73.37 Frequency of floating leg payments and floating leg index reference.
73.38 Margin on floating rate leg.
73.39 Coupon on fixed rate leg.
73.40 Swap payments made by the RMT.
73.41 Swap payments received by the RMT.
73.42 Swap breakage and other costs paid by the RMT.

*Senior Fees*

73.43 Total senior fees and expenses paid.
73.44 Payment to Unit Holder.
73.45 Payment to Charity.

*Loan Servicing*

73.46 Detail any change in underwriting standards implemented in that month.
73.47 Detail any change in servicing standards implemented in that month.
73.48 Current information in relation to the moderate balance principle requirements of eligible loans and eligible securities' maturities and maximum invested amounts.

### 5.1.6 Loan servicing requirements

74. Loan servicing requirements refer to loan underwriting and loan servicing standards such as the processing of claims, credit administration, debt collection and work out services.

75. In general, all mortgage loan credit administration and workout services will adhere to high standards, be documented in respective service level agreements and be carried out by qualified staff, and be conducted free of any conflict of interest.

*Servicer*

76. The Servicer or Back-up Servicer would service the mortgage loan pool in the interests of the note holders. Any Servicer or Back-up Servicer would:
    76.1 service all loans in accordance with Originator's servicing guidelines or guideline changes as notified to and agreed with the Security Trustee as being insignificant.
    76.2 have employees with a minimum of five years of experience in administering and servicing residential mortgage loans in New Zealand.

*Back-up Servicer*

77. The RMT must ensure that there are contractual provisions in place for a Facilitator to takeover servicing the mortgage loan portfolio at any specified point in time. Contractual provisions must include the identification and ring-fencing of the Servicer's qualified servicing staff.

78. The RMT may direct the Facilitator to replace the Servicer if:
    78.1 The Servicer's senior unsecured debt is downgraded more than three notches from the level prevailing at Closing Date by one of the external rating agencies.
    78.2 For any reason at the RMT's discretion.
    78.3 At any time when at least 75% of noteholders vote to replace the Servicer with the designated or another Back-up Servicer.

**5.1.7 Other fiduciary requirements**

79. Any RMT is a special purpose vehicle that is legally separate and bankruptcy remote from the Originator's balance sheet under New Zealand Law. It is a special purpose trust (SPT), a portfolio investment entity operated on a trust basis (PIE), or a special purpose entity (in cases where there is only one series issued through it).

80. RMTs would be chartered to comply with relevant Trust legislation under New Zealand law. The Trust Manager and Security Trustee would have at least five years experience in conducting fiduciary services in New Zealand.

*Capital Centres*

81. Any Capital Centre is constituted by owning a single mortgage loan pool from a single Originator, and by owing a default capital structure as specified. The assets and liabilities of a given Capital Centre are held separate from the assets and liabilities of another Capital Centre within a RMT, except in cases where Trust Reserve Account might be shared for capital loss purposes.

*Security Trustee*

82. A Security Trustee would be appointed and would hold security interest over the loan pool for a given Capital Centre in accordance with a Security Trust Deed. If there is any conflict of interest, the Security Trustee must give priority to the interest of noteholders:
    82.1 On a pari passu basis, for AA-Note holders and AB-Note holders.
    82.2 Only thereafter, for Capital-Note holders.

*Interest rate swap counterparty*

83. To adhere to the Moderate Balance Principle an RMT must mitigate material interest rate risk by entering into interest rate swaps under an ISDA agreement. The counterparty to the interest rate swap may be the Originator or another qualified third party.

## 5.2 RMO Valuation Model

84. The RMO Valuation Model has been developed for the Reserve Bank by Eticore Operating Company Pty Limited (the Developer). The RMO Valuation Model represents one potential solutions to model, assess and value a mortgage bond product like RMO.

*Disclaimer*

85. The RMO Valuation Model is a trial product and is not currently used in the Reserve Bank's market operations. The RMO Valuation Model is being made available for informational purposes only and is not meant to be used in a commercial context.

86. The Reserve Bank and the Developer make no representations or warranties, express or implied, as to the reasonableness of the assumptions or the quality, accuracy or completeness of the RMO Valuation Model and do not undertake to update the model.

87. The RMO Valuation Model is meant to support public information about RMO securities. The Reserve Bank and the Developer do not offer financial, rating, or risk assessment advice and the RMO Valuation Model should not and cannot be relied upon as such.

*Available downloads*

88. The RMO Valuation Model can be downloaded from the Reserve Bank website, along with a User Guide. The cash flow model underlying the RMO Valuation Model is a prototype replicating the majority of functionality outlined in this consultation document.

89. By downloading the RMO Valuation Model from the Reserve Bank's website you agree that neither the Reserve Bank nor the Developer shall be liable for any losses, costs, expenses or damages (incidental, special, consequential, compensatory or exemplary) arising directly or indirectly out of the use of or reliance on the RMO Valuation Model.

*User guide*

90. The RMO Valuation Model 'User Guide' holds respective links to excel templates that the user can populate to operate the model and upload loan level data.

91. There are some modelling limitations in the RMO Valuation Model, some of which represent inconsistencies with the Standard, and these are listed below:
    - 91.1 AB-Notes can only be modelled having a floating coupon rate.
    - 91.2 Capital-Notes are called when a call is exercised.
    - 91.3 A date-based call option is included for illustration.
    - 91.4 Loan write-offs are written off immediately in full.
    - 91.5 Mortgage loan pool replenishment is not modelled.
    - 91.6 Deposits are made to the Trust Reserve Account, but no drawings are made.
    - 91.7 RBNZ limit checks are applied at pool and borrower unit level, and not at loan level.
    - 91.8 A check of compliance with the Moderate Balance Principle is not undertaken.

## Glossary of selected terms

**Aggregate Initial Invested Amount**: the sum of Initial Invested Amount across all note classes.

**Assignment Date**: the date mortgage loans are transferred to the RMT.

**Closing Date**: the date all mortgage loans are transferred to the Security Trustee and the RMO notes are issued.

**CPR**: Constant Prepayment Rate

**Cut-Off Date**: the date all mortgage loans are identified and the mortgage pool is finalised ahead of RMO notes being issued for the first time.

**Distribution Date**: 10th day of the month following the end of the quarter, based on:

- modified following business day convention
- Wellington and Auckland holiday calendars

**Replenishment Date**: the date all mortgage loans are identified and the mortgage pool is finalised ahead of the mortgage pool being added to.

**In-arrears**: the mortgagor has not paid their mortgage in full over the last month, irrespective of whether they are ahead of their mortgage payments due to previous over-payment.

**Initial Invested Amount**: Invested Amount at Closing Date.

**Invested Amount**: the principal amount of the note class less any principal payments made.

**Originator**: the entity that originated the loans.

**Restructured**: means the stated loan maturity has been lengthened beyond the stated loan maturity when the loan was first written.

**RMT eligible assets**: New Zealand government bonds and treasury bills, Reserve Bank reserve account, Reserve Bank bills, and RMO AA-Notes that an RMT may re-invest or hold proceeds in.

**Stated Amount**: the Initial Invested Amount less principal payments less unreimbursed principal charge-offs.

**Unit Holder**: Any entity including the Originator or RMT.

**Default**: defined as by underwriting criteria and by accounting standards, and would include:

- the mortgagor has a residential mortgage loan that is more than 90-days past due, or
- the bank has declared the mortgagor is in default, or
- the mortgagor has filed for bankruptcy.

### 5.3 RMO cash flow waterfalls

RMT Stylised Waterfalls