



TMG FINANCIAL SERVICES

COLLATERALIZED
ADVANCE PROGRAM:
Investing in the Future

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EXECUTIVE SUMMARY

The Collateralized Advance Program (CAP) is a way for credit unions of all sizes to invest in the future of the industry. Through a collateralized loan for TMG Financial Services, credit unions are ensuring that critical credit union credit card assets are staying in the industry. Without such a program, credit union credit card portfolios are being sold to large national banks that often have competing products and little interest in managing the portfolio with the credit union's interest in mind.

The following white paper explores why your participation in CAP is important. As you evaluate this program, keep in mind that extending a loan or investing in a CUSO isn't a new concept – in fact, it has been done for years with straightforward vehicles like the Collateralized Advance Program. CAP features include:

- Funding structured as a loan to a CUSO – TMG Financial Services
- Competitive cost of funds, often higher than CDs
- A one year, fixed interest rate on commitment
- A wide variety of terms and rates for funded advances
- Interest payments made semiannually
- TMG Financial Services assumes all credit and fraud losses, these costs are not “participated” or “shared” with lenders

When you choose to participate in the Collateralized Advance Program, you are joining a growing number of like-minded credit union partners. Already more than \$100 million in advances have been made to TMG Financial Services through CAP to fund the 37 purchased portfolios that serve more than 40,000 credit union members.

For additional information about TMG Financial Services or the Collateralized Advance Program, contact the marketing department at 515.457.5533.

COLLATERALIZED ADVANCE PROGRAM: INVESTING IN THE FUTURE

From the beginning, credit unions have worked for mutual success, which has created a long and rich history of collaboration and innovation.

Simply look at the wide variety of credit union service organizations (CUSOs) that exist. From auto loans to credit card processing to marketing services, credit unions have created and invested in CUSOs that provide essential products, services and returns on investment. A CUSO is often formed to create economies of scale, but more importantly, these CUSOs have created a network of business partners that have a fundamental understanding of values and practices that govern and connect credit unions regardless of geographic location.

The CAP is a unique opportunity that allows credit unions to once again work together for the common good of the industry and its members.

TMG Financial Services is no different. This CUSO was created more than two years ago as a solution for credit unions considering the sale of their credit card portfolio. But that is only part of the story. TMG Financial Services' business model also allows for collaboration among credit unions that have not (or maybe will never) sold their credit card portfolio.

The Collateralized Advance Program is an opportunity created for credit unions to invest in the future of the industry. With the funding of other credit unions, TMG Financial Services purchases credit card receivables while collaborating with the selling credit union on a member-friendly program. In return, those credit union lenders receive competitive yields based on a soundly underwritten asset.

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BACKGROUND

In 2007, TMG Financial Services was created as a separate but collaborative partner to The Members Group, a CUSO that processes and provides services for credit union credit, debit, ATM and prepaid card programs since 1987. The creation was due not only to an increasing desire by credit unions to evaluate the sale of their portfolios, but the lack of a partner who truly understood credit unions, their members and the values on which the industry is built.

Credit union portfolio partnering is not a new trend. Since the early 2000s, an increasing number of credit unions had begun investigating the potential advantages of actually selling their portfolios. For many who did sell their portfolios, the shortcomings of these partnerships became quickly evident. Sold meant the credit union couldn't make judgment calls on loyal members who might not look like a good risk on paper. It meant partnering with banks that had similar and competing products. These same partners would promise not to cross-sell, but in some cases would encourage members to make their credit card payments by coming into competing branches. In the end, the revenue from the sale did little to cover the cost of losing valuable relationships.

Even with these widespread stories, the economic realities of today's business climate have continued to push credit unions to investigate the option of selling. As margins have compressed, credit unions have had to do more with less. Marketing campaigns and employee education focused on growing accounts and balances has often taken a back seat to promoting another product or service. When this happens, the portfolio becomes stagnant and ceases to provide long-term value for the credit union.

But credit cards are a “must have” product for credit unions. Members simply expect their financial institution to provide a competitive credit card, but this doesn’t mean they will use it. Consumers -- including credit union members -- search for the best product that fits their needs, leading to fierce competition for primary credit card status. Not only are credit unions competing with the financial institution across town, but also with large global issuers who spent millions of dollars to romance cardholders with teaser rates and other short-term benefits.

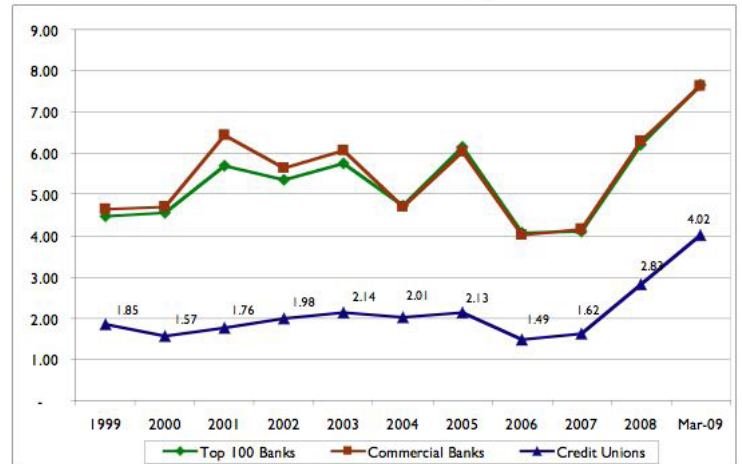
Today there is an opportunity for credit unions and their consumer-friendly credit card programs to gain market share with existing membership and new cardholders. However, this is only possible with a competitive product.

In the current climate, competitive is defined by a strong rewards program, low interest rate and reasonable fees. However, not all credit unions have the time and resources to manage that kind of program. And with the passage of the Credit Card Act of 2009, there will be additional pressure on credit union resources that will make it even tougher to be successful. This is when credit unions turn to a partner who can help.

This landscape is important to understand – because even if selling your credit card portfolio isn’t on the table for your credit union, for many others it is. And for those credit unions, it is important to have options – particularly one that aligns with credit union values.

Any given week for the past year, TMG Financial Services has had the potential to bid on credit card portfolios with varying balances from as high as \$80 million and as low as \$500,000. In fact, we estimate there are \$200 million in portfolios currently in the pipeline for evaluation. Clearly, not all of these portfolios will partner. Some credit unions are “kicking tires” and decide instead to continue managing their portfolio. Others have a processing contract in place that will delay the purchase. And, with others, TMG Financial Services will determine their credit card portfolios are not a good fit for our own portfolio. This

Bank vs. CU Charge Offs



Source: CUNA, NCUA, Federal Reserve Board Statistical Releases, all quarterly data annualized

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HIGH QUALITY ASSETS

Since early 2009, both the trade press and the mainstream media have been looking for the next financial crisis. In this search, there have been many conversations why credit cards could be the next big problem facing the financial services industry. Credit unions and their boards of directors are particularly tuned in to the risk given the unprecedented circumstances of the past year. However, because TMG Financial Services owns credit union credit card assets, the risk picture is different from that of the major issuers.

Credit unions have long subscribed to the idea that the best risk management is sound underwriting, so a majority of the portfolio owned by TMG Financial Services is “high-quality.” Accounts have reasonable credit lines and the average cardholder has a FICO score of 723.

Consider that credit unions as a whole have traditionally fared better than their bank counterparts. Typically credit union credit card charge-offs are 35%-45% of bank charge offs. This is directly related to strong risk management practices.

Additionally, as portfolios are evaluated by TMG Financial Services for purchase, there is no doubt we are starting with premium assets, however, we conduct our own due diligence as well. This includes:

Market potential. How does the portfolio match up to others we are evaluating, as well ones we've recently purchased? We look at charge-offs, delinquencies and growth to evaluate performance, and if necessary, we make adjustments to take the credit union's local economy into consideration.

Quality. Our overall portfolio has comparatively high standards (average 723 FICO score), so how does the evaluated portfolio compare?

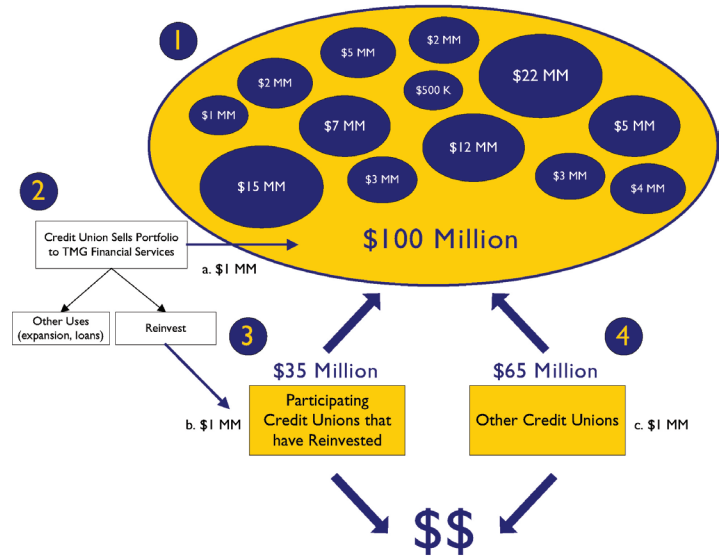
Partner fit. We look at the management team and the overall performance of the credit union. This includes understanding why the credit union is selling the portfolio, as well as future growth plans. We look for credit unions who truly seek a partnership opportunity.

In the end, we are confident that when a portfolio purchase is completed the asset is a "clean" portfolio. This means that there are no accounts more than 30 days delinquent, no suspected fraudulent activity, no pending litigation, and no pending bankruptcies.

LENDING FOR THE FUTURE

The Collateralized Advance Program offering is a unique opportunity for credit unions. It provides lending credit unions with a competitive interest rate on a loan that is collateralized by the high quality credit receivables we currently own and will be purchasing in the future.

TMG Financial Services CAP Overview



The program features include:

Loan to a CUSO. Because TMG Financial Services is a Credit Union Service Organization (CUSO), there are some regulatory limits set on how much a credit union can loan or invest. Because of the number of CUSOs that exist, credit unions need to be aware of how much, if anything, they have already extended as a loan to a CUSO. For credit unions with a Federal Charter, 1% of assets is the limit for both investments and loans to a CUSO. State-chartered credit unions are also sometimes subject to limits based on their individual states regulations. For example, in Iowa, the limit is 5% of assets, but there is no individual limit on investments or loans, the sum simply cannot exceed 5% of assets.

Credit unions interested in participating in a program like the Collateralized Advance Program or other CUSO endeavors should consult with their legal counsel to fully understand the regulations governing CUSO investment.

Competitive interest rates. During the past 12-18 months, there haven't been many safe places to put spare liquidity to work at great rates. One of the attractive features of the CAP program is the rate. TMG Financial Services re-prices the lending opportunities each month to ensure rates are competitive.

Like locking into a favorable mortgage rate, once a credit union commits to the CAP offering, the rate is locked in for the commitment period of 12 months. It is also the rate that is assigned if the advance is funded.

Advance Commitments and Funded Advances.

Because we are continually evaluating portfolios, we have a continual need for available funding. An advance commitment works like a line of credit -- we will not draw on a commitment until the portfolio purchase date is set and until we own the collateral that backs the loan. Lending credit unions receive the rate they locked in when first making the commitment.

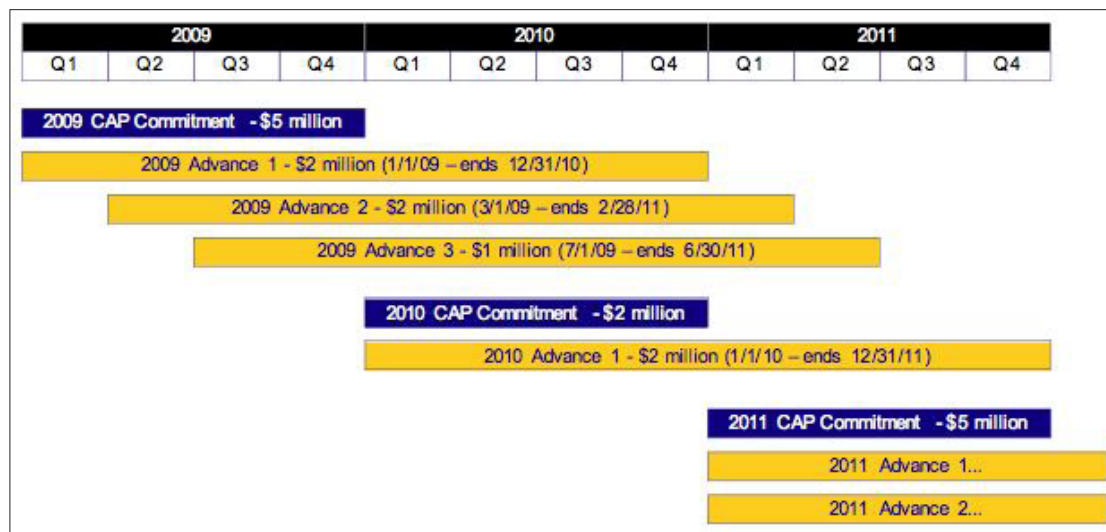
Once the Advance is funded, it is typically a two-year loan. The rate remains fixed for the term of the advance. Like a CD, a CAP Advance can be rolled upon completion of the term, but it will be reset to the current rate. There are other interest rate options available; however, they are priced according to term and on an individual basis.

Return on Investment. Semiannually, TMG Financial Services distributes interest payments on the investment.

All credit and fraud losses are assumed by TMG

Financial Services. One of the frequently asked questions is how safe is this investment, particularly with all that is being said in the media. First, these are high quality assets, which doesn't mean they are immune to loss, but the risk is much lower. Second, TMG Financial Services assumes all credit and fraud losses. Nothing is passed on to the investing credit union except the assurance of high quality assets to fully back your loan.

How does CAP work?



FINAL THOUGHTS

Even in these uncertain economic times, credit unions are thriving. They are doing so because they have found ways to collaborate and be innovative. The key lies in the ongoing efforts of credit unions investing and participating in CUSOs. For all the collaboration and innovation, it is important to remember this isn't a new idea – CUSOs have a long history of providing the credit union industry with necessary services. The opportunities provided by TMG Financial Services are no different. Participating in the Collateralized Advance Program gives credit unions the opportunity to invest in their future, as well as the future of the industry.

TMG Financial Services currently has more than \$200 million in credit card receivables in its pipeline to potentially purchase by mid-year. This is just a fraction of the available market. If you would like to learn more about partnering with TMG Financial Services and the CAP program, contact Jeff Russell, President and CEO at 515.457.5475 or jeffr@tmgfinancialservices.com.