

Schedule I

THE TAANZ BONDING SCHEME REQUIREMENTS FOR BONDING

Introduction

The success of the TAANZ Bonding Scheme is dependent upon members individually and collectively meeting their obligations at three levels.

1. Individual members (usually limited liability companies) being financially sound, well managed and respecting the special 'trust' nature of funds which they handle for clients and principals (airlines, wholesalers and others).
2. In the event of failure of a member, the shareholders or a third party honouring the required limited guarantee which they have provided to reimburse TAANZ for claims met from the TAANZ Bonding Fund.
3. The maintenance of a fund (The TAANZ Bonding Fund) which enables TAANZ to promptly meet legitimate claims. The fund is also used to cover that part of the cost of claims which for any reason cannot be recovered from the member concerned or from the guarantors.

In considering the obligations of individual members, account has been taken of the level of risk imposed, on the Bonding Fund by different categories of member. Members should refer to Attachment I to establish the category under which they come.

It has been determined that the major risks to the fund are from:

- (a) the failure of new members in the first two years of operation;
- (c) the possibility of major failure of high volume members where claims will inevitably exceed the level of guarantee available.

Accordingly extra compliance and reporting requirements apply to members in those categories. The requirements are summarised in [Attachment I](#). Further details are provided in these notes.

BONDING AUTHORITY

TAANZ recognises the personal nature of the information which it requires for bonding purposes and has appointed an independent Bonding Authority to maintain confidentiality. He/she considers the information provided by members, determines the

bonding category and requirements for each member and (subject to prior notice to the member concerned) discusses exceptional problem cases with the TAANZ Bonding Committee and/or IATA.

REQUIREMENTS TO BE MET BY ALL BONDED MEMBERS DEED OF COVENANT

Each member of TAANZ is required to execute a Deed of Covenant which acknowledges the responsibility of the member to faithfully account to the appropriate principals for all money received from clients. The undertaking which is given in signing this covenant also acknowledges the responsibility of the member, usually a limited liability company, to properly account for funds received from travel clients. The Deed of Covenant is signed by a director or directors on behalf of a company and by proprietors where no company is involved.

DEED OF INDEMNITY

Each member is required to arrange for the provision of a bond. This is to be provided in the form of a Deed of Indemnity signed by covenantors. Usually the covenantors are the shareholders or a related party. All members are required to provide security for the bond. Security can be a combination of mortgage, bank or insurance bond, or cash deposit. (further details are given later).

The Deed of Indemnity sets out the terms and conditions and limits of the amount payable to the Bonding Fund by the covenantors. Payment is required in the event of the Bonding Fund being required to meet claims from the clients or principals of the member concerned.

LEVEL OF INDEMNITY

The basic level of indemnity required is determined by a combination of the following factors:

- (a) The annual gross sales (which can be reduced by commission and qualifying credit card sales – see comment below)
- (c) The frequency of BSP payments.

The level of indemnity for any member is calculated by applying the appropriate percentage from Chart 1 below to the adjusted annual gross sales for the year under review. (For new applicants the gross sales for the first year shall be estimated).

Chart 1

BSP Reporting And Payment Cycle

Category of Member

Category A

All others

7 days 4.00% 2.66%

14 days

* 4.00%

Subject to a minimum indemnity of \$50,000 in all cases

The maximum indemnity required shall be: \$500,000 for those on 7 day reporting, \$750,000 for those on 14 day reporting

* This option not available

CALCULATION OF TURNOVER

For the purposes of determining the level of indemnity each member's turnover is calculated as follows:

1. Start with the annual gross travel business turnover of the member, i.e. the gross value of the goods and services billed as retailer, consolidator, or wholesaler. (Directors will be required to provide an annual statutory declaration of this turnover).
2. Deduct the gross value of airline services for which payment was made direct to an airline or through BSP by way of a recognised credit card. This gives "turnover for bonding purposes".
3. Deduct the amount of commissions payable to the member by principals on the "turnover for bonding purposes". Upon request members must provide the Bonding Authority with the following information within the timeframe required:

Confirmation acceptable to the Bonding Authority of the level of commissions received for the financial year under review.

Any other information which the Bonding Authority may in the circumstances require.

CLIENTS AND PRINCIPALS FUNDS

Required Practice:

All monies paid to a TAANZ member as an agent, for services to be rendered by other parties, must be kept separate from other funds (in a travel funds account) and shall be deposited or invested only with the following:

- (a) Any New Zealand registered bank and their subsidiary savings bank

(b) Trustee saving banks

(c) New Zealand Government or Local Body Investments

The only funds which can be drawn from a travel funds account are:

(1) Payment to an airline or other principal on account of the party who provided the funds.

(2) Refund to clients.

(3) Withdrawal of commission and interest earned on the relevant transactions.

(4) Temporary investment as listed above.

In essence this requirement means that a member must maintain one bank account for client travel funds. Another bank account is required for the payment of operating expenses, including shareholder drawings in anticipation of salary.

The two principal advantages are:

(1) The knowledge that client travel funds are intact and available for payment to principals; and

(2) As client monies have been separated from company funds, management will be assisted in its awareness of any unfavourable trend in its financial position from the status of the business account plus accounts receivable.

The Civil Aviation (Passenger Agents' Commission Regime) Notice 1983, together with the Passenger Sales Agency Agreement, provide that all monies received by an agent in relation to the sale of international travel by air shall be kept in a separate bank account on behalf of the principal until it is accounted for to the principal by the agent. These TAANZ requirements extend that requirement to funds received from consumers on behalf of all principals.

Directors or proprietors will be required to provide an annual statutory declaration of compliance with the above procedures. In addition the Bonding Authority can require evidence that the appropriate level of funds are held in properly designated bank accounts.

ANNUAL REVIEW

Members are required to submit an annual bonding return, including annual financial statements to the Bonding Authority no later than three months after the date of the member's annual balance. Failure to submit the annual bonding return as required in the preceding paragraph will render the member liable to suffer a fine of up to \$1,000 (plus GST) being imposed by the Board of Directors without further notice.

Failure to submit the annual bonding return within five months of the member's annual balance date will render the member liable to be lapsed by TAANZ. In the event of TAANZ taking such action it will forthwith notify IATA that the member is no longer a bonded member of TAANZ. In addition TAANZ will publish advertisements to that effect in a newspaper circulating in the district where the business is situated. The annual bonding return for each category of member shall be in a format supplied by the TAANZ Bonding Authority and approved by the TAANZ Board of Directors.

A special information booklet has been provided by TAANZ as a helpful guide to members, explaining the annual review process.

SPECIAL REVIEW

In addition to the quarterly, six monthly and the annual review the Bonding Authority shall have the power to carry out a special review of a member at any time if he considers that the member may be a risk to the bonding Scheme. Should the Board of TAANZ determine that membership be terminated the member shall have the same right of appeal as in the case of a decision not to renew membership.

FORM AND CONTENT OF ACCOUNTS

Financial statements must be in accordance with standard accounting practice and, where relevant, in accordance with the requirement of the Companies Act 1993 and the Financial Reporting Act 1993.

As a standard industry practice, the following items must be disclosed in members' financial statements, either in the accounts themselves or as notes thereto:

(a) Gross sales revenue:

Gross sales revenue will be used for the calculation of the indemnity level. However, members with substantial sales revenue other than as a travel agent may wish to advise the level of nonagent sales revenue if they consider a lower indemnity would be more appropriate to the level of risk to travel consumers and airlines.

(b) Recognition of Income Earned.

The earliest point that a travel agent may recognise income in financial statements used for Annual Financial Review calculations is:

1. When a deposit has been received, the amount of the deposit, to the extent that it covers a cancellation fee in accordance with the booking conditions.
2. The full commission value of the travel arrangement may be recognised as income when either a ticket or redeemable voucher has been issued to the customer or when

the principal has been paid. The basis of recognition of income earned must be explained in the Notes to the Accounts.

(c) Salary and other remuneration to directors and shareholders.

(d) The amount held in bank accounts and representing advance payments by clients must be separately identified.

(e) Accounts receivable to show as separate items:

- (i) amounts due from clients
- (ii) amounts due from airlines
- (iii) amounts due from shareholders
- (iv) other

If the amount shown as “other” is material, it should be fully explained.

(f) Accounts payable should show separately:

- (i) amounts due to clients
- (ii) amounts due to airlines and principals
- (iii) other trade creditors
- (iv) amounts due to shareholders

Amounts due to clients and airlines and from clients and airlines must be separately disclosed and must not be offset unless a legal right of offset exists. i.e. amounts due to one client or airline must not be offset against amounts due from other clients or airlines.

(g) State whether bank overdraft or loan facilities are secured and details of securities.

(h) Disclose nature of any encumbrances. For example if the assets of the member are used as security for third parties.

(i) Details of total commissions received.

SPECIAL REQUIREMENTS FOR DIFFERENT CATEGORIES OF MEMBERSHIP

Category A – New Members

Period in Category A

A member will be classified as a new member (Category A) for a minimum period of 18 months following admission to TAANZ membership. At least 2 “annual reviews” must be conducted during the minimum period, e.g. member joins TAANZ August 2002 with annual balance date of 31 March. New membership criteria apply for reviews based on bonding returns to 31 March 2003 and 2004.

The new membership status applies if the company or entity is applying for new membership of TAANZ. However, applicants for new membership can apply to the Bonding Authority for exemption from this requirement on the following grounds:

- (a) The new member applicant is a company or entity resulting from the merger or reconstruction or sale and purchase of established businesses conducted by members in categories B or C and
- (b) There is a continuity of senior management or Directors; and
- (c) The new member is, in the opinion of the Bonding Authority, adequately capitalised.

Capital Adequacy

New members must provide the Bonding Authority with evidence that the company or business has adequate shareholders equity (paid up capital plus retained profits and reserves) to meet reasonable commitments. The initial information required will include an “opening” statement of financial position and a budget of income and expenditure for a period of at least two financial years. In particular, the Bonding Authority needs to be satisfied that the member has adequate working capital to meet outgoings as they fall due.

A minimum shareholders’ equity of \$40,000 will be required but in many cases a larger amount will be required to cover fixed assets, working capital and also any goodwill paid for. The capital adequacy test must be met for the period of category A membership.

Remittance Period and Bonding Level

As stated under “Level of Indemnity” above, category A members must pay airlines on a 7 day reporting cycle and the initial indemnity will be 4% of estimated turnover. A minimum of \$50,000 applies.

Interim reporting requirements

Category A members are required to provide the Bonding Authority with interim financial statements covering the first 6 months of each financial year. This requirement will not apply in the first period of membership if the interim reporting period would be less than three months. The interim financial statements may be in the form of internally generated management reports but must incorporate a statement of financial position as well as operating results. The interim and annual reports must be accompanied by a directors/ proprietors declaration that the company is solvent and is properly accounting for client and principal funds.

CATEGORY B MEMBERS

Category B covers members whose adjusted turnover, as defined for bonding purposes, is less than \$10.0 million

These members are required to meet financial criteria at all times.

A special requirement for this category of member is that in addition to the annual report they must provide the Bonding Authority with an interim financial statement covering the first 6 months of each financial year. Both the interim financial statement and the annual report must be accompanied by a statutory declaration from directors that the company is solvent and is properly accounting for client and principal funds. The interim financial statements may be in the form of internally generated management reports but they must incorporate a statement of financial position as well as operating results.

CATEGORIES C

Category C covers members whose adjusted turnover, as defined for bonding purposes, is \$10.0 million or more.

These members are required to meet financial criteria at all times.

Special requirements for this category of member are:

- The provision of three monthly financial reports with a statutory declaration from directors that the company is solvent and is properly accounting for client and principal funds.
- In those circumstances where the financial statements are not subject to independent audit, an annual limited verification report from an independent chartered accountant must be supplied.

PROVISION OF SECURITY

These requirements apply to all members:

Members are required to provide security to back up the indemnity and the following alternatives may be considered by the Bonding Authority:

- (a) Security over assets (real estate, insurance policies);
- (b) A bank guarantee;
- (c) A cash deposit with the TAANZ Bonding Scheme;
- (d) Such other protection as the Bonding Authority may reasonably require.

The choice of security to be given may be made by the member involved after

discussion with the Bonding Authority. The following information may assist in this consideration.

(a) Mortgage of Real Estate:

The availability of a house property or other real estate as support for an indemnity will vary depending upon its precise ownership and it is helpful if a copy of the Certificate of Title is provided. Many applicants are unaware of the precise ownership of such properties which may be owned solely, owned jointly, owned by trustees, or be registered as a joint family home.

An independent valuer's valuation is usually required. In giving mortgages for normal lending it is customary for the valuer to make a recommendation for a first mortgage loan, normally restricted to 2/3 of his/her valuation. In taking mortgage securities the TAANZ Board has authorised the Bonding Authority to accept first, second, or even third mortgages up to 80% of the valuation. If there are existing mortgages on the property, the level of priority required by the existing mortgagee will be taken into account in assessing the equity available to the TAANZ Bonding Scheme. The costs for the security, namely valuation costs and the costs of the mortgage documentation, are payable by the member. It should be noted that these costs do not recur and can be regarded as one-off costs. Through the experience of past years it appears this form of security is the most widely used and is the least costly to members.

(b) Life Insurance Policies:

Where the policy (or policies) has an appropriate surrender value, an assignment to TAANZ may be accepted as security for the bond.

(c) A Bank Guarantee:

In the case of an indemnity or guarantee from a bank or insurance company, an annual fee is charged to the members by the bank/insurance company, and in addition most banks may require the indemnifier to give them security, probably in the form of a mortgage or real estate. If this is the case members must meet annual fees and the costs of providing a mortgage to the bank/insurance company. For most members, a mortgage direct with TAANZ under the first option would be preferable and less costly.

(d) Insurance Cover:

TAANZ may accept as security arrangements put up from time to time by insurance and/or bonding companies. These frequently involve the insurance company/bonding

company providing up to 50% of the indemnity requirement. Usually these companies provide the second 50% of the indemnity which is exposed and can only be called upon once the 50% of the indemnity provided by the shareholders has been exhausted. Members opting for this form of security have to be in a position to provide cash or other security to cover the first 50% of their bond. Invariably, the insurance company/bonding company will have its own criteria which will also need to be met by the member before this option is available.

(e) Money lodged with TAANZ:

Money deposited with the Bonding Scheme is lodged by TAANZ with a registered trading bank at the interest rate available at the time. Interest on this type of security is paid to the member without deduction, other than Resident Withholding Tax.

RELEASE FROM INDEMNITY AND SECURITY

A person who provides security and/or indemnity should be aware that the security/indeemnity will remain in place for a period of six months after the effective date of termination of that person's ongoing future liability for the activities of a member. This is because third parties have up to six months to lodge claims against the Bonding Fund.

BONDING FINANCIAL CRITERIA

Members in Categories B and C must all meet specified financial requirements. Members failing these tests will lose bonding (subject only to the TAANZ Board, on the recommending of The Bonding Authority, exercising its discretion to provide time for the member to remedy the situation). (Note: Details of the financial requirements will be advised prior to introduction of the new bonding requirements.)

LIMITED INDEPENDENT VERIFICATION

Members in Category C will be require to provide with their annual bonding returns independent verification of certain financial procedures and contents of the financial statements. (Note – details of those requirements are to be determined from time to time by the TAANZ Board, based on recommendations from The Bonding Authority.)

It is likely that in cases where the financial statements have not been subject to independent audit a report will be required from an independent chartered accountant confirming such matters as:

- (a) Bank account balances and the distribution between client/airline funds and the member's funds.

- (b) The collection of major debtors accounts subsequent to balance date.
- (c) Cut-off procedures to ensure that income is not brought into account prematurely and that there is a correct matching of income and expenditure.
- (d) That all major creditors at balance date have been properly brought into account.
- (e) That client deposits/prepayments have throughout the year been paid into a designated “travel fund” and year-end balances are properly accounted for.

Movements between Categories

The Bonding Authority has discretion to allow a member to remain in an existing category when the turnover level is within 5 percent of the upper limit of the category.

Significant Variations in Annual Turnover

Because of special events or tours etc. the turnover of some members varies significantly from year to year. In the annual bonding return members will be asked to state whether in the ensuing year the turnover level is likely to be significantly increased because of circumstances known at the time of making the return. The Bonding Authority will in some circumstances seek a higher level of indemnity for that year and treat the member as having moved to a higher turnover category.

Group Bonds

Major franchise groups or members operating under other group arrangements may wish to provide security on a group basis. The Bonding Authority and the TAANZ Board are prepared to consider proposals for group security. The main requirement will be that the proposals are backed by arrangements, which ensure that the group bond will remain intact or be replenished in the event of failure of any member of the group.

Financial Discretion

It is recognised that the different interpretations of financial accounts are possible and do occur. Accordingly the Bonding Authority shall have discretion as to the most appropriate accounting classification in accordance with standard accounting practices for all items included in Financial Statements.

Residual Discretion with the TAANZ Bonding Committee

The Bonding Committee may, notwithstanding the fact that a member fails to satisfy the financial criteria or other criteria for bonding, agree to extend bonding to such member. This overriding residual discretion vests in the Bonding Committee and nothing elsewhere contained in these criteria, or in the Bonding Committee Regulations, or in the Requirements of the TAANZ Bonding Scheme, shall be interpreted as restricting or

limiting this discretion. The discretion extends to and includes the power to extend bonding to members who fail to satisfy any criteria for bonding including those criteria described as mandatory criteria or which are referred to in mandatory terms.

The Bonding Committee shall have complete and absolute discretion in this regard but it shall give careful consideration to what it considers to be in the best interests of the Association from the perspective of maintaining the Fund.

The Bonding Committee, in agreeing to extend bonding to such a member, may require the member to provide additional security and/or to comply with special operating procedures or conditions. In determining whether it shall extend bonding to such a member the Bonding Committee shall have regards to the views of the Bonding Authority. The Bonding Authority shall have the ability to refer such cases to the Bonding Committee for consideration.

Any member or applicant for membership who has bonding extended to it by the Bonding Committee by virtue of this residual discretion shall be deemed, for so long as that approval continues, to meet and comply with the criteria for membership.

The Bonding Committee may delegate the function of investigating whether it is appropriate to exercise its residual discretion to extend bonding to any member under this provision to a sub-committee of the Bonding Committee comprising not less than three members who shall report back with a recommendation to the full Bonding Committee. The final decision shall however rest with the Bonding Committee.