OAK CAPITAL MORTGAGE FUND

ASIC Benchmark Disclosure Update
30 June 2020

OAK CAPITAL

ARSN 166 411 463 | Issuer: Oak Capital Mortgage Fund Pty Ltd | ABN 45 622 106 692 | AFSL 438659

1 ASIC benchmarks and disclosure principles

1.1 Introduction

ASIC has developed eight benchmarks and eight disclosure principles for unlisted mortgage schemes and these are published in *Regulatory Guide 45 – Mortgage schemes: Improving disclosure for retail investors*. Fund managers are required to disclose against the disclosure principles and state whether they comply with the benchmarks, and if not, explain why not.

1.2 Benchmarks

a) Liquidity

Benchmark: For a pooled mortgage scheme, the responsible entity has cash flow estimates for the scheme that:

i. demonstrate the scheme's capacity to meet its expenses, liabilities and other cash flow needs for the next 12 months;

ii. are updated at least every three months and reflect any material changes; and

iii. are approved by the directors of the responsible entity at least every three months

Oak Capital response

Not applicable as the Fund is a contributory mortgage scheme not a pooled mortgage scheme.

b) Fund Borrowing

Benchmark: The responsible entity does not have current borrowings and does not intend to borrow on behalf of the scheme.

Oak Capital response

Oak Capital complies in that the Fund does not undertake borrowings secured against its full portfolio of mortgages. Nor does Oak Capital set up Mortgage Investments with the intention of borrowing against the assets of individual Mortgage Investments. Although the Constitution permits Oak Capital to borrow against Mortgage Investment assets to pay Management Costs and Disbursements, we do not intend to exercise these rights.

c) Portfolio Diversification

Benchmark: For a pooled mortgage scheme:

i. the scheme holds a portfolio of assets diversified by size, borrower, class of borrower activity and geographic region;

ii. the scheme has no single asset in the scheme portfolio that exceeds 5% of the total scheme assets;

iii. the scheme has no single borrower who exceeds 5% of the scheme assets; and

iv. all loans made by the scheme are secured by first mortgages over real property (including registered leasehold title).

Oak Capital response

Not applicable as the Fund is a contributory mortgage scheme not a pooled mortgage scheme.

d) Related Party Transactions

Benchmark: The responsible entity does not lend to related parties of the responsible entity or to the scheme's investment manager.

Oak Capital response

Oak Capital complies.

However, Oak Capital, and its related parties, have in the past and may in the future;

i. lend money to a borrower;

ii. invest in Mortgage Investments alongside other Investors (on identical terms);

General trust law requires that where a trustee (Oak Capital) makes a profit from activities related to its trust (the Fund), it can only do so if the beneficiaries (the Investors) give their informed consent. By completing the Fund Application Form, you will be deemed to have given your informed consented to Oak Capital and its related parties profiting from the above activities.

Oak Capital, or a related party, may invest alongside Investors in a Mortgage Investment (on identical terms), or assume a first loss position behind a Mortgage Investment (by providing subsequent priority loans to the Borrower).

However, where Oak Capital, or a related party, loans money to a Mortgage Investment, or to the Borrower, in priority to the Mortgage Investment, then Oak Capital must:

i. only permit this if it reasonably believes it is in the interest of the Investors in the Mortgage Investment; and

ii. only do so (without the express consent of the Investors in the relevant Mortgage Investment) if the interest rates charged under the loan are no higher than those charged under the Mortgage Investment's loan to the Borrower.

e) Oak Capital Valuation Policy

Benchmark: In relation to valuations for the scheme's mortgage assets and their security property, the board of the responsible entity requires:

i. a valuer to be a member of an appropriate professional body in the jurisdiction in which the relevant property is located;

ii. a valuer to be independent;

iii. procedures to be followed for dealing with any conflict of interest;

iv. the rotation and diversity of valuers;

v. in relation to security property for a loan, an independent valuation to be obtained:

A. before the issue of a loan and on renewal:

I. for development property, on both an 'as is' and 'as if complete' basis; and

II. for all other property, on an 'as is' basis; and

B. within two months after the directors form a view that there is a likelihood that a decrease in the value of security property may have caused a material breach of a loan covenant.

Oak Capital response

Oak Capital does not meet benchmark.

In respect of the issue of a loan, Oak Capital obtains an independent valuation on any underlying security which is used for the calculation of the LVR disclosed in the SPDS before a Mortgage Investment is made.

However, Oak Capital does not necessarily obtain an independent valuation each time there is an extension (or renewal) of the loan. For example, for some short-term loans, the Directors do not consider it necessary to obtain further independent valuations of security property supporting the loan if the renewal is only for a short term or there is otherwise no indication of a significant change in the underlying market value of the security property.

f) Loan to Valuation Ratios

Benchmark: If the scheme directly holds mortgage assets:

i. where the loan relates to property development—funds are provided to the borrower in stages based on independent evidence of the progress of the development;

ii. where the loan relates to property development—the scheme does not lend more than 70% on the basis of the latest 'as if complete' valuation of property over which security is provided; and

iii. in all other cases—the scheme does not lend more than 80% on the basis of the latest market valuation of property over which security is provided

Oak Capital response

Oak Capital does not comply with the benchmark. In certain circumstances, we will lend on an LVR of greater that 70% on the basis of an 'as if complete' valuation of property over which security is provided.

Where a loan relates to property development, we sometimes utilise the construction experience of our Directors to conduct an assessment of each stage of completion prior to permitting drawdown on further funds rather than engaging an independent quantity surveyor. This practice generally only occurs when the loan is of a relatively small value (in comparison to the remainder of our loan book) and in the circumstances where the nature of the construction being undertaken is within the skills and experience of our Directors that allows them to make an assessment of the work completed at each stage.

g) Distribution Practices

Benchmark: The responsible entity will not pay current distributions from scheme borrowings.

Oak Capital response

i. Oak Capital complies. Distributions are paid to Investors from the following sources[1]:

A. Prepaid interest (see 3.5(e) of PDS);

B. interest payments made by the Borrowers (see 3.5(f) and 3.5(g) of PDS);

C. the sale of Security Property;

D. the pursuit of Guarantors and Borrowers.

ii. If, from all viable sources, there are insufficient funds to:

A. pay any prior ranking charge (for example a higher-ranking mortgage or Land Tax);

B. pay all the Management Costs and Disbursements (see section 7 of PDS); or

C. pay Investors all their Interest and capital Distributions;

then the available monies will be applied in the above order (first (A), then (B), then (C)). This means there is a risk that Investors will suffer a shortfall on the payment of income and/or capital Distributions ('Impairment').

The following table contains a summary of the major factors that could have the most material impact on Distributions. See also section 4 of PDS – *Benefits and Risks of the Fund*.

[1]Distributions are not the only monies paid from these sources, Management Costs and Disbursements are also paid, in priority from these sources.

FACTOR	RISK	SENSITIVITY ANALYSIS
If the borrower defaults on interest payment obligations.	Loans will not be entered into by Oak Capital unless the risk that the borrower will default is assessed by the Lending Committee as being acceptable. However, it must be understood that the primary consideration when entering into a loan is always the ability, in the final resort, to recover all outstanding monies through the sale of the Security Property.	If the borrower does not pay interest then no distributions will be made until the
If the borrower defaults and recovery process is delayed or prolonged.	If the borrower defaults on the loan Oak Capital will follow its recovery process. However, it must be understood that from time to time borrowers may adopt stalling or delaying tactics, example: involving the Australian Financial Complaints Authority or other actions that could delay the recovery, possession or sale of the security.	Extended delays and costs associated with defending any claims, default interest, other charges associated with recovering the asset could lead to a shortfall in full recovery of funds.
If the tenant does not renew, becomes insolvent, or stops paying rent.	This is really a specific example of the preceding two risks. Sometimes the borrower will be relying on the rent paid by a tenant of the Security Property to pay the interest.	If the tenant stops paying, the borrower may have other resources from which to pay interest.
Development delay.	If the Mortgage Investment relates to a development loan, and the facility relies upon prepaid interest in order to fund distributions, then a delay in the construction progress which causes the development to overrun the facility term will result in interest distributions ceasing.	If the development is delayed, it will almost certainly result in distributions ceasing. This is because Developers, by the nature of their business, do not have cashflow other than from selling completed developments.

h) Withdrawal Arrangements

Benchmark: For liquid schemes:

i. the maximum period allowed for in the constitution for the payment of withdrawal requests is 90 days or less;

ii. the responsible entity will pay withdrawal requests within the period allowed for in the constitution; and

iii. the responsible entity only permits members to withdraw at any time on request if at least 80% (by value) of the scheme property is:

A. money in an account or on deposit with a bank and is available for withdrawal immediately, or otherwise on expiry of a fixed term not exceeding 90 days, during the normal business hours of the bank; or

B. assets that the responsible entity can reasonably expect to realise for market value within 10 business days.

For non-liquid schemes, the responsible entity intends to make withdrawal offers to investors at least quarterly.

Oak Capital response

The benchmark is not met. Each Mortgage Investment will be non-liquid. Unless you find a substitute investor, it is not possible to withdraw your investment during the term of a Mortgage Investment. If the loan is not repaid upon maturity, then your investment will not be available for withdrawal upon expiry of its nominal term. Investments in a Mortgage Investment last as long as it takes to recover the investment from the Borrower and/or the sale of the Security Property.

If a loan goes into default and the Security Property has to be realised, there may be significant delay before the capital available to repay investors can be realised. For example, in the case of a development loan to a builder, if the builder goes into insolvency it may be another builder may have to be found and this process will often significantly delay completion and sale of the development.

Capital from a Mortgage Investment is only returned to the Cash Account upon the repayment of a loan by a borrower or if proceeds are received on the sale of Security Property. Withdrawals are normally paid from the Cash Account within five business days of receiving a request. The Fund's Constitution allows up to 90 days to consider a withdrawal request and a further 21 days to process the payment.

1.3 Benchmarks

a) Disclosure principle 1 - liquidity

As the Fund is a contributory mortgage scheme, ASIC's liquidity disclosure principle does not apply to it.

b) Disclosure principle 2 - scheme borrowing

The Fund does not have any borrowings and does not intend to borrow.

c) Disclosure principle 3 – loan portfolio and diversification

As the Fund is a contributory mortgage scheme, ASIC's loan portfolio and diversification disclosure principle does not apply to it.

d) Disclosure principle 4 – related party transactions

Oak Capital may from time to time engage related parties to provide services to the Fund. It does not make loans to related parties from Fund property.

Oak Capital has policies and guidelines in place to manage the risk of any actual or perceived conflict of interest as a result of a related party transaction. Related party transactions between Oak Capital and its related parties are reviewed, approved and monitored by senior management of Oak Capital in accordance with Oak Capital conflicts of interest policies.

The risks associated with related party transactions is that they could be assessed and reviewed less rigorously than arrangements with third parties.

Oak Capital intends to only enter into related party transactions on commercial arm's length terms.

e) Disclosure principle 5 – valuation policy

Investors can obtain a copy of Oak Capital's valuation policy by calling Oak Capital on 1300 625 227/ (03) 9621 1399.

Independent valuations in relation to security property for a loan are obtained:

i. before the issue of a loan and on renewal:

   A. for development property, on both an 'as is' and 'as if complete' basis; and

   B. for all other property, on an 'as is' basis; and

ii. within two months after the directors form a view that there is a likelihood that a decrease in the value of security property may have caused a material breach of a loan covenant.

f) Disclosure principle 6 – loan-to-valuation ratios

The maximum and weighted average loan-to-valuation ratio for the Fund as at 30 June 2020 is:

FACTOR	% AS AT 30 JUN 2020
Maximum LVR	80%
Weighted LVR[2]	55.0%

[2]Weighted by the value of loans of the Fund.

Where a loan relates to property development, in some cases our Directors conduct an assessment of each stage of completion to ensure construction is being completed in accordance with the terms of the contract. In other cases, an independent quantity surveyor may be engaged to undertake this task. Funds are provided to the Borrower in stages based on evidence of the progress of the development. When funds are drawn, we aim to ensure that the amount that has not been drawn down under the loan is generally equal or more than equal to the cost-to-complete as assessed by our Directors.

As at 30 June 2020 there were no development loans.

g) Disclosure principle – distribution practices

The Distribution Rate for each Mortgage Investment is set out in the SPDS. Generally, all distributions are sourced from income or prepaid interest received in the relevant distribution period.

Oak Capital intends to make distributions monthly, except where otherwise disclosed in an SPDS. Please note, the payment of distribution is subject to the relevant Borrower making principal and interest repayments on their loan.

h) Disclosure principle – withdrawal arrangements

The Fund and each Mortgage Investment will be non-liquid. Unless you find a substitute investor, it is not possible to withdraw your investment during the term of a Mortgage Investment. If a loan is not repaid upon maturity, then your investment will not be available for withdrawal upon expiry of its nominal term. Investments in a Mortgage Investment last as long as it takes to recover the investment from the

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