

2 August 2013

Dear Member

Banksia Mortgage Fund (ARSN 089 852 246)
Responsible Entity: Banksia Mortgages Limited

As you know, Banksia Mortgages Limited (**BML**) is the responsible entity (**RE**) of the Banksia Mortgage Fund (**BMF**). I am writing to you because you are recorded in BML's records as a member of BMF, having invested in one or more mortgage loans made by BML in its capacity as RE of BMF.

Outcome of process to transfer the operation of BMF

I refer to my circulars to members dated 14 December 2012 and 18 February 2013, which can be accessed at Banksia's website (www.banksiagroup.com.au). In my circular of 14 December 2012, I reported to you that receivers and managers had been appointed to two companies in The Banksia Financial Group (**Group**), Banksia Securities Limited (**BSL**) and Cherry Fund Limited. In my circular of 18 February 2013 I reported to you that the directors of companies in the Group had resolved to pursue an orderly process aimed at achieving a solvent winding up of the affairs of each company in the Group, including BML. That circular also advised that BML and its parent company, Securities Holdco Limited, had appointed Melbourne-based corporate advisory firm, Flagstaff Partners Pty Ltd (**Flagstaff**), to investigate opportunities to transfer the operation of BMF to an organisation with the ability to regenerate BMF so as to preserve and maintain investment opportunities for BMF investors.

That investigation process concluded in late June 2013, without BML identifying a party which would be prepared to accept a transfer of the operations of BMF or enter into any other arrangement acceptable to BML.

Subsequent approach to ASIC

When the outcome of the process became clear, BML approached ASIC to enquire whether it was aware of any party that might be prepared to accept the role of a replacement or temporary RE of BMF. ASIC responded formally to BML on 12 July 2013 that it was not aware of any parties that were suitable to assume the role of a replacement or temporary RE at this stage. Similarly, BML is not aware of any suitable party to assume the RE's role.

Resolution of board of BML to apply for direction to wind up BMF

Having considered carefully the position of BML and BMF in light of ASIC's communication and the terms of BSL's ongoing funding commitment to BML (referred to further below), and having taken advice from its lawyers, Allens, the board of BML met on 29 July 2013 and concluded that it would be in the best interests of members of BMF to issue a proceeding in the Supreme Court of Victoria and make an application for an order directing BML to wind up BMF. BML's application will be heard on 20 August 2013.

If the Court agrees to make an order directing BML to wind up BMF, as things currently stand, BMF must be wound up in accordance with BML's constitution. While the constitution is not prescriptive regarding the manner in which winding up must occur, BML considers that the constitution contemplates that an orderly 'wind-down' of the scheme loans with repayment of investors' principal, as each loan reaches its term, is the required course.

Additional option to wind up BMF by a portfolio sale

In the present circumstances, the board of BML considers that there is merit in exploring an additional option of winding up BMF by conducting a portfolio sale of BMF loans as a means of accelerating the repayment of investors' principal and bringing forward the completion of the winding up of BMF, instead of conducting an orderly 'wind down' of the loans. This additional option was raised for the BML board's consideration by the receivers of BSL. The board of BML has given independent consideration to the option and has formed the view that it is in the best interests of members to pursue this additional option.

To do this, in summary, the following steps are required.

- amend the BMF constitution;
- engage a transaction manager to market the loan portfolio to potential purchasers;
- engage an independent adviser to BML to oversee this process;
- obtain a court order directing that BML is justified in taking these steps;
- assess any offers which may be made to consider whether they are in the best interests of BMF members;
- if satisfied that an offer is in the best interests of members, apply to the Court for a direction that BML is justified in completing the necessary contracts and documents to finalise the transaction; and
- finally, if such a direction is obtained and the transaction is finalised, return money to investors.

Each of these steps is explained in further detail below.

Necessity for amendments to the constitution of BMF to pursue this additional option

To enable BML to have the flexibility to pursue this additional option, BML has determined that it is necessary to make certain amendments to the constitution of BMF. While one way of doing this would be to convene a meeting of BMF members to consider passing a resolution to make amendments to the constitution, BML instead intends to apply to the Court, on the day on which its application for the winding up of BMF is heard, to seek judicial advice that it is justified in making the amendments to the constitution. This is because BML has formed the view that to do so would be in the best interests of members and, while the amendments to the constitution would affect members' rights, members' rights would not be affected adversely. Further, BML considers that the amendments are otherwise consistent with the exercise of BML's duties as RE of BMF.

The effect of the amendments would be to introduce provisions:

- (a) permitting BMF to be wound up by BML by way of a portfolio sale of some or all of the BMF loans, if there is a Court order to wind up BML;
- (b) giving BML the power to conduct a portfolio sale of BMF loans, including by engaging advisers, managers and other third parties to assist BML in doing so; and
- (c) under which each member appoints BML as its attorney and agent in connection with the carrying out of a portfolio sale of BMF loans by BML.

Importantly, the amendments would provide that BML may effect a disposal of a BMF loan under a portfolio sale only if, prior to completion of the sale of that loan, BML has obtained the approval or advice of the Court that it is justified in completing such sale.

Process for portfolio sale

If the Court makes an order directing BML to wind up BMF, and provides judicial advice to BML that it is justified in amending the constitution of BMF in the manner proposed to enable BML to explore the additional option of a portfolio sale of BMF loans, then BML proposes to undertake the following steps:

- (a) BML will execute a deed giving effect to the amendments to the constitution of BMF and lodge that deed with ASIC, whereupon the amendments will take effect;
- (b) BML (through BSL as its transaction manager (see paragraph (c) below)) would market the portfolio of loans which have not been repaid by borrowers at that time, using a competitive bid process, on the basis that offers from interested parties (most likely financial institutions) would need to be made on a loan-by-loan (ie sub-scheme by sub-scheme) basis;
- (c) BML would engage BSL – which itself is a major investor in the portfolio of loans – as its transaction manager to conduct the competitive bid process for the portfolio of loans (the board of BML considers that the receivers of BSL have both the experience and the expertise to enable BSL to perform the transaction manager role effectively);
- (d) the board of BML would approve the marketing process for the portfolio of loans, have full transparency around all steps taken by BSL as the transaction manager and would make the ultimate decision as to whether to consummate any proposed sale transaction on a loan-by-loan basis;
- (e) in anticipation of undertaking this process, BML has engaged Flagstaff as its independent advisor to advise BML in respect of all aspects of its retainer of BSL and to assist BML in assessing any offers to purchase the portfolio of loans in the context of BML's duties to members; and
- (f) in response to offers received for the portfolio of loans, BML would form a view, for each loan in respect of which an offer is received, as to whether it would be in the best interests of the investors in the relevant BMF loan to accept the offer.

Documents giving effect to portfolio sale process

Documents have been prepared which would give effect to the portfolio marketing and sale process. These will be executed upon the Court making the orders sought by BML and the proposed amendments to the constitution of BMF becoming effective.

Further Court application

If BML receives an offer for a sub-scheme loan and forms the view that it would be in the best interests of the investors in the relevant BMF loan to accept the offer, completion of the sale of that loan will depend on BML obtaining the approval or advice of the Court that it is justified in completing the sale. It is BML's intention to make a further application to the Court for such approval or advice if it receives such an offer.

Any such application will be based on appropriate affidavit material and members will have an opportunity to consider that material, raise any queries and have their position conveyed to the Court, in addition to having the opportunity to appear at the hearing of the application.

Terms of ongoing financial support by BSL for winding up of BMF

Since the appointment of receivers to BSL, BML has been able to continue to meet its obligations to members of BMF with the financial support of BSL. BSL indicated to BML on 26 July that it is presently unwilling to fund BML in a winding up of BMF that involves an orderly 'wind-down' of the loans in the BMF portfolio in accordance with the constitution of BMF, preferring the portfolio sale option.

In this context, BML considers that the winding up of BMF by a portfolio sale of BMF loans represents the only realistic option. The alternative would be to appoint a voluntary administrator to BML, which in turn would result in an externally-controlled winding up of BMF and likely value destruction for members, as all costs of a voluntary

administrator would be borne out of the assets of BMF. On the other hand, the option of a portfolio sale offers investors a new mechanism to realise their investments in BMF without the potentially destructive impact of either voluntary administration of BML or any enforcement action that may involve a mortgagee sale process.

That said, BSL has also indicated that if the portfolio sale process does not lead to a completion of a contract of sale approved by the Court, BSL is prepared to consider (without at this stage committing to) providing funding for an orderly wind-down of the loans in accordance with the terms of the constitution of BMF.

How to find out more

BML has prepared additional information to help you understand the Court application and the proposed portfolio sale. If you wish you can access more detailed information (including a list of frequently asked questions in relation to the application and the proposed portfolio sale, and BML's responses to those questions) as well as the documents for the Court application online at Banksia's website www.banksiagroup.com.au. You may also call a hotline set up by BML on **1800 722 079**.

In the period leading up to the hearing please continue to monitor the Banksia website for developments in relation to the Court application.

Do You need to do anything now?

The first Court application will be heard by Justice Sifris of the Supreme Court of Victoria in Melbourne at a hearing on 20 August 2013.

If you wish to raise any query, comment or make affirmation or objection to the course being proposed by BML as set out in this circular, you may call the hotline or email BML at info@banksiagroup.com.au. All communications made by you to BML through the hotline or by email, together with any required response from BML, will form part of the materials provided to the Court by BML at the time of the hearing of the application by the Court.

You may wish to seek independent legal advice and/or appear at the hearing on 20 August 2013. In doing so, you should have regard to the orders made by the Court on 1 August 2013, available on the Banksia website (www.banksiagroup.com.au). Any legal or other costs incurred will be at your own expense, subject to any order of the Court to the contrary.

You should note that if the Court gives a direction to BML to wind up BMF and provides judicial advice to BML that it is justified in making the amendments to the constitution, you will be bound by the Court's decision. It is therefore important to read the information in this letter and provided by BML on the Banksia website (www.banksiagroup.com.au) carefully. Otherwise, you don't need to take any action.

You will be kept informed of future developments by circular. The next circular will be sent to you once the outcome of the Court application is known.

Yours faithfully



Warren Shaw
Chief Executive Officer