

New enhanced disclosure rules for mortgage funds

ASIC is seeking feedback on proposals to increase the disclosure requirements for mortgage funds. It recently released a consultation paper which you can access at http://www.mcmahonclarke.com/ckfinder/userfiles/files/CP_141.pdf. The consultation paper relates to changes to ASIC's policy on mortgage funds, RG 45.

RG 45 was implemented in 2008 and sets out eight benchmarks responsible entities (REs) of unlisted mortgage schemes must disclose against on an 'if not, why not' basis. Disclosures against the benchmarks are required in product disclosure statements and ongoing disclosures.

ASIC has reviewed the disclosures made by the mortgage fund industry against the current disclosure requirements and is dissatisfied with the current level of disclosure. It now wishes to enhance the disclosure benchmarks to ensure consistency across the industry and to require further disclosure from REs.

The table below highlights the differences between the benchmarks in RG 45 and the proposed refined benchmarks set out in CP 141.

Old disclosure	New disclosure
Liquidity	
Cash flow estimates for each scheme demonstrating the scheme's capacity to meet expenses for rolling three month periods.	Cash flow estimates must be shown for 12 months.
Scheme borrowing	
Disclosure of actual and expected borrowing showing amounts owing and maturity profiles, any lender's priority and the purpose for which funds have been borrowed.	The revised benchmark is simply the RE does not borrow on behalf of the scheme. If an RE does borrow on behalf of a scheme, then there are proposed changes to the disclosure which the RE must make about those borrowings.
Loan portfolio and diversification	
Disclosure of a scheme's investment portfolio including loans by class and geographic region plus details of arrears and security.	<p>The scheme—</p> <ol style="list-style-type: none"> holds a portfolio of assets diversified by size, borrower, class of borrower activity and geographic region has no single asset in the scheme portfolio that exceeds 10 percent of total scheme assets, and has no single borrower who exceeds 10 percent of scheme assets. <p>The refined benchmark also provides all loans made by the scheme are secured by first mortgages over real property.</p> <p>If the scheme does not have each of the attributes outlined above, then the RE must explain why it does not.</p>
Related party transactions	
Disclosure of approach to related party transactions including number of loans, policy on assessment and approval process and enforcement of that policy.	<p>The refined benchmark is simply the RE does not lend to related parties of the RE or its directors.</p> <p>If the RE does not meet the benchmark, then it must provide additional disclosure about those loans.</p>

Old disclosure	New disclosure
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Valuation policy	
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Disclosure of the approach to valuations of properties provided to the scheme as security for loans including valuing on an “as is” basis, and for development property, on an “as if complete” basis, disclosure of the policy on obtaining valuations and establishment of a panel of valuers.

The RE appoints valuers in accordance with its valuation policy and that valuation policy requires a number of prescribed items including **independence, dealing with conflicts and rotation and diversity of valuers**.

In addition, the RE will need to disclose where investors may **access a scheme’s valuation policy** (for example, by disclosing that the policy is available on the RE’s website).

Lending principles—LVRs	
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REs should maintain 70 percent LVR for property developments and 80 percent in all other cases.

The scheme does not lend more than 70 percent of the “as is” value of property over which security is provided. Additionally, in the case of loans for property development, funds are provided to the borrower in stages based on independent evidence of the progress of the development.

If the scheme does not meet these benchmarks, then the RE must explain **why it does not**.

Distribution practices	
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Disclosure on the expected source for distributions, whether this differs to historical sources and whether distributions sourced other than from scheme income are sustainable.

The RE will pay distributions in accordance with the scheme’s **distribution policy**.

Withdrawal arrangements	
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Disclosure of the maximum withdrawal period allowed under the constitution, significant risk factors impeding withdrawals and the approach to rollovers (including whether automatic rollover is the default).

For liquid schemes the benchmarks are that—

1. the period in the scheme’s constitution for the payment of withdrawal requests is less than 90 days
2. payment will be made within the period allowed for in the scheme’s constitution, and
3. withdrawal rights are only provided if at least 80 percent of scheme property is cash or assets the RE can reasonably expect to realise for market value within 10 business days.

For illiquid schemes the benchmark is simply the RE intends to make withdrawal offers at least quarterly.

ASIC also proposes to ensure that feeder funds (i.e., a scheme that invests all or most of its assets in other unlisted mortgage investment schemes) must also disclose how the benchmarks apply at the feeder fund level as well as at the underlying funds level.

ASIC is seeking feedback on the proposed reforms and in particular it is asking the industry to provide it with information about—

1. the likely compliance costs of the proposed reforms
2. the likely effect on competition
3. any other impacts, costs and benefits, and
4. whether there are any alternative approaches that should be adopted by ASIC.

McMahon Clarke is preparing a submission on the proposals and we encourage you to contact us with any feedback which can be incorporated in that submission.



Chris Mee

Partner

07 3239 2961

chris.mee@mcmahonclarke.com

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62 Charlotte Street Brisbane Q 4000 | GPO Box 1279 Brisbane Q 4001 T 07 3831 8999 F 07 3831 1121