

FIRST MORTGAGE INVESTMENTS

ARSN 089 600 920

ANNUAL FINANCIAL REPORT

30 JUNE 2018

This is annexure A of 35 pages referred to in form 388 "Copy of financial statements and reports"



Director

13/9/18

Date

FIRST MORTGAGE INVESTMENTS
ARSN 089 600 920

RESPONSIBLE ENTITY'S REPORT

The directors of First Mortgage Managed Investments Limited ('the Responsible Entity'), the Responsible Entity of First Mortgage Investments ('the Scheme'), present their report together with the financial report of the Scheme, for the year ended 30 June 2018 and the auditor's report thereon.

Responsible Entity

The registered office and principal place of business of the Responsible Entity and the Scheme is 11 West Street, Burleigh Heads, and Queensland.

First Mortgage Managed Investments Limited (ABN 39 089 507 899) has been the Responsible Entity of the Scheme since 15 September 1999.

The directors of First Mortgage Managed Investments Limited during or since the end of the financial year are:

Name, qualifications and independence status	Age	Experience, responsibilities and other directorships
Michael Boyce	56	Michael Boyce has over 30 years' experience in operating and managing the provision of mortgage finance. Michael is also a solicitor of the Supreme Court of Queensland and New South Wales and has completed his Diploma of Mortgage Lending. His main responsibilities are specialist knowledge in the administration and management of the fund.
Karen Scott	47	Karen Scott has over 20 years of experience in the mortgage industry. Karen's involvement is predominantly with investing clients and investor portfolios. Karen has completed a Diploma of Mortgage Lending with the Securities Institute of Australia.
Megan Boyce	27	Megan commenced employment with the Manager, First Mortgage Investments Pty Ltd, in 2011 and holds a Bachelor of Business degree. Megan has also completed a Certificate IV in Financial Services and a Diploma of Finance Mortgage Broking Management. Megan's responsibilities include all aspects of pre-settlement requirements and assisting with risk management analysis.

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RESPONSIBLE ENTITY'S REPORT

Principal activities

The Scheme is a registered managed investment scheme domiciled in Australia.

The investment activities of the Scheme continued to be in accordance with the investment policy of the Scheme as outlined in the current product disclosure statement.

The Scheme is a contributory mortgage investment scheme investing in first mortgages over freehold property in Australia. It is designed to allow investors to select individual investments from a range of approved mortgage products at agreed terms and at agreed rates of interest.

The Scheme did not have any employees during the year.

Review and result of operations

The Scheme's net income from operations before financing costs for the current year was \$4,828,876 (2017: \$3,891,382)

Distributions

The rate of distribution paid to each investor is set at the time of entering into the mortgage investment. The distribution rates ranged from 6.50% to 7.25% per annum from 1 August 2016. Prior to 1 August 2016, distribution rates ranged from 7.00% to 7.75% per annum.

Distributions paid or payable by the Scheme since the end of the previous financial year were \$4,828,876 (2017: \$3,891,382).

Investors Funds – liability

The Scheme received \$23,388,000 of investor funds during the financial year (2017: \$17,640,100), while \$13,671,757 was withdrawn (2017: \$6,267,278), resulting in a balance of investors' funds of \$70,895,470 as at 30 June 2018 (2017: \$61,179,227).

The Scheme had total assets valued at \$74,146,272 as at 30 June 2018 (2017: \$63,789,554). The basis for measurement of the Scheme's assets is disclosed in Note 2 to the financial statements.

As the Scheme is a contributory mortgage scheme, the liability to investors by the Scheme is limited to the extent of their interest in specific mortgage loans and receivables, which have been included as assets of the Scheme.

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RESPONSIBLE ENTITY'S REPORT

Likely developments

The Scheme will continue to pursue its policy of increasing returns through active investment selection.

Environmental Regulation

The Scheme's operations are not subject to any significant regulation under Commonwealth, State or Territory legislation.

Events subsequent to balance date

There has not arisen in the interval between the end of the financial year and the date of this report any item, transaction or event of a material and unusual nature likely, in the opinion of the Responsible Entity, to affect significantly the operations of the Scheme, the results of those operations, or the state of affairs of the Scheme, in future financial years.

Interests of the Responsible Entity

The following fees were paid by the Scheme to the Responsible Entity and its associates during the financial year:

	2018	2017
	\$	\$
■ Management fees for the year, paid and payable to First Mortgage Investments Pty Ltd by the Scheme under the terms of the Service Agreement between that company and the Responsible Entity, net of reduction or increment in management fee to offset impairment losses or reversal of impairment. For the years ended 30 June 2018 and 30 June 2017, there was no adjustment to the management fee.		
	2,904,382	2,192,930

Management fees are utilised by First Mortgage Investments Pty Ltd to pay for services provided to the Scheme as follows:

- accounting and audit services;
- corporate lawyer's services;
- loan recovery expenses;
- insurance premiums;
- licences and registrations;
- general office expenses; and
- promotion and marketing.

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RESPONSIBLE ENTITY'S REPORT

Interests of the Responsible Entity (cont.)

Associates of the Responsible Entity had \$14,275,650 (2017: \$11,453,650) invested in the Scheme at year-end on normal terms and conditions.

Significant changes in the state of affairs

In the opinion of the Responsible Entity there were no significant changes in the state of affairs of the Scheme that occurred during the financial year.

Indemnities and insurance premiums for Officers or Auditors

Indemnification

Under the Scheme constitution the Responsible Entity, including its officers and employees, is indemnified out of the Scheme's assets for any loss, damage, expense or other liability incurred by it in properly performing or exercising any of its powers, duties or rights in relation to the Scheme.

The Scheme has not indemnified any auditor of the Scheme.

Insurance premiums

No insurance premiums are paid out of the Scheme's assets in relation to insurance cover for the Responsible Entity, its officers and employees, the Compliance Committee or the auditors of the Scheme.

Lead auditor's independence declaration under Section 307C of the *Corporations Act 2001*

The lead auditor's independence declaration is set out on page 5 and forms part of the Responsible Entity's report for the year ended 30 June 2018.

Signed in accordance with a resolution of the directors of First Mortgage Managed Investments Limited.



Karen Scott
Director

Burleigh Heads
Date: 13 September 2018



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Lead Auditor's Independence Declaration under Section 307C of the Corporations Act 2001

To: the directors of First Mortgage Managed Investments Limited, the Responsible Entity of First Mortgage Investments.

I declare that, to the best of my knowledge and belief, in relation to the audit for the financial year ended 30 June 2018 there have been:

- no contraventions of the auditor independence requirements as set out in the *Corporations Act 2001* in relation to the audit; and
- no contraventions of any applicable code of professional conduct in relation to the audit.

KPMG

JJ Frazer
Partner

Burleigh Heads
13 September 2018

FIRST MORTGAGE INVESTMENTS
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STATEMENT OF FINANCIAL POSITION

AS AT 30 JUNE 2018

	Note	2018 \$	2017 \$
Assets			
Cash and cash equivalents	7a	1,562,616	1,786,025
Interest receivable	8	2,159,290	1,339,663
Mortgage loans	8	<u>70,424,366</u>	<u>60,663,866</u>
Total assets		74,146,272	63,789,554
Liabilities			
Distribution payable	9	198,798	176,733
Manager fees payable	10	1,393,982	596,417
Mortgage bonds		883,498	1,395,223
Other payables		329,156	172,402
Interest received in advance		<u>445,368</u>	<u>269,552</u>
Total liabilities (excluding net assets attributable to investors)		<u>3,250,802</u>	<u>2,610,327</u>
Net assets attributable to investors - Liability	4	<u>70,895,470</u>	<u>61,179,227</u>
Net assets		<u>-</u>	<u>-</u>
Equity		<u>-</u>	<u>-</u>

The accompanying notes are an integral part of these financial statements

FIRST MORTGAGE INVESTMENTS
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STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME

FOR THE YEAR ENDED 30 JUNE 2018

	Note	2018 \$	2017 \$
Revenue			
Interest income – mortgage loans	5	7,732,109	6,084,083
Interest income – bank	5	4,364	5,627
Net investment income		<u>7,736,473</u>	<u>6,089,710</u>
Expenses			
Management fees	10	2,904,382	2,192,930
Other expenses		3,215	5,398
Impairment losses/(reversal of impairment)	8,10	-	-
Operating expenses before financing costs		<u>2,907,597</u>	<u>2,198,328</u>
Operating profit before finance costs		<u>4,828,876</u>	<u>3,891,382</u>
Finance costs			
Distribution expense to investors	9	<u>4,828,876</u>	<u>3,891,382</u>
Net profit		<u>-</u>	<u>-</u>
Other comprehensive income		<u>-</u>	<u>-</u>
Total comprehensive income		<u><u>-</u></u>	<u><u>-</u></u>

The accompanying notes are an integral part of these financial statements

**FIRST MORTGAGE INVESTMENTS
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STATEMENT OF CHANGES IN EQUITY

FOR THE YEAR ENDED 30 JUNE 2018

The Scheme's net assets attributable to investors are classified as a liability under AASB 132 Financial Instruments: Presentation. As the Scheme has no equity, there are no items included in the Statement of Changes in Equity for the current or comparative year.

FIRST MORTGAGE INVESTMENTS
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STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED 30 JUNE 2018

	Note	2018 \$	2017 \$
Cash flows from operating activities			
Interest received		6,580,937	6,715,882
Operating expenses paid		(3,215)	(5,398)
Management fee paid		(1,950,063)	(1,967,233)
Distributions paid		(4,806,811)	(3,865,567)
Net cash provided/(used) in operating activities	7(b)	(179,152)	877,684
Cash flows from investing activities			
Mortgage loans made		(35,506,000)	(33,314,000)
Mortgage loans repaid		25,745,500	21,905,500
Net cash provided by/(used in) investing activities		(9,760,500)	(11,408,500)
Cash flow from financing activities			
Proceeds from receipt of investor applications		23,388,000	17,640,100
Payments on redemption of investor funds		(13,671,757)	(6,267,278)
Net cash provided by/(used in) investors' activities		9,716,243	11,372,822
Net (decrease)/increase in cash and cash equivalents		(223,409)	842,006
Cash and cash equivalents at 1 July		1,786,025	944,019
Cash and cash equivalents at 30 June	7(a)	<u>1,562,616</u>	<u>1,786,025</u>

The accompanying notes are an integral part of these financial statements

**FIRST MORTGAGE INVESTMENTS
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**NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 30 JUNE 2018**

1. REPORTING ENTITY

First Mortgage Investments (the 'Scheme') is a registered managed investment scheme under the *Corporations Act 2001*. The financial report of the Scheme is for the year ended 30 June 2018.

2. BASIS OF PREPARATION

(a) Statement of compliance

The financial report is a general purpose financial report which has been prepared in accordance with Australian Accounting Standards ("AASBs") adopted by the Australian Accounting Standards Board ("AASB") and the *Corporations Act 2001*. The financial report of the Scheme also complies with International Financial Reporting Standards and interpretations adopted by the International Accounting Standards Board.

The financial statements were approved by the Board of Directors of the Responsible Entity on 13 September 2018.

(b) Basis of measurement

The financial statements have been prepared on the historical cost basis.

(c) Functional and presentation currency

These financial statements are presented in Australian dollars, which is the Scheme's functional currency.

(d) Use of estimates and judgements

The preparation of financial statements require management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected.

In particular, information about significant areas of estimation uncertainty and critical judgements in applying accounting policies that have the most significant effect on the amount recognised in the financial statements are described in the following notes:

- Notes 8 & 10 – Impairment losses

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2018

3. SIGNIFICANT ACCOUNTING POLICIES

The accounting policies set out below have been applied consistently to all periods presented in these financial statements.

The Scheme has not early adopted any accounting standards.

(a) Financial instruments

(i) Classification

Financial assets that are classified as loans and receivables include mortgage loans and balances due from accounts receivable.

Financial liabilities that are not at fair value through the profit or loss include balances due to the manager, distributions payable, mortgage bonds and income received in advance.

(ii) Recognition

The Scheme recognises financial assets and financial liabilities on the date it becomes a party to the contractual provisions of the instrument. From this date any gains and losses arising from changes in fair value of the financial assets or financial liabilities are recorded.

(iii) Measurement

Financial instruments are measured initially at fair value plus, in the case of a financial asset or financial liability not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the financial asset or financial liability.

Financial assets classified as loans and receivables are carried at amortised cost using the effective interest rate method, less impairment losses if any.

Financial liabilities are measured at amortised cost using the effective interest rate.

Financial liabilities arising from investor funds are carried at the redemption amount representing the investors' right to a residual interest in the Scheme's assets, effectively fair value at reporting date.

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**NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 30 JUNE 2018**

3. SIGNIFICANT ACCOUNTING POLICIES (CONT.)

(a) Financial instruments (cont.)

(iv) Impairment

Financial assets that are stated at cost or amortised cost are reviewed at each balance date to determine whether there is objective evidence of impairment. If any such indication exists, an impairment loss is recognised in the income statement as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate.

If in a subsequent period the amount of an impairment loss recognised on a financial asset carried at amortised cost decreases and the decrease can be linked objectively to an event occurring after the write-down, the write-down is reversed through the income statement.

(v) Derecognition

The Scheme derecognises a financial asset when the contractual rights to the cash flows from the financial asset expire or it transfers the financial asset and the transfer qualifies for derecognition in accordance with AASB 139 Financial Instruments: Recognition and Measurement.

A financial liability is derecognised when the obligation specified in the contract is discharged, cancelled or expired.

(vi) Specific Instruments

Cash and Cash Equivalents

Cash comprises current deposits with banks. Cash equivalents are short-term highly liquid investments that are readily convertible to known amounts of cash, are subject to an insignificant risk of changes in value, and are held for the purpose of meeting short-term cash commitments rather than for investments or other purposes.

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 30 JUNE 2018

3. SIGNIFICANT ACCOUNTING POLICIES (CONT.)

(b) Interest income

Interest income is recognised in the income statement as it accrues, using the original effective interest rate of the instrument calculated at the acquisition or origination date. Interest income includes the amortisation of any discount or premium, transaction costs or other differences between the initial carrying amount of an interest-bearing instrument and its amount at maturity calculated on an effective interest rate basis.

Interest income is recognised on a gross basis, including withholding tax, if any.

(c) Distribution income

Income distributions from other managed investment schemes are recognised in the income statement as dividend income when declared.

(d) Expenses

All expenses, including management fees, are recognised in the income statement on an accrual basis.

(e) Distribution and taxation

Under current legislation, the Scheme is not subject to income tax as the taxable income (including assessable realised capital gains) is distributed in full to the investors. The Scheme fully distributes its distributable income, calculated in accordance with the Scheme constitution and applicable taxation legislation, to the investors who are presently entitled to the income under the constitution.

Financial instruments held at fair value may include unrealised capital gains. Should such a gain be realised that portion of the gain that is subject to capital gains tax will be distributed so that the Scheme is not subject to capital gains tax.

Realised capital losses are not distributed to unit-holders but are retained in the Scheme to be offset against any future realised capital gains. If realised capital gains exceeds realised capital losses the excess is distributed to the investors.

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**NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS
FOR THE FINANCIAL YEAR ENDED 30 JUNE 2018**

3. SIGNIFICANT ACCOUNTING POLICIES (CONT.)

(f) Redeemable units

All redeemable units issued by the Scheme provide the investors with the right to require redemption for cash and give rise to a financial liability. In accordance with the Product Disclosure Statement the Scheme is contractually obliged to redeem units at redemption price.

(g) Finance costs

Distributions paid and payable on investor funds are recognised in the income statement as finance costs and as a liability where not paid. Distributions paid are included in cash flows from operating activities in the statement of cash flows.

(h) Goods and services tax

Management fees and other expenses are recognised net of the amount of goods and services tax (GST) recoverable from the Australian Taxation Office (ATO) as reduced input tax credit (RITC).

Payables are stated with the amount of GST included.

The net amount of GST recoverable/payable from the ATO is included in receivables/payables in the statement of financial position.

Cash flows are included in the statement of cash flow on a gross basis.

(i) Accounting estimates and judgements

The directors of the Responsible Entity have discussed with management the development, selection and disclosure of the Scheme's critical accounting policies and estimates and the application of these policies and estimates.

(j) Change in net assets attributable to investors

Non-distributable income, which may comprise unrealised changes in the fair value of investments, net capital losses, tax deferred income, accrued income not yet assessable and non-deductible expenses are reflected in the profit and loss as change in net assets attributable to investors.

These items are included in the determination of distributable income in the period for which they are assessable for taxation purposes.

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**NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS
FOR THE FINANCIAL YEAR ENDED 30 JUNE 2018**

3. SIGNIFICANT ACCOUNTING POLICIES (CONT.)

(k) New standards and interpretations not yet adopted

A number of new standards and amendments to standards are effective for annual periods beginning after 1 July 2017, and have not been applied in preparing these financial statements. Those which may be relevant to the Scheme are set out below. The Scheme does not plan to adopt these standards early.

AASB 9 Financial Instruments

In July 2014, the Australian Accounting Standards Board issued the final version of AASB 9 Financial Instruments.

AASB 9 is effective for annual periods beginning on or after 1 January 2018, with early adoption permitted. The Scheme does not plan to adopt this standard early. At this stage, it is expected that under the new standard, financial assets of the Scheme will continue to be carried at amortised cost using the effective interest rate method, less any impairment losses if any. AASB 9 introduces an expected credit loss model when assessing impact of financial instruments. As a result, the introduction of the new standard may result in a change in how impairment of interest receivable and mortgage loans is assessed. However, the Scheme is still currently assessing the potential impact on its financial statements resulting from the application of AASB 9.

(l) Unit price

The unit price is based on unit price accounting outlined in the Scheme's Constitution and Product Disclosure Statement.

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS

FOR THE FINANCIAL YEAR ENDED 30 JUNE 2018

4. NET ASSETS ATTRIBUTABLE TO INVESTORS - LIABILITY

	2018	2017
	\$	\$
Opening balance	61,179,227	49,806,405
Applications	23,388,000	17,640,100
Redemptions	(13,671,757)	(6,267,278)
Closing balance	<u>70,895,470</u>	<u>61,179,227</u>

The Scheme considers its capital to be Investor Funds. The Scheme manages its net assets attributable to investors as capital, notwithstanding net assets attributable to investors are classified as a liability.

All units in the Scheme are of the same class and carry equal rights.

As the Scheme is a contributory mortgage scheme, the liability to investors by the Scheme is limited to the extent of their interest in specific mortgage loans and receivables, which have been included as assets of the Scheme.

Refer to Note 11 for Liquidity risk.

5. REVENUE

	2018	2017
	\$	\$
Interest income arises from:		
Cash and cash equivalents	4,364	5,627
Mortgage loans	<u>7,732,109</u>	<u>6,084,083</u>
	<u>7,736,473</u>	<u>6,089,710</u>

The interest rate for cash and cash equivalents at 30 June 2018 was 0.09% (2017: 0.05%).

The weighted average interest rate for mortgage loans at 30 June 2018 was 11.18% (2017: 11.30 %).

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS

FOR THE FINANCIAL YEAR ENDED 30 JUNE 2018

6. AUDITOR'S REMUNERATION

	2018	2017
	\$	\$
Audit fees paid by a related entity of the Responsible Entity on behalf of the Scheme:		
Audit services		
Audit and review of the financial report	46,750	45,650
Other regulatory audit services	9,000	8,750
	<u>55,750</u>	<u>54,400</u>
Other services		
Other fees paid by a related entity of the Responsible Entity on behalf of the Scheme:		
Other services	<u>1,820</u>	<u>1,820</u>

7a. CASH AND CASH EQUIVALENTS

Current balances with banks	<u>1,562,616</u>	<u>1,786,025</u>
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7b. RECONCILIATION OF CASH FLOW FROM OPERATING ACTIVITIES

Profit from ordinary activities	-	-
Adjustments for:		
Impairment losses on mortgage loans	-	-
Changes in operating assets and liabilities:		
Interest and other receivables	(819,627)	(213,026)
Payables and other liabilities	640,475	1,090,710
Cash inflows/(outflows) from operating activities	<u>(179,152)</u>	<u>877,684</u>

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS
FOR THE FINANCIAL YEAR ENDED 30 JUNE 2018

8. MORTGAGE LOANS AND INTEREST RECEIVABLE

	2018	2017
	\$	\$
Interest receivable		
Interest receivable	2,159,290	1,339,663
Provision for impairment losses (1)	-	-
	<u>2,159,290</u>	<u>1,339,663</u>
Mortgage loans		
With contractual terms:		
Maturing < 1 year	53,920,000	47,394,500
Maturing > 1 year	17,149,000	13,914,000
Mortgage loans before impairment loss	<u>71,069,000</u>	<u>61,308,500</u>
Provision for impairment losses*	<u>(644,634)</u>	<u>(644,634)</u>
	<u>70,424,366</u>	<u>60,663,866</u>

(1) The Scheme entered into an arrangement on 1 July 2009, which assigns certain interest receivable from current and prior periods to an entity related to the manager. For further information refer to Note 12.

*Refer Note 10 for management fee adjustment.

For information about the Scheme's exposure to credit risk, see Note 11.

The Scheme mortgage investments are secured by a registered first mortgage over real property.

At 30 June 2018 and 30 June 2017, the Responsible Entity reviewed the carrying value of interest receivable and mortgage loans of the Scheme in order to identify whether any loans or interest may be impaired.

In assessing whether mortgage loans or interest receivable were impaired, the Responsible Entity considerations included but were not limited to:

- Valuations of security properties completed by registered valuers;
- Appraisals of security properties completed by real estate agents;
- Actual sales prices realised on completed projects;
- Collateral security; and
- Estimated time to realise mortgage loans.

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS

FOR THE FINANCIAL YEAR ENDED 30 JUNE 2018

8. MORTGAGE LOANS AND INTEREST RECEIVABLE (CONT.)

Impairment

As a result of this review, the Responsible Entity did not record any impairment in respect of mortgage loans during the year (2017: \$ nil).

The unrealised impairment loss represents estimates of losses that may be incurred based on a number of assumptions including amounts that will be received upon repayment or sale of the security property and the period until funds are returned. In the current economic conditions there is uncertainty as to the amount that could be realised on the sale of security properties, and the time it may take to achieve a sale. Accordingly, actual impairment losses incurred may differ significantly from these estimates.

9. DISTRIBUTIONS PAID AND PAYABLE

	2018	2017
	\$	\$
Distributions paid	4,630,078	3,714,649
Distributions payable	198,798	176,733
	<u>4,828,876</u>	<u>3,891,382</u>

As investors are presently entitled to the distributable income of the Scheme, no income tax is payable by the Scheme.

10. MANAGEMENT FEES

	2018	2017
	\$	\$
Management fees paid and payable	2,904,382	2,192,930
	<u>2,904,382</u>	<u>2,192,930</u>

At 30 June 2018 an amount of \$1,393,982 (2017: \$596,417) is payable to the Manager for the year ended 30 June 2018. At year end an amount of \$644,634 has been recorded in relation to impairment losses on mortgage loans outstanding. In the event that the actual realised impairment is more or less than the estimate at 30 June 2018 the Manager's fee will be varied accordingly at the time the loss is reassessed or realised.

The Scheme entered into an arrangement on 1 July 2009, which assigns certain interest receivable from current and prior periods to an entity related to the Manager. For further information refer to Note 12.

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS
FOR THE FINANCIAL YEAR ENDED 30 JUNE 2018

11. FINANCIAL INSTRUMENTS

The Scheme's assets principally consist of financial instruments which comprise mortgage investments and interest receivable. It holds these investment assets in accordance with Product Disclosure Statement ("PDS"). The Scheme's investment strategy per the PDS is to invest in first mortgages only over commercial, rural and residential properties, including properties which require construction or development funding.

The allocation of assets as between the various sectors described above is determined by the Responsible Entity who manages the Scheme's portfolio of assets to achieve the Scheme's investment objectives.

The scheme's investing activities expose it to the following risks:

- Market risk
- Credit risk
- Liquidity risk
- Operational risk

Overview

The nature and extent of the financial instruments employed by the Scheme are discussed below. This note presents information about the Scheme's exposure to each of the above risks, the Scheme's objectives, policies and processes for measuring and managing risks. The Board of Directors of the Responsible Entity has overall responsibility for the establishment and oversight of the Scheme's risk management framework.

The Board of Directors is responsible for developing and monitoring the Scheme's risk management policies, including those related to its investment activities. The Responsible Entity's risk management policies are established to identify and analyse the risks faced by the Scheme, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions and the Scheme's activities. The Scheme, through training, management standards and procedures, aims to develop a disciplined and constructive control environment in which all staff understand their roles and obligations.

The Board monitors compliance with the Scheme's risk management procedures and reviews the adequacy of the risk management framework in relation to the risks faced by the Scheme.

The Scheme's assets principally consist of loans secured by registered first mortgages over real property, interest receivable and cash investments. It holds these investment assets at the discretion of the Responsible Entity in accordance with the Scheme's constitution and Product Disclosure Statement.

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**NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS
FOR THE FINANCIAL YEAR ENDED 30 JUNE 2018**

11. FINANCIAL INSTRUMENTS (CONT.)

Overview (cont.)

As the Scheme is a contributory mortgage scheme, the risk of losses from a loan are attributable directly to the investors in that loan.

Interest rate risk is the risk that changes in interest rates will affect the Scheme's income or the value of its holdings of financial instruments. Interest rate risk embodies the potential for both loss and gains. The objective of interest rate risk management is to manage and control interest rate risk exposures within acceptable parameters, while optimising the return on risk.

Interest rate risk is managed by the Board who meet regularly to monitor and review interest rates.

Currency risk

The Scheme is not exposed to any currency risk as all transactions are performed in their functional currency, being Australian dollars.

Interest rate risk

The majority of the Scheme's financial assets and financial liabilities are interest bearing. Interest-bearing financial assets and financial liabilities generally mature in the short-term. As a result, the Scheme is subject to limited exposure to fair value interest rate risk due to fluctuations in the prevailing levels of market interest rates. Any excess cash is invested in an interest-bearing deposit account with an Australian regulated banking institution.

The Scheme's overall interest rate risk is monitored on a monthly basis by the Board of Directors.

Property value risk

The majority of the Scheme's financial assets are secured by registered first mortgages over real property. As a result, the Scheme is subject to property value risk being fluctuations in the prevailing levels of property market values.

The Scheme's property value risk is managed on a regular basis by management in accordance with policies and procedures in place, including but not limited to the adoption of maximum initial loan to valuation ratios of 80%, with target ratios less than 70%.

In prior years, the property and financial services sectors have experienced significant adverse market conditions. Should these conditions arise, this may result in a decline in property values, which should they be significant, may result in diminished security values, which may result in losses should properties held as security be realised below the loan and receivable book values.

As the Scheme is a contributory mortgage scheme, loan losses are attributable directly to the investors in a loan.

**FIRST MORTGAGE INVESTMENTS
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**NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS
FOR THE FINANCIAL YEAR ENDED 30 JUNE 2018**

11. FINANCIAL INSTRUMENTS (CONT.)

Operational Risk

Operational risk is the risk of direct loss arising from a wide variety of causes associated with the Scheme's processes, personnel, technology and infrastructure, and from external factors other than credit, market and liquidity risks such as those arising from legal and regulatory requirements and generally accepted standards of corporate behaviour. Operational risks arise from all of the Scheme's operations.

The objective of the Responsible Entity of the Scheme is to manage operational risk so as to balance the avoidance of financial losses and damage of the Group's reputation with overall cost effectiveness and to avoid control procedures that restrict initiative and creativity.

The primary responsibility for the development and implementation of controls to address operational risk is assigned to the Responsible Entity. The responsibility is supported by the development of overall standards for the management of operational risk in the following areas:

- Requirements for appropriate segregation of duties, including the independent authorisation of transactions
- Requirements for the reconciliation and monitoring of transactions compliance with regulatory and other legal requirements
- Documentation of controls and procedures
- Training and professional development
- Risk mitigation, including insurance where this is effective

FIRST MORTGAGE INVESTMENTS
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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS

FOR THE FINANCIAL YEAR ENDED 30 JUNE 2018

11. FINANCIAL INSTRUMENTS (CONT.)

Market risk

Interest rate profile

At reporting date the interest rate profile of the Scheme's interest-bearing financial instruments prior to impairment losses was:

	Carrying amount	
	2018	2017
Fixed rate instruments		
Financial assets	71,069,000	61,308,500
Financial liabilities	(70,895,470)	(61,179,227)
	<u>173,530</u>	<u>129,273</u>

	Carrying amount	
	2018	2017
Variable rate instruments		
Financial assets	<u>1,562,616</u>	<u>1,786,025</u>

Cash flow sensitivity analysis for variable rate instruments

A change of 100 basis points in interest rates at the balance date would have increased/(decreased) profit or loss by \$1,563 (2017: \$1,786).

Credit risk

Credit risk is the risk that a counterparty to a financial instrument will fail to discharge an obligation or commitment that it has entered into with the Scheme. The Scheme has a credit policy in place and the exposure to credit risk is monitored on an ongoing basis. The Scheme's maximum exposure to credit risk at the reporting date was:

	Carrying amount	
	2018	2017
Loans and receivables – after unrealised impairment losses	70,424,366	60,663,866
Cash and cash equivalents	1,562,616	1,786,025
Interest receivable	2,159,290	1,339,663
	<u>74,146,272</u>	<u>63,789,554</u>

FIRST MORTGAGE INVESTMENTS
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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS
FOR THE FINANCIAL YEAR ENDED 30 JUNE 2018

11. FINANCIAL INSTRUMENTS (CONT.)

Credit risk (cont.)

Exposure to credit risk

The Scheme's maximum exposure to credit risk for mortgage investments at reporting date by geographic region was:

	Carrying amount	
	2018	2017
Victoria	8,967,000	6,268,000
New South Wales	17,220,366	14,587,613
Queensland	44,192,000	39,594,218
Australian Capital Territory	-	169,035
Northern Territory	45,000	45,000
	<u>70,424,366</u>	<u>60,663,866</u>

The Scheme's maximum exposure to credit risk for mortgage investments at the reporting date by mortgage investment type was:

	Carrying amount	
	2018	2017
Commercial	5,506,000	3,319,620
Vacant land	10,237,000	13,673,470
Residential and rural	<u>54,681,366</u>	<u>43,670,776</u>
Total after impairment losses	<u>70,424,366</u>	<u>60,663,866</u>

Impairment

The ageing of the Scheme's mortgage investments at reporting date was:

	Gross	Impairment	Gross	Impairment
	2018	2018	2017	2017
Not past due	50,242,000	-	44,281,500	-
Past due 0-30 days	10,081,000	-	1,165,000	-
Past due 31-120 days	4,090,000	-	1,651,000	-
Past due 121 days to one year	4,902,000	-	4,907,000	-
More than one year	1,754,000	644,634	9,304,000	644,634
	<u>71,069,000</u>	<u>644,634</u>	<u>61,308,500</u>	<u>644,634</u>

FIRST MORTGAGE INVESTMENTS
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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS

FOR THE FINANCIAL YEAR ENDED 30 JUNE 2018

11. FINANCIAL INSTRUMENTS (CONT.)

Credit risk (cont.)

The ageing of the Scheme's interest receivable at reporting date was:

	Gross 2018	Impairment 2018	Gross 2017	Impairment 2017
Not past due	-	-	-	-
Past due 0-30 days	148,014	-	119,714	-
Past due 31-120 days	267,040	-	168,950	-
Past due 121 days to one year	333,095	-	232,071	-
More than one year	1,411,141	-	818,928	-
	<u>2,159,290</u>	<u>-</u>	<u>1,339,663</u>	<u>-</u>

The movement in the provision for impairment losses in respect of mortgage investments during the year was as follows:

	2018 \$	2017 \$
Balance at 1 July	644,634	644,634
Provision for impairment loss recognised/(reversal)	-	-
Impairment realised on mortgage loans repaid	-	-
Balance at 30 June	<u>644,634</u>	<u>644,634</u>

The provision for impairment loss of mortgage loans and interest receivable is used to record impairment losses unless the Scheme is satisfied that no recovery of the amount owing is possible, at that point the amount is considered irrecoverable and is written off against the mortgage loan directly.

In situations where the borrower cannot meet the holding costs the Scheme has taken possession of the security with a view to controlling the marketing and sale of the security property.

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**NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS
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11. FINANCIAL INSTRUMENTS (CONT.)

Credit risk (cont.)

The Scheme mortgage investments are secured by a registered first mortgage over real property. Credit risk for mortgage loans is mitigated by the Scheme establishing a Prudential Lending Manual which requires the Board of Directors of the Responsible Entity to obtain a valuation that must be not more than 6 months old at the time of mortgage loan approval and conduct a range of searches on both the mortgage investment and secured property. Such searches include credit reference searches, bankruptcy searches, valuation reports and insurance searches. In addition, proof of serviceability for each new mortgage investment is also obtained. The Board of Directors monitors mortgage investments on a monthly basis.

The Scheme has no exposure to mortgage investments that individually exceeds 5% (2017: 5%) of the total value of mortgage loans.

Liquidity risk

Liquidity risk is the risk that the Scheme will not be able to meet its financial obligations as they fall due. The Scheme's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under normal conditions, without incurring unacceptable losses or risking damage to the Scheme's reputation.

In accordance with the Constitution and the Product Disclosure Statement ("PDS"), as the Scheme is a contributory fund, the redeeming of investment funds prior to the repayment of the associated mortgage loan is not readily available. Funds can only be redeemed if an alternative investor can be found.

The Scheme's liquidity risk is managed on a monthly basis by the Board of Directors in accordance with the policies and procedures in place.

The Responsible Entity manages its liquidity by:

- Offering investments with fixed maturity terms of usually 12 to 24 months;
- Lending to borrowers with first mortgage security for periods generally not exceeding 24 months only where borrowers meet the Scheme's lending criteria; and
- Having the ability under the Scheme's Constitution and Product Disclosure Statement to only pay redemptions upon the repayment of the applicable mortgage loans.

FIRST MORTGAGE INVESTMENTS
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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS

FOR THE FINANCIAL YEAR ENDED 30 JUNE 2018

11. FINANCIAL INSTRUMENTS (CONT.)

Liquidity risk (cont.)

The following are the contractual maturities of financial liabilities, excluding interest payments and excluding the impact of netting agreements:

2018	Carrying value \$	Contractual cash flows \$	0-3 months \$	3-6 months \$	6-12 months \$	12-24 months \$	> 2 years \$
Members distributions payable	198,798	198,798	198,798	-	-	-	-
Other payables	1,212,654	1,212,654	474,984	135,225	309,831	292,614	-
Manager fees payable	1,393,982	1,393,982	1,393,982	-	-	-	-
Net assets attributable to investors	70,895,470	70,895,470	27,769,030	7,905,649	18,113,663	17,107,128	-
TOTAL	73,700,904	73,700,904	29,836,794	8,040,874	18,423,494	17,399,742	
2017	Carrying value \$	Contractual cash flows \$	0-3 months \$	3-6 months \$	6-12 months \$	12-24 months \$	> 2 years \$
Members distributions payable	176,733	176,733	176,733	-	-	-	-
Other payables	1,567,625	1,567,625	585,336	249,762	376,753	355,774	-
Manager fees payable	596,417	596,417	596,417	-	-	-	-
Net assets attributable to investors	61,179,227	61,179,227	22,843,731	9,747,404	14,703,431	13,884,661	-
TOTAL	63,520,002	63,520,002	24,202,217	9,997,166	15,080,184	14,240,434	-

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS

FOR THE FINANCIAL YEAR ENDED 30 JUNE 2018

11. FINANCIAL INSTRUMENTS (CONT.)

Liquidity risk (cont.)

Fair values versus carrying amounts

The Directors consider that the fair value of financial assets and liabilities of the Scheme approximate their carrying amounts.

12. RELATED PARTIES

Responsible Entity

The Responsible Entity of First Mortgage Investments during the financial year was First Mortgage Managed Investments Limited (ABN 39 089 507 899).

Key management personnel

The Scheme does not employ people in its own right. However it is required to have an incorporated Responsible Entity to manage the activities of the Scheme and this is considered the key management personnel. The directors of the Responsible Entity are key management personnel of that entity and their names are:

Name	Period of directorship
Mr Michael Henry Boyce	Appointed 15 September 1999
Ms Karen Joan Scott	Appointed 15 September 1999
Ms Megan Kay Boyce	Appointed 3 March 2014

The manager is entitled to a management fee which is based on the margin between interest income and distributions to investors.

No compensation is paid to directors directly by the Scheme or to any of the key management personnel of the Responsible Entity.

Related party investments held by the Scheme

The scheme has no investment in the key management personnel related parties or their associates (2017: nil).

Key management personnel loan disclosures

The Scheme has not made, guaranteed or secured, directly or indirectly, any loans to the key management personnel or their personally related entities at any time during the reporting period (2017: nil).

FIRST MORTGAGE INVESTMENTS
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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS
FOR THE FINANCIAL YEAR ENDED 30 JUNE 2018

12. RELATED PARTIES (CONT.)

Other transactions within the Scheme

Apart from those details disclosed in this note, no key management personnel has entered into a material contract with the Scheme since the end of the previous year and there were no material contracts involving such interests subsisting at year end (2017: nil).

Related party transactions

The following fees were paid by the Scheme to associates of the Responsible Entity during the financial year:

	2018	2017
	\$	\$
Management fees for the year, paid and payable to First Mortgage Investments Pty Ltd by the Scheme under the terms of the Service Agreement between that company and the Responsible Entity, net of reduction or increment in management fee to offset impairment losses or reversal of impairment. For the year ended 30 June 2018, there was no adjustment to the management fee (2017: nil)	2,904,382	2,192,930
<i>Balances with related parties</i>		
Fees (payable to)/receivable from related parties by the Scheme at balance date are as follows:		
First Mortgage Investments Pty Ltd	(1,393,982)	(596,417)

First Mortgage Investments Pty Ltd is entitled to recover from borrowers interest paid under the Income Protection Plan. Under the Income Protection Plan, in the event that a borrower defaults or is late in making interest payments, First Mortgage Investments Pty Ltd may advance funds equivalent to the Scheme to fund the income payments. These funds are reimbursed to First Mortgage Investments Pty Ltd upon receipts of the monies from borrowers.

The Scheme entered into an arrangement on 1 July 2009, which was formalised by a Deed of Assignment dated 28 October 2010, the arrangement assigns certain interest receivable from current and prior periods to First Mortgage Investments Pty Ltd, an entity related to the manager. During the year an amount of \$135,120 (2017: \$262,704) was assigned to First Mortgage Investments Pty Ltd and the total interest assigned at 30 June 2018 for loans outstanding at that date was \$2,480,622 (2017: \$2,478,357)

FIRST MORTGAGE INVESTMENTS
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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS
FOR THE FINANCIAL YEAR ENDED 30 JUNE 2018

12. RELATED PARTIES (CONT.)

If the Scheme had not entered into this arrangement, total impairment losses at 30 June 2018 of \$2,480,622 (2017: \$2,478,357) in relation to the assigned interest receivable on mortgage loans may have been incurred by the Scheme to date on loans outstanding at 30 June 2018.

Members investing activities

Detailed below are investments in the Scheme by the Responsible Entity or its related parties, as referred to in the scheme's Register of Related Parties.

Entity	Value of investment at 1 July \$	Value of investment at year end \$	Interest held in scheme at year end	Amount invested during the year \$	Amounts withdrawn during the year \$	Distributions paid \$
30 June 2018						
First Mortgage Investments Pty Ltd	5,539,500	7,227,500	10.19%	13,923,500	(12,235,500)	588,857
Other director related entities – associates of Michael Boyce and Megan Boyce	5,694,150	6,758,150	9.53%	1,064,000	-	438,936
Other director related entities – associates of Karen Scott	220,000	290,000	0.41%	70,000	-	15,151
30 June 2017						
First Mortgage Investments Pty Ltd	993,050	5,539,500	9.05%	9,300,300	(4,753,850)	101,212
Other director related entities – associates of Michael Boyce and Megan Boyce	4,169,300	5,694,150	9.31%	1,524,850	-	340,300
Other director related entities – associates of Karen Scott	105,000	220,000	0.36%	115,000	-	7,541

These investments are on normal terms and conditions as provided to other members. First Mortgage Investments Pty Ltd invests in the Scheme from time to time on a short-term basis to provide sufficient funds for certain mortgage investments to be fully funded. These investments are withdrawn when other investors' funds are obtained.

13. CONTINGENCIES

There are no contingent liabilities at 30 June 2018 or 30 June 2017.

FIRST MORTGAGE INVESTMENTS
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14. EVENTS SUBSEQUENT TO REPORTING DATE

There has not arisen in the interval between the end of the financial year and the date of this report any item, transaction or event of a material and unusual nature likely, in the opinion of the Responsible Entity, to affect significantly the operations of the Scheme, the results of those operations, or the state of affairs of the Scheme, in future financial years.

FIRST MORTGAGE INVESTMENTS
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DIRECTORS' DECLARATION

In the opinion of the directors of First Mortgage Managed Investments Limited, Responsible Entity of First Mortgage Investments:

1. The financial statements and notes set out on pages 6 to 31, are in accordance with the *Corporations Act 2001*, including:
 - (a) giving a true and fair view of the financial position of the Scheme as at 30 June 2018, and of its performance, as presented by the results of its operations and its cash flows for the year ended on that date; and
 - (b) complying with Australian Accounting Standards and the *Corporations Regulations 2001*; and
2. There are reasonable grounds to believe that the Scheme will be able to pay its debts as and when they become due and payable.
3. The directors draw attention to Note 2(a) to the financial statement, which includes a statement of compliance with International Financial Reporting Standards.

Signed in accordance with a resolution of the directors of First Mortgage Managed Investments Limited.

Dated at Burleigh this 13th day of September 2018.



Karen Scott
Director
Burleigh Heads

Independent Auditor's Report

To the members of First Mortgage Investments

Opinion

We have audited the **Financial Report** of the First Mortgage Investments (the Scheme).

In our opinion, the accompanying **Financial Report** of the First Mortgage Investments Scheme is in accordance with the *Corporations Act 2001*, including

- giving a true and fair view of the Scheme's financial position as at 30 June 2018, and of its financial performance and its cash flows for the year ended on that date; and
- complying with *Australian Accounting Standards* and the *Corporations Regulations 2001*.

The **Financial Report** comprises the:

- Statement of financial position as at 30 June 2018
- Statement of profit or loss and other comprehensive income for the year then ended
- Statement of changes in equity, and Statement of cash flows for the year then ended
- Notes including a summary of significant accounting policies
- Directors' Declaration.

Basis for opinion

We conducted our audit in accordance with *Australian Auditing Standards*. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the Financial Report* section of our report.

We are independent of the Scheme in accordance with the *Corporations Act 2001* and the relevant ethical requirements of the *Accounting Professional and Ethical Standards Board's APES 110 Code of Ethics for Professional Accountants* (the Code). We have fulfilled our other ethical responsibilities in accordance with the Code.

Other Information

Other Information is financial and non-financial information in the First Mortgage Investments Scheme's annual reporting which is provided in addition to the Financial Report and the Auditor's Report. This includes the Responsible Entity's Report. The Directors of First Mortgage Managed Investments Limited (the Responsible Entity) are responsible for the Other Information.

The Other Information we obtained prior to the date of this Auditor's Report was the Responsible Entity's Report.

Our opinion on the Financial Report does not cover the Other Information and, accordingly, the auditor does not express any form of assurance conclusion thereon.

In connection with our audit of the Financial Report, our responsibility is to read the Other Information. In doing so, we consider whether the Other Information is materially inconsistent with the Financial Report or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

We are required to report if we conclude that there is a material misstatement of this Other Information, and based on the work we have performed on the Other Information that we obtained prior to the date of this Auditor's Report we have nothing to report.

Responsibilities of Directors for the Financial Report

The Directors of First Mortgage Managed Investments Limited (the Responsible Entity) are responsible for:

- preparing the Financial Report that gives a true and fair view in accordance with *Australian Accounting Standards* and the *Corporations Act 2001*;
- implementing necessary internal control to enable the preparation of a Financial Report that gives a true and fair view and is free from material misstatement, whether due to fraud or error; and
- assessing the Scheme's ability to continue as a going concern and whether the use of the going concern basis of accounting is appropriate. This includes disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless they either intend to liquidate the Scheme or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the Financial Report

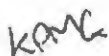
Our objective is:

- to obtain reasonable assurance about whether the Financial Report as a whole is free from material misstatement, whether due to fraud or error; and
- to issue an Auditor's Report that includes our opinion.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with *Australian Auditing Standards* will always detect a material misstatement when it exists.

Misstatements can arise from fraud or error. They are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of this Financial Report.

A further description of our responsibilities for the Audit of the Financial Report is located at the Auditing and Assurance Standards Board website at:
http://www.auasb.gov.au/auditors_responsibilities/ar4.pdf. This description forms part of our Auditor's Report.



KPMG



JJ Frazer
Partner

Burleigh Heads

13 September 2018