



**Bendigo**Wealth

# Sandhurst Select Mortgage Fund

**Annual Report 2011**

ARSN 090 909 069

Issued by **Sandhurst Trustees**

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# Directors' report

## Report of the Directors of the Responsible Entity

The directors of Sandhurst Trustees Limited (ABN 16 004 030 737), the 'Responsible Entity', present this report on the Sandhurst Select Mortgage Fund (the Fund) for the year ended 30 September 2011.

## Managed investment scheme

The Fund is a managed investment scheme registered by the Australian Securities and Investments Commission in accordance with the Corporations Act 2001. The Fund was established on 16 September 1996 and issued its first offer document on 1 October 1996.

## Directors

The name of each person who has been a director of Sandhurst Trustees Limited, during the financial year and to the date of this report are:

Jennifer L Dawson (Chairman)

Ian G Mansbridge

Marnie A Baker

John A Billington

Jennifer Dawson and Ian Mansbridge are non-executive directors, Jennifer Dawson is also a non-executive director of Bendigo and Adelaide Bank Limited, of which Sandhurst Trustees Limited is a wholly owned subsidiary company. Marnie Baker and John Billington are employed and paid as executives or senior management of Bendigo and Adelaide Bank Limited. Complementing the board is an independent compliance committee, responsible for ensuring that the activities of the Responsible Entity in relation to the Fund comply with obligations imposed by specified legislation and associated policies promulgated by government agencies.

## Net operating income

The net profit attributable to investors for the year ended 30 September 2011 was \$56,282,654 (2010: \$50,797,592).

## Indirect Cost Ratio

The Indirect Cost Ratio (ICR) is the ratio of the Fund's management costs over the Fund's average net assets attributable for the year, expressed as a percentage.

Management costs include management fees and other expenses or reimbursements deducted in relation to the Fund, but do not include interest expense and transactional such as brokerage.

The ICR for the Fund for the year ended 30 September 2011 was 1.11% (2010: 1.09%).

## Significant changes in state of affairs

No significant changes in the Fund's state of affairs occurred during the year.

## Principal activity

The principal activity of the Fund during the year was to provide competitive returns, regular income and capital stability by investment of the Fund in a broad selection of Australian first registered mortgage assets and other interest rate securities.

No significant change in the nature of this activity occurred during the year.

## After balance date events

No matters or circumstances have arisen since the end of the year that significantly affected or may significantly affect the operations of the Fund, the results of those operations, or the state of affairs of the Fund in subsequent financial years.

## Future developments

The Fund intends to continue to invest in accordance with its investment strategy.

## Distributions

During the year ended 30 September 2011 \$56,282,654 was distributed to investors as interest income.

## Options

No options over interests in the Fund were granted during or since the end of the year and there were no options outstanding at the date of this report.

## Indemnities and insurance premiums for officers or auditors

The Constitution of the Responsible Entity requires it to indemnify all current and former officers of the Responsible Entity (but not including auditors) out of the property of the Responsible Entity, against any liability incurred by the officer in or arising out of the conduct of the business of the Responsible Entity or in or arising out of the discharge of the duties of the officer, unless the liability was incurred by the officer through his or her own dishonesty, negligence, lack of good faith or breach of duty.

The Responsible Entity is indemnified from the assets of the Fund for any loss or liability incurred by it in the management and administration of the Fund. The Fund has not directly indemnified or made a relevant agreement for indemnifying against a liability any person who is or has been an auditor of the Fund.

During the financial year the Responsible Entity paid a premium under a contract insuring each director of the Responsible Entity against liability and legal expenses incurred in their respective capacities. Such insurance contracts insure against certain liability (subject to specified exclusions) for persons who are or have been directors of the Responsible Entity or executive officers of the Responsible Entity.

Disclosure of the nature of the liability and the amount of the premium is prohibited by the confidentiality clause of the contract of insurance. The Responsible Entity has not provided any insurance to a related body corporate or to an auditor of the Responsible Entity.

## Proceedings on behalf of the Fund

No person has applied for leave of a court to bring proceedings on behalf of the Fund or intervene in any proceedings to which the Fund is a party for the purpose of taking responsibility on behalf of the Fund for all or any part of those proceedings.

The Fund was not a party to any such proceedings during the year.

## Environmental regulation and expected results

The operations of the Fund are not subject to any particular or significant environmental regulation under a law of the Commonwealth or of a State or Territory. There have been no known significant breaches of any other environmental requirements applicable to the Fund.

## Rounding

The amounts contained in the Financial Report and the Directors' Report have been rounded off under the option under ASIC Class Order 98/100. The Fund is an entity to which the Class Order applies, and in accordance with that Class Order, amounts in the Financial Report have been rounded to the nearest thousand dollars.

## Other information

During the year ended 30 September 2011 the total assets of the Fund decreased by \$38,308,709 to \$1,006,361,706.

For details of any interests the Responsible Entity and its associates may hold in the Fund, refer to Note 14 — Related party disclosures of the Notes to the Financial Statements.

Fees paid to the Responsible Entity and its associates during the year were \$17,226,859 (2010: \$18,994,103).

Signed in accordance with a resolution of the board of directors.



**Jennifer L Dawson**

Director

Bendigo

24 November 2011

## Auditor independence declaration

The directors received the following declaration from the auditor of the Fund:

Auditor's Independence Declaration to the directors of Sandhurst Trustees Limited, as Responsible Entity for the Fund

In relation to our audit of the Financial Report of the Fund for the year ended 30 September 2011, to the best of my knowledge and belief, there have been no contraventions of the auditors independence requirements of the Corporations Act 2001 or any applicable code of professional conduct.



**Warren Sinnott**

Partner

Richmond Sinnott & Delahunty

24 November 2011

# Statement of Comprehensive Income

## Sandhurst Select Mortgage Fund

For the year ended 30 September 2011

	<b>2011</b> <b>\$'000</b>	<b>2010</b> <b>\$'000</b>
<b>Revenues from ordinary activities</b>		
Interest revenue		
Mortgage loans	65,185	65,176
Bank accepted bills	137	-
Negotiable certificates of deposit	5,745	4,456
Other interest bearing deposits	2,479	2,476
Other revenues from ordinary activities	818	576
	<b>74,364</b>	<b>72,684</b>
<b>Expenses from ordinary activities</b>		
Trustee management fee	10,237	10,932
Loan originator management and trailer fees	7,023	8,226
Annual report costs	-	12
Product disclosure statement costs	8	29
Legal fees	(8)	9
Audit and accounting fees	31	27
Interest expense	498	2,609
Other expenses from ordinary activities	292	42
	<b>18,081</b>	<b>21,886</b>
<b>Net profit attributable to investors</b>	<b>56,283</b>	<b>50,798</b>
Interest paid / payable	56,283	50,798
Hedge accounting adjustments under AIFRS	2,636	(862)
<b>Change in net assets attributable to investors</b>	<b>(2,636)</b>	<b>862</b>

The accompanying notes form part of these accounts.

# Statement of Financial Position

## Sandhurst Select Mortgage Fund

As at 30 September 2011

	Note	2011 \$'000	2010 \$'000
<b>Current assets</b>			
Cash assets	2	16,909	17,311
Receivables	3	4,637	7,053
Investments	4		
Held to Maturity		134,967	90,811
Loans and Advances		114,294	131,706
<b>Total current assets</b>		<b>270,807</b>	<b>246,881</b>
<b>Non-current assets</b>			
Investments	4		
Held to Maturity		43,052	32,075
Loans and Advances		692,502	765,715
<b>Total non-current assets</b>		<b>735,554</b>	<b>797,790</b>
<b>Total assets</b>		<b>1,006,361</b>	<b>1,044,671</b>
<b>Current liabilities</b>			
Payables	5	5,743	51,428
<b>Total current liabilities</b>		<b>5,743</b>	<b>51,428</b>
<b>Total liabilities excluding net assets attributable to investors</b>		<b>5,743</b>	<b>51,428</b>
<b>Net Assets</b>		<b>1,000,618</b>	<b>993,243</b>
<b>Net assets attributable to investors</b>			
Investors' funds	6	991,442	982,326
Investors' accrued interest	6	14,090	13,195
Hedge accounting adjustments under AIFRS		(4,914)	(2,278)
<b>Total net assets attributable to investors</b>		<b>1,000,618</b>	<b>993,243</b>

The accompanying notes form part of these accounts.

# Statement of Changes in Net Assets Attributable to Investors

## Sandhurst Select Mortgage Fund For the year ended 30 September 2011

	2011 \$'000	2010 \$'000
<b>Opening balance</b>	993,243	1,185,213
Contributions	470,464	391,515
Interest earned	56,283	50,798
Redemptions	(461,348)	(586,496)
Interest paid	(55,388)	(48,649)
Hedge accounting adjustments under AIFRS	(2,636)	862
<b>Closing balance</b>	<b>1,000,618</b>	<b>993,243</b>

The accompanying notes form part of these accounts.

# Statement of Cash Flows

## Sandhurst Select Mortgage Fund For the year ended 30 September 2011

	Note	2011 \$'000	2010 \$'000
<b>Cash flows from operating activities</b>			
Interest received		76,282	69,372
Interest paid		(55,388)	(48,649)
Trustee management fees		(10,194)	(10,863)
Origination and trailer fees		(7,038)	(8,062)
Other revenue		396	443
Other expenses		(1,068)	(2,436)
<b>Net cash provided by / (used in) operating activities</b>	<b>7(c)</b>	<b>2,990</b>	<b>(195)</b>
<b>Cash flows from investing activities</b>			
(Purchases) and sales of investment securities		(55,133)	10,732
Mortgage loans (advanced) and repaid		90,625	127,028
<b>Net cash provided by / (used in) investing activities</b>		<b>35,492</b>	<b>137,760</b>
<b>Cash flows from financing activities</b>			
Amount borrowed / (repaid) via liquidity facility		(48,000)	48,000
Net increase/(decrease) in investors' funds		9,116	(194,981)
<b>Net cash provided by / (used in) financing activities</b>		<b>(38,884)</b>	<b>(146,981)</b>
<b>Net increase / (decrease) in cash held</b>		<b>(402)</b>	<b>(9,416)</b>
Cash at the beginning of the financial year		17,311	26,727
<b>Cash at the end of the financial year</b>	<b>7(a)</b>	<b>16,909</b>	<b>17,311</b>

The accompanying notes form part of these accounts.

# Notes to the Financial Statements

## Sandhurst Select Mortgage Fund For the year ended 30 September 2011

### 1. Statement of accounting policies

#### (a) Basis of preparation of the financial report

The financial report is a general purpose financial report which has been prepared in accordance with the requirements of the Corporations Act 2001 which includes applicable Accounting Standards. Other mandatory professional reporting requirements (Urgent Issues Group Consensus Views) have also been complied with.

The financial report has been prepared on the basis of historical costs, except for the valuation of investments in financial assets, which have been measured at fair value or amortised cost.

The financial report is presented in Australian dollars and all values are rounded to the nearest thousand dollars (\$'000) unless otherwise stated under the option available to the Fund under ASIC Class Order 98/100. The Fund is an entity to which the Class Order applies.

The financial report was authorised for issue in accordance with a resolution of the Directors of the Responsible Entity on 24 November 2011.

#### (b) Statement of Compliance

The financial report complies with Australian Accounting Standards, which include Australian equivalents to International Financial Reporting Standards (AIFRS). Compliance with AIFRS ensures that the financial report, comprising the financial statements and notes thereto, complies with International Financial Reporting Standards (IFRS).

### (c) Valuation of investments

Investments and financial assets in the scope of AASB 139 Financial Instruments: Recognition and Measurement are categorised as either financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments, or available-for-sale financial assets. The classification depends on the purpose for which the investments were acquired or originated. Designation is re-evaluated at each reporting date, but there are restrictions on reclassifying to other categories. When financial assets are recognised initially, they are measured at fair value. In the case of assets not measured at fair value through profit or loss, they include any directly attributable transaction costs.

#### (i) Held-to-maturity investments

All negotiable certificates of deposit (NCDs), term deposits (TDs), residential mortgage backed securities (RMBS) and bank accepted bills (BABs) held by the Fund are classified as “held to maturity” investments. These investments are initially recorded at fair value on recognition and are subsequently measured at amortised cost using the effective interest method, with interest and impairment costs being recognised in the Statement of Comprehensive Income. These investments are not classified as “available for sale” investments as sufficient funds are held on 11 am account to meet day-to-day financing needs, therefore no NCDs, TDs, RMBS or BABs are sold prior to maturity.

#### (ii) Loans and advances

All mortgage and loan investments held by the Fund are classified as “loans and advances”. These investments are initially recorded at fair value on recognition and are then measured at amortised cost using the effective interest method, with interest and impairment costs being recognised in the Statement of Comprehensive Income.

## 1. Statement of accounting policies (cont.)

### (d) Derivative financial instruments and hedging

The Fund uses derivative financial instruments to hedge interest rate risk (including forward exchange contracts and interest rate swap contracts). Such derivative financial instruments are recorded at fair value. The fair value of forward exchange contracts is calculated by reference to current forward exchange rates with similar maturity profiles. The fair value of interest rate swap contracts is determined by reference to market values for similar instruments.

For the purposes of hedge accounting, hedges are classified as:

- fair value hedges when they hedge the exposure to changes in the fair value of a recognised asset or liability, or
- cash flow hedges where they hedge exposure to variability in cash flows that is either attributable to a particular risk associated with a recognised asset or liability or a forecast transaction. The Fund currently has cash flow hedges attributable to payment of interest on borrowings.

Hedges that meet the strict criteria for hedge accounting are accounted for as follows:

#### **(i) Fair value hedges**

For fair value hedges, any gain or loss from remeasuring the hedging instrument at fair value is recognised immediately in the Statement of Comprehensive Income. Any gain or loss attributable to the hedged risk on remeasurement of the hedged item is adjusted against the carrying amount of the hedged item and recognised in the Statement of Comprehensive Income. Where the adjustment is to the carrying amount of a hedged interest-bearing financial instrument, the adjustment is amortised to the Statement of Comprehensive Income such that it is fully amortised by maturity.

#### **(ii) Cash flow hedges**

For cash flow hedges, to hedge firm commitments which meet the conditions for special hedge accounting, the portion of the gain or loss on the hedging instrument that is determined to be an effective hedge is recognised

directly in net assets attributable to investors (“equity”) and the ineffective portion is recognised in the Statement of Comprehensive Income.

When the hedged firm commitment results in the recognition of an asset or liability, then, at the time the asset or liability is recognised, the associated gains or losses that had previously been recognised in equity are included in the initial measurement of the acquisition cost or other carrying amount of the asset or liability. For all other cash flow hedges, the gains or losses that are recognised in equity are transferred to the Statement of Comprehensive Income in the same year in which the hedged firm commitment affects the net profit and loss, for example when the future sale actually occurs.

For derivatives that do not qualify for hedge accounting, any gains or losses arising from changes in fair value are taken directly to the Statement of Comprehensive Income for the year.

Hedge accounting is discontinued when the hedging instrument expires or is sold, terminated or exercised, or no longer qualifies for hedge accounting. At that point in time, any cumulative gain or loss on the hedging instrument recognised in equity (net assets attributable to investors) is kept in equity until the forecast transaction occurs. If a hedged transaction is no longer expected to occur, the net cumulative gain or loss recognised in equity is transferred to the Statement of Comprehensive Income for the year.

#### (e) Income and expenditure

Income from investments is brought to account on a daily accrual basis. Expenses are also brought to account on a daily accrual basis.

#### (f) Income tax

Under the current Income Tax legislation the Fund is not liable to Income Tax, as all income is distributable to investors. The new Legislation Taxation of Financial Arrangements (TOFA) has been implemented effective 1 July 2010. The regime aims to align the tax and accounting treatment of financial arrangements. The Fund made a transitional election to bring pre-existing arrangements into TOFA.

## 1. Statement of accounting policies (cont.)

### (g) Application of Accounting Standards

Australian Accounting Standards and Urgent Issues Group Interpretations that have been recently issued or amended but are not yet effective have not been adopted for the annual reporting period ended 30 September 2011.

## 2. Cash assets

	<b>2011</b>	<b>2010</b>
	<b>\$'000</b>	<b>\$'000</b>
Cash at bank	486	686
11AM call deposits	10,113	10,534
Treasury settlement account	6,310	6,091
	<b>16,909</b>	<b>17,311</b>

Deposit taking, lending and investing facilities for the Fund are supplied by Bendigo and Adelaide Bank Limited, the parent entity of the Responsible Entity. The net position of all Fund transactions undertaken by Bendigo and Adelaide Bank Limited is settled daily in arrears via the treasury settlement account.

## 3. Receivables

Sundry debtors	3,496	3,637
Accrued interest	413	405
Loan repayments	728	3,011
	<b>4,637</b>	<b>7,053</b>

Terms and conditions - all receivables are non-interest bearing. Sundry debtors and accrued interest generally have payment terms of between 30 and 90 days.

## 4. Investments

	2011 \$'000	2010 \$'000
<b>Current</b>		
Held to Maturity		
Negotiable certificates of deposit	134,967	90,811
Loans and Advances		
Mortgage loans	114,294	131,706
	<b>249,261</b>	<b>222,517</b>
<b>Non-current</b>		
Held to Maturity		
Bank bills	10,986	-
RMBS	32,066	32,057
Loans and Advances		
Mortgage loans	692,502	765,715
	<b>735,554</b>	<b>797,772</b>
<b>Maturity analysis - investment securities</b>		
At call	-	-
Not longer than 3 months	132,200	73,148
Longer than 3 months and not longer than 12 months	13,753	17,663
Longer than 1 year and not longer than 5 years	-	-
Longer than 5 years	32,066	32,075
	<b>178,019</b>	<b>122,886</b>

## 4. Investments (cont.)

	<b>2011</b> <b>\$'000</b>	<b>2010</b> <b>\$'000</b>
<b>Maturity analysis - mortgage loans</b>		
At call	-	-
Not longer than 3 months	52,887	48,592
Longer than 3 months and not longer than 12 months	61,407	83,225
Longer than 1 year and not longer than 5 years	234,392	231,396
Longer than 5 years	458,110	534,208
	<b>806,796</b>	<b>897,421</b>

## 5. Payables

Liquidity facility	-	48,000
Sundry creditors and accrued expenses	5,743	3,428
	<b>5,743</b>	<b>51,428</b>

Terms and conditions - Sundry creditors and accrued expenses are normally settled on commercial 30 day terms. The liquidity facility with Bendigo and Adelaide Bank Limited is interest bearing and is repayable on 23 June 2012 or earlier if required by the Bendigo and Adelaide Bank Limited. The maximum amount available under the facility is \$30 million at balance date.

## 6. Net assets attributable to investors

Movements in net assets attributable to investors during the year were as follows:

### (a) Units on issue

	<b>2011</b> <b>\$'000</b>	<b>2010</b> <b>\$'000</b>
Opening balance	982,326	1,177,307
Contributions	470,464	391,515
Redemptions	(461,348)	(586,496)
<b>Closing balance</b>	<b>991,442</b>	<b>982,326</b>

All units in the Fund are valued at \$1.

### (b) Investors' accrued interest

Opening balance	13,195	11,046
Interest earned	56,283	50,798
Interest paid	(55,388)	(48,649)
<b>Closing balance</b>	<b>14,090</b>	<b>13,195</b>

## 7. Notes to the Statement of Cash Flow

### (a) Reconciliation of cash

For the purposes of the Statement of Cash Flows, cash includes cash on hand and "at call" deposits with other financial institutions. Cash at the end of the financial year as shown in the Statement of Cash Flows is reconciled to the related items in the Statement of Financial Position as follows:

Cash at bank	486	686
11AM call deposits	10,113	10,534
Treasury settlement account	6,310	6,091
	<b>16,909</b>	<b>17,311</b>

## 7. Notes to the Statement of Cash Flow (cont.)

### (b) Cash flows presented on a net basis

Cash flows arising from the following activities are presented on a net basis in the Statement of Cash Flows:

- (i) customer deposits in and withdrawals from the Fund;
- (ii) sales and purchases of dealing securities;
- (iii) sales and purchases of maturing certificates of deposit; and
- (iv) mortgage loans advanced and repaid.

### (c) Reconciliation of changes in net assets attributable to investors to net cash provided by / (used in) operating activities

	<b>2011 \$'000</b>	<b>2010 \$'000</b>
<b>Changes in net assets attributable to investors</b>	<b>(2,636)</b>	<b>862</b>
Hedge accounting adjustments under AIFRS	2,636	(862)
(Increase) / decrease in receivables	2,147	(2,746)
Increase / (decrease) in investors' accrued interest	895	2,149
Increase / (decrease) in sundry creditors and accrued expenses	(52)	403
<b>Net cash (used in) / provided by operating activities</b>	<b>2,990</b>	<b>(194)</b>

### (d) Non-cash financing and investing activities

During the financial year no non-cash financing and investing activities occurred.

## 8. Financial risk management

Risks arising from holding financial instruments are inherent in the Funds activities and are managed through a process of ongoing identification, measurement and monitoring. The Fund has exposure to credit risk, liquidity risk and market risk from its use of financial instruments.

This note presents information about the Funds exposure to each of these risks, its objectives, policies and processes for measuring and managing risk.

Financial instruments of the Fund comprise investments in financial assets for the purpose of generating a return on the investment made by investors.

The Responsible Entity is responsible for identifying and controlling the risks that arise from these financial instruments. This is done through a combination of techniques and controls, including the use of hedging and the development of strict lending criteria for mortgage loans.

### (a) Credit risk

Credit risk represents the risk that the counterparty to the financial instrument will fail to discharge an obligation and cause the Fund to incur a financial loss.

The maximum exposure to credit risk, excluding the value of any collateral or other security, at balance date to recognised financial assets is the carrying amount of those assets, net of any provisions for doubtful debts, as disclosed in the Statement of Financial Position and Notes to the Financial Statements. This does not represent the maximum risk exposure that could arise in the future as a result of changes in values, but best represents the current maximum exposure at the reporting date.

Credit risk arising from derivative financial instruments is, at any time, limited to those with positive fair values. The Fund minimises its exposure to credit risk on derivatives by only trading with credit graded financial institutions and has limits on the level of instruments that it holds with each counterparty.

## 8. Financial risk management (cont.)

The Funds exposure to credit risk is limited to Australia by geographic area. The Fund does not have any material credit risk exposure to any single debtor or group of debtors under financial instruments entered into by the Fund.

Credit risk is not considered to be significant to the Fund except in relation to investments in mortgage loans. Mortgage credit risk is managed by having in place strict lending criteria including ensuring appropriate security is in place to endeavour to cover potential mortgage defaults.

Based on historic default rates, the Responsible Entity believes that no impairment allowance is necessary in respect of mortgage loans. While a small number of mortgage loans have payments in arrears as at the date of this report, it is not expected that these will result in any material non-recovery.

### (b) Liquidity risk

Liquidity risk is the risk that the Fund will not be able to meet its financial obligations as they fall due.

Mortgage loans are relatively illiquid compared to some other assets classes and delays may occur in converting these investments into cash. This may affect distributions and/or redemptions to investors. The Responsible Entity minimises liquidity risk by holding a percentage of the total assets of the Fund in liquid investments, such as cash and readily negotiated assets including bank accepted bills and negotiable certificates of deposit. In addition, the Fund has standby liquidity facilities in place to draw upon to meet redemption requests, for the short term, should the need arise.

### (i) Maturity analysis for financial liabilities

Financial liabilities of the Fund comprise sundry creditors and accrued expenses, a liquidity facility provided by the Bendigo and Adelaide Bank Limited and net assets attributable to investors.

All sundry creditors and accrued expenses have no contractual maturities but are normally settled on commercial 30 day terms.

The liquidity facility with Bendigo and Adelaide Bank Limited is available for short term funding needs. The maximum amount available under the facility is \$30 million as at the date of this report, however the facility has not been utilised at balance date. The facility is repayable on 23 June 2012 or earlier if required by the Bendigo and Adelaide Bank Limited.

Initial and subsequent investor funds are fixed for a minimum of 90 days then have same day access. As such, the large majority of net assets attributable to investors are payable on demand.

There is a risk that withdrawal proceeds will not be paid within a reasonable period after the initial investment term. The Responsible Entity shall satisfy withdrawal requests as soon as practicable (generally within 48 hours, but not more than 12 months). However, withdrawal requests may be delayed or refused if in the Responsible Entity's reasonable opinion it is in the best interests of investors as a whole to do so. Investors will only have limited rights to withdraw if the Fund does not satisfy the liquidity test in the Corporations Act 2001.

#### (c) Market risk

Market risk is the risk that market prices, such as interest rates and property prices, will affect the Funds income or its holdings of financial instruments. Market risk relates to the performance of the market as a whole impacting on the Funds investment returns. Factors that can influence the market include economic, technological, political, taxation and legal conditions and even market sentiment. Changes in such conditions can affect the ability of a borrower to repay a loan, the value of property held as security or the value of fixed interest securities, which in turn may impact the value and return of the Fund.

The objective of market risk management is to manage and control market risk exposures within acceptable parameters. The Responsible Entity attempts to minimise market risk by ensuring the investment portfolio is well diversified and managed within designated parameters.

## 8. Financial risk management (cont.)

### (i) Interest rate risk

Interest rate risk arises from the possibility that changes in interest rates will affect future cash flows, the Funds income or the fair values of financial instruments. The Responsible Entity attempts to minimise interest rate risk by using hedging.

The value of interest rate swaps at balance date was as follows:

	2011 \$'000	2010 \$'000
Maturing within 1 year (net)	135,060	156,510
Maturing 1 to 5 years (net)	(135,060)	(156,510)

At the reporting date the interest rate profile of the Funds *interest bearing* financial instruments was:

#### Fixed rate instruments

Financial assets	538,307	450,978
Financial liabilities	-	-
<b>Net fixed rate instruments</b>	<b>538,307</b>	<b>450,978</b>

#### Variable rate instruments

Financial assets	463,417	586,640
Financial liabilities	(991,442)	(1,030,326)
<b>Net variable rate instruments</b>	<b>(528,025)</b>	<b>(443,686)</b>

### (ii) Interest rate sensitivity analysis - Held to Maturity investments

A reasonably possible change (assumed to be 100 basis points) in interest rates at the reporting date would have increased/(decreased) equity and profit or loss by the amounts shown below. This analysis assumes that all other variables remain constant. The analysis is performed on the same basis for 2010.

	<b>Profit or loss \$'000</b>	<b>Equity \$'000</b>
<b>30 September 2011</b>		
100 basis points increase	(200)	(200)
100 basis points decrease	200	200
<b>30 September 2010</b>		
100 basis points increase	(126)	(126)
100 basis points decrease	126	126

**(iii) Interest rate sensitivity analysis - Loans and Advances**

A reasonably possible change (assumed to be 100 basis points) in interest rates at the reporting date would have increased/(decreased) equity and profit or loss by the amounts shown below. This analysis takes into account the periodic repricing of the loan terms based on the yield curve as at 30 September 2011, and assumes that all other variables remain constant. The analysis is performed on the same basis for 2010.

	<b>Profit or loss \$'000</b>	<b>Equity \$'000</b>
<b>30 September 2011</b>		
100 basis points increase	4,265	4,265
100 basis points decrease	(5,417)	(5,417)
<b>30 September 2010</b>		
100 basis points increase	5,865	5,865
100 basis points decrease	(5,865)	(5,865)

## 8. Financial risk management (cont.)

### (d) Net fair values

All financial assets and liabilities have been recognised at balance date at their net fair values and approximate total carrying amounts as per the Statement of Financial Position.

The Fund has used derivative financial instruments to hedge against adverse movements in interest rates. The value of these derivative financial instruments is not recognised in the accounts of the Fund and realised or unrealised gains or losses are recognised as described in Note 1(d).

## 9. Segment information

The Fund invests in a range of Australian first registered mortgages as well as Australian domiciled Bank accepted bills, Negotiable certificates of deposit, Term deposits, Residential mortgage backed securities and cash.

## 10. The Fund

The Fund is constituted by deed (the Constitution) dated 12 October 1992, as amended.

## 11. Contingent assets and liabilities

No material contingent assets or liabilities existed at, or have arisen since, balance date.

## 12. Significant events after balance date

No other significant events have occurred since balance date which would impact on the financial position of the Fund as disclosed in the Statement of Financial Position as at 30 September 2011 and the results of the Statement of Comprehensive Income and Statement of Cash Flows of the Fund for the year ended on that date.

## 13. Director and executive disclosures

(a) Details of specified directors and specified executives

### **(i) Details of specified directors of the Responsible Entity**

The directors of the Responsible Entity during the financial year were:

Jennifer L Dawson (Chairman)

Ian G Mansbridge

Marnie A Baker

John A Billington

### **(ii) Specified executives**

Neither the Fund or Responsible Entity employ persons deemed to be specified executives of the Fund.

(b) Remuneration of specified directors

#### **(i) Remuneration policy**

Remuneration of directors is paid directly by the parent entity, Bendigo and Adelaide Bank Limited. The Directors do not receive any remuneration directly from the Fund. The above named Directors form the key management personnel of the Fund.

Bendigo and Adelaide Bank Limited is responsible for determining and reviewing compensation arrangements for the directors of the Responsible Entity. The remuneration of each director is assessed annually by reference to relevant employment market conditions with the overall objective of emoluments of the directors ensuring maximum stakeholder benefit from the retention of a high quality board.

## 14. Related party disclosures

- (i) The Responsible Entity of the Sandhurst Select Mortgage Fund is Sandhurst Trustees Limited, a wholly owned subsidiary of Bendigo and Adelaide Bank Limited (ABN 11 068 049 178).
- (ii) Directors, officers and employees of the Responsible Entity and related body corporate may from time to time have investments or loans in the Fund. Any transactions are conducted under normal commercial terms and conditions.
- (iii) Independent compliance committee: Compliance committee members of Sandhurst Trustees Limited may from time to time have investments in the Fund. Any transactions are conducted under normal commercial terms and conditions.
- (iv) The Responsible Entity does not have any direct interest in the assets held by the Fund, other than of a management and investment nature.
- (v) As at 30 September 2011, the Responsible Entity held investments in the Fund of \$876,262 (2010: \$13,419,627).
- (vi) Trustee management/administration fees paid/payable to the Responsible Entity in accordance with the Funds Constitution for the year ended 30 September 2011 amount to \$10,237,076 (2010: \$10,931,777).
- (vii) Accounting fees paid/payable to Bendigo and Adelaide Bank Limited for the year ended 30 September 2011 amount to \$2,112 (2010: \$2,112).
- (viii) As part its asset acquisition strategy, the Fund may purchase via equitable assignment mortgage loans from time to time from Bendigo and Adelaide Bank Limited. Management fees paid/payable to Bendigo and Adelaide Bank Limited for loan management services for the year ended 30 September 2011 amount to \$3,919,640 (2010: \$5,550,721).

- (ix) Loan origination fees paid/payable to Bendigo and Adelaide Bank Limited for the year ended 30 September 2011 amount to \$Nil (2010: \$Nil). For accounting purposes, these origination fees are capitalised and amortised over a 3 year period.
- (x) Loan origination management fees and commissions paid/payable to National Mortgage Market Corporation Limited (ABN 52 006 325 640), a wholly owned subsidiary of Bendigo and Adelaide Bank Limited, for the year ended 30 September 2011 amount to \$3,068,031 (2010: \$2,509,493).
- (xi) As at 30 September 2011, the amount owing to Sandhurst Trustees Limited by the Fund was \$Nil (2010: \$Nil).
- (xii) As at 30 September 2011, the Fund owed \$Nil (2010: \$48 million) to Bendigo and Adelaide Bank Limited under the terms of a liquidity facility. The maximum amount available under the facility was \$30 million at balance date and at the date of this report. This facility is provided on commercial terms and conditions.
- (xiii) As at 30 September 2011, the Fund had \$61,805,882 (2010: \$75,830,607) on deposit with the Bendigo and Adelaide Bank on normal commercial terms and conditions.

## 15. Auditors' remuneration

Amounts received, or due and receivable by the auditors for:

	<b>2011</b> \$	<b>2010</b> \$
Audit and review services	11,400	11,000

# Directors' declaration

The directors of the Responsible Entity declare that:

1. The financial statements and notes of the Fund,
  - (a) comply with Accounting Standards, the Fund's Constitution and the Corporations Act 2001; and
  - (b) give a true and fair view of the financial position of the Fund as at 30 September 2011 and of its performance as represented by the results of its operations and cash flows for the year ended on that date;
2. In the directors' opinion there are reasonable grounds to believe that the Fund will be able to pay its debts as and when they become due and payable.

This declaration is made in accordance with a resolution of the board of directors of the Responsible Entity.



Jennifer L Dawson  
Director  
Bendigo

24 November 2011

# Independent audit report

## To the Members of Sandhurst Select Mortgage Fund

### Scope

The financial report comprises the statement of financial position, statement of comprehensive income, statement of changes in net assets attributable to investors, statement of cash flows, accompanying notes to the financial statements, and the directors' declaration for Sandhurst Select Mortgage Fund ("the Fund"), for the year ended 30 September 2011.

The Responsible Entity of the Fund is responsible for preparing a financial report that gives a true and fair view of the financial position and performance of the Fund, and that complies with Accounting Standards in Australia, in accordance with the Corporations Act 2001. This includes responsibility for the maintenance of adequate accounting records and internal controls that are designed to prevent and detect fraud and error, and for the accounting policies and accounting estimates inherent in the financial report.

### Audit approach

We conducted an independent audit of the financial report in order to express an opinion on it to the members of the Fund. Our audit has been conducted in accordance with Australian Auditing Standards in order to provide reasonable assurance as to whether the financial report is free of material misstatement. The nature of an audit is influenced by factors such as the use of professional judgement, selective testing, the inherent limitations of internal control, and the availability of persuasive rather than conclusive evidence. Therefore, an audit cannot guarantee that all material misstatements have been detected.

We performed procedures to assess whether in all material respects the financial report presents fairly in accordance with the Corporations Act 2001, including compliance with Accounting Standards in Australia, and other mandatory financial reporting requirements in Australia, a view which is consistent with our understanding of the Fund's financial position, and of its performance as represented by the results of its operations and cash flows.

We formed our audit opinion on the basis of these procedures, which included:

- examining, on a test basis, information to provide evidence supporting the amounts and disclosures in the financial report; and
- assessing the appropriateness of the accounting policies and disclosures used and the reasonableness of significant account estimates made by the Responsible Entity.

While we considered the effectiveness of management's internal controls over financial reporting when determining the nature and extent of our procedures, our audit was not designed to provide assurance on internal controls.

We performed procedures to assess whether the substance of business transactions was accurately reflected in the financial report. These and our other procedures did not include consideration or judgement of the appropriateness or reasonableness of the business plans or strategies adopted by the Responsible Entity of the Fund.

## Independence

We are independent of the Responsible Entity, and have met the independence requirements of the Australian Professional Ethical Pronouncements and the Corporations Act 2001.

## Audit Opinion

In our opinion, the financial report of Sandhurst Select Mortgage Fund is in accordance with:

- (a) the Corporations Act 2001, including;
  - (i) giving a true and fair view of the Sandhurst Select Mortgage Fund's financial position as at 30 September 2011, and of its performance for the year ended on that date; and
  - (ii) complying with Accounting Standards and the Corporations Regulations;
- (b) the provisions of the Constitution dated 12 October 1992, as amended; and
- (c) other mandatory professional reporting requirements.

**Richmond Sinnott & Delahunty**  
**Chartered Accountants**



W J Sinnott  
Partner  
Bendigo  
24 November 2011

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Adelaide Bank**

The responsible entity and issuer of Sandhurst Select Mortgage Fund is Sandhurst Trustees Limited ABN 16 004 030 737 AFSL 237906 a subsidiary of Bendigo and Adelaide Bank Limited ABN 11 068 049 178 AFSL 237879 (S38317) (11/11)

 **Bendigo Wealth**  
managed funds