Australian Annuity Funding Trust 2024-1

Transaction Summary

Executive Summary

Australian Annuity Funding Pty Ltd (AAF) was established by Surinder Agnihotri after the sale of his previous business Australian Business Credit (ABC). The key personnel behind AAF have more than 75 years of combined experience in the sector and have stated they have written more than $1.0bn in loans. AAF specialises in trail book lending to mortgage brokers, financial planners, and property management businesses. The lending is against ongoing commission income from mortgages, insurance policies or rent rolls.

The attractiveness of this type of lending is that commission trail book funding benefits from being tied to collateral of well-known contracted cashflows. The cashflows can be readily modelled to ascertain future income and potential risks. AAF states that the loss history over the last six years of similar loans written at ABC was less than 0.25%, and arrears over the same period tracked at less than 2.28% of total cashflow.

In December 2023 AAF established the $11.0m Australian Annuity Funding Trust 2023-1 to finance such trail book lending. AAF advise that this vehicle has experienced zero arrears and losses.

To fund further growth of the loan portfolios AAF is seeking to establish another bankruptcy remote special purpose vehicle (SPV), the Australian Annuity Funding Trust 2024-1 (Trust) to provide diversified longer-term funding options for the business. The Trust will provide a bankruptcy remote structure into which AAF will then originate new loans and provide oversight and risk assessment.

The Trust consist of Class A, Class B, and C Notes. Class A and B Notes are available to investors while Class C Notes will be held by AAF as a 'first loss' equity tranche (Figure 1). The Issuer will have the option to redeem all or some of the Notes at $102.0 after 6 months, $101.0 after 12 months and at $100.0 after 2 years. The proposed issue yield is detailed below.

Figure 1: Australian Annuity Funding Trust 2024-1

Class	Subordination	Coupon	Maturity
Class A	30.0%	[9.5%]	3 Years
Class B	10.0%	[11.5%]	3 Years
Class C	Equity first loss	N/A	N/A

Source: Source: AAF

The Class A Notes rank before the Class B Notes which rank before the Class C Notes. The A Notes have 30.0% subordination, the B Class Notes have 10.0% subordination. If Class C Notes, to be held by AAF, incur any losses it has provided an undertaking to subscribe for further Class C Notes to ensure the 10.0% subordination test is met. The subordination tests must be met for AAF to be able to continue to sell loans to the Trust. Furthermore, the AAF has informed us a component of the Excess Spread defined below is intended to be retained in the Trust to provide further collateral, though this excess collateral will have slightly different eligibility criteria or be used to call and replace the Class B Notes with the issuance of further Class C Notes.

Please refer Appendix 1 for expanded key terms of the notes.

The underlying loans are secured by a first ranking General Security Agreement (GSA), a specific Personal Property Securities Register (PPSR) charge over the receivables book, a tripartite agreement with the relevant payer of the commissions, director guarantees from companies being paid the commissions and receiving the loans and the right to lodge a caveat over any real property owned by the directors in the event of a default.

Key risks of the transaction include:

- Exposure to Australian small business loan market and, in particular, SMEs working in mortgage brokering, financial planning, and property management services.
- Reliance on AAF as originator and servicer of the individual loans. A Noteholder's recourse against the Issuer is limited to the amount by which the Issuer is indemnified from the Trust assets. High level of exposure to the largest Obligors which comprise 25.0% of the Trust, however this should decrease as the Trust grows.

The major risk mitigants are as follows:

- Tripartite agreements over the assets of the borrower acknowledging security and cash flow in any event of default.
- The underlying cash flow exposure is to mortgages that the broker has originated, rent that is paid and managed by real estate agents and commissions due to planners for life insurance policies.
- A low loss history and the credibility of AAF principals as credit underwriters and servicers.
- The underlying security provides individual loan recovery in the event of default of a borrower. The maximum loan to a borrower is the lower of $2.5m (until the Trust reaches $10.0m, then 25.0% of the Trust thereafter) or 1.5 times the size of the Obligor's commission book in any one year.
- Excess income is intended to be retained in the Trust, though the limit of 1.5 times the size of the Obligor's commission book in any one year can be increased to 2 times and this loan can be subordinated to any other loan from AAF to the Obligor.
- AAF believes the underlying security is readily saleable at a minimum of 2.0 times the annual ongoing revenue received.
- The structural integrity of the deal: fully segregated portfolio; all assets/securities assigned to the trust to hold directly; subordination and replenishing clauses providing an extra layer of protection; ability to capture excess spread in the event of losses building; and the existence of standby servicer arrangements.

The transaction appears attractive on a risk/reward basis. The underlying loans are being written by experienced market participants, supported by solid security, in a segregated trust and with a solid first loss piece.

Security Structure and Investor Protections

Subordination: Noteholders have the benefit of a security interest over all the Trust assets under the General Security Deed and the Master Security Trust Deed. The A Notes will have 30.0% subordination while the B Notes have a minimum of 10.0% subordination. The Class C Notes will be retained by AAF as a 'first loss' equity tranche. In addition, AAF will be required to subscribe for Class C Notes as required to maintain the 10.0% credit enhancement to the Class B Noteholders, to continue selling loans to the Trust.

Stop Funding, Amortisation Events and Events of Default:

- If the arrears in the Trust (90 days or more) are greater than 5.0% this will trigger a Stop Funding Event which, if not remedied within 90 days will become an Event of Default.
- If the 1.0% Threshold Requirement (referred to in "Excess Spread" below) is not maintained this will trigger a Stop Funding Event which, if not remedied will become an Event of Default.
- If there are losses in the loans that impact the 10.0% credit enhancement of the Class B Notes and AAF does not subscribe for further Class C Notes to meet the required subordination test, then this will be an Amortisation Event and AAF will not be able to continue to sell loans to the Trust.

In such circumstances, Noteholders are then repaid from the proceeds of the loans as they mature naturally. In such a run-off event, excess spread is trapped in the Trust and used to accelerate the repayment of principal and outstanding interest to Class A Notes first, then Class B Notes, followed by Class C Notes subject to the waterfall priorities.

Excess Spread: The underlying loans in the SPV portfolio are intended to earn rates of return in excess of what is needed to pay the coupons owed to Class A and B Noteholders. There is a Threshold Requirement meaning that at all times the asset yield must be sufficient to pay for all required payments (Class A and B Note interest plus expenses) and maintain a buffer of 1.0%. If this is less than 1.0% this will lead to a Stop Funding Event which, if not remedied within 90 days will become an Event of Default. Any excess spread above this 1.0% can be maintained in the Trust and be used to write further loans or go to either Class C Noteholders or to AAF, the Trust unitholder. If there are losses, the excess spread is applied to reinstating the stated amount of the notes in respect of those losses. If the excess spread does not cover all losses, there will be a write-down of the Class C Note first, followed by Class B Notes, then Class A Notes (if required).

Standby Servicer: As a segregated trust structure, investors are only exposed to the loans in that trust. AMAL Asset Management is a standby servicer to the loans where AAF as servicer resigns or its appointment is terminated under the transaction documents.

Eligibility Criteria and Underlying Loans: Each underlying loan, excluding loans made from the Excess Spread, must meet various criteria including (please refer to Appendix 2 for full information):

a) Average Credit scores of greater than 500 for the company and directors.
b) The average expected life of the commission trail book is greater than 5 years.
c) The borrower has been subject to income verification.
d) The loan is not more $2.5m when the portfolio is less than $10.0m or 25.0% when above.
e) The expected sales price of the commission book is a minimum 2.0 times the value of the commission book in any one year.
f) Maximum debt service ratio of 60.0% of confirmed ongoing income.
g) Must have a tripartite agreement in place with the ultimate payer of the income stream.
h) Each loan's related security must have first ranking ALLPAAP registered on the PPSR (as applicable), and Director’s guarantees.
i) The term of the Receivable does not exceed three years.

Loans made from the Excess Spread pool can breach the above criteria, with maximum 2.0 times the value of the commission book in any one year.

Proposed Initial Portfolio

Figure 2 summarises the proposed initial portfolio to be acquired by the Trust. The proposed initial portfolio is comprised of 5 loans totalling $8.5m.

Figure 3: Largest Borrower Exposures

Customer (Names Withheld)	Type	Size	% of Trust
Client 1	Mortgage trail book	**$2.5m**	29.4%
Client 2	Trail and Planning	**$2.5m**	29.4%
Client 3	Mortgage trail book	**$2.5m**	29.4%
Client 4	Loan trail book	**$0.5m**	5.9%
Client 5	Mortgage trail book	**$0.5m**	5.9%
TOTAL		**$8.5m**	

Source: AAF

Sponsor and Servicer

AAF is a business financier whose key personnel have more than 75 years of combined experience in the sector and state they have written more than $1.0bn in loans. AAF state that the previous businesses associated with the principals of the business have returned 100.0% of capital without an impairment. Please refer to Appendix 3 for more information.

Strengths and Risks

Based on the information provided by the Issuer and AAF the strengths and risks include the following. Please also refer to the Risk section of the Information Memorandum for more details.

Strengths

- **Bankruptcy Remote Special Purpose Vehicle Structure (SPV):** The proceeds of the Notes and all Receivables are held in a Trust, managed by AMAL Trustees Pty Ltd, for the benefit of Noteholders. This means that Note investors are protected from failure of AAF. If AAF was to face difficulty or go into liquidation, an alternative Servicer can be appointed.
- **Structural Protections:** Structural protections including minimum subordination levels, solid Eligibility Criteria and exposure parameters, and Stop Funding and Amortisation Events provisions to curtail any further funding should arrears or losses arise. Further any loss incurred on Class C Notes is required to be replenished to maintain the minimum subordination levels.
- **All underlying loans are secured:** The maximum loan to a borrower is the lower of $2.5m (until the Trust reaches $10.0m, then 25.0% of the Trust thereafter) or 1.5 times the size of the Obligor's commission book in any one year. AAF believes the underlying security is readily saleable at over 2.0 times the size of the commission book.
- **Excess Spread:** AAF expects excess spread to be greater than 6.0%. This acts as additional credit support as a means of covering losses. Furthermore, the Threshold Rate requirement means that there must always be at least 1.0% excess spread over and above the required payments, otherwise there is a Stop Funding Event.
- **Experienced Financier:** The AAF team are experienced SME lenders with history running credit businesses and originating financing arrangements.
- **Attractive Risk/Return:** High yielding for a medium term against secured assets and robust structural protections.

Risks

- **Credit Risk:** Noteholders are exposed to the credit risk of the underlying portfolio held by the Trust. Failure of a borrower and any resultant bad debt has the potential to cause losses on the Notes issued. Further, the pool's composition can change over time and could represent higher risk exposures. However, such risk is offset by the structural protections and Eligibility Criteria.
- **Servicing Risk**: While the documentation provides strong protections in relation to reporting requirements there is a risk of potential loan fraud, documentation risk, and in general what is referred to as servicing of the loan risk by the servicer, AAF, that could impact on the recoverability of the individual loans.
- **Exposure to AAF**: AAF conducts the origination and servicing of the loans. If the operating companies were to go into liquidation, the ability to originate new loans and service existing loans would be

impacted. However, AMAL as the Trustee has the power to appoint a replacement Servicer (which can be AMAL Asset Management Ltd as standby servicer). The existing loan assets will remain in the secured SPV for the benefit of the Noteholders.

- **Potential Conflicts of Interest**: AAF has advised that there may be instances where it may want to invest in some of the businesses it funds. However, as per the Information Memorandum, it has stated that under such circumstances, it would be at arm's length with an independent review of all legal documents, that all entities are independently audited, that there is at least one independent director, and the trustee will be notified and given such audit reports.
- **Replenishment Risk:** AAF is required to replenish any losses incurred on the loans to a level that provides 10.0% subordination to the Class C Notes (ie. by subscribing for further Class C Notes to ensure the required subordination test is met). There is risk that this obligation will not be met. However, if it fails to replenish the required amount within the required time frame, an Amortisation Event occurs, providing a strong incentive to do so. In addition, if the Portfolio does go into run off, the excess spread from the existing loans at the time provides further subordination.
- **Liquidity Risk:** As a small size issue, liquidity is likely to be limited, although FIS will endeavour to make a market in the Notes.

Conclusion

The transaction appears attractive on a risk/reward basis. The underlying loans are being written by experienced market participants, supported by solid security, in a segregated trust and with a solid first loss piece.

Appendix 1: Key Terms of the Notes

Key terms and structural features of the Note issue as provided by the Issuer are summarised below. Please refer to the Issue documentation including the Issue Supplement and IM for full details.

Item	Description
Issuer	AMAL Trustees Pty Ltd as trustee of the Australian Annuity Funding Trust 2024-1
Security Trustee	AMAL Security Services Pty Limited
Trust Manger	AMAL Management Services Pty Ltd
Servicer and Seller	Australian Annuity Funding Pty Ltd
Standby Servicer	AMAL Asset Management Limited
Type of the Notes	Multi-class, asset backed, secured, limited recourse, fixed rate debt securities and are issued with the benefit of, and subject to, the Master Trust Deed, the Master Security Trust Deed, the General Security Deed, the Issue Supplement, the Note Deed Poll and the other Transaction Documents in respect of the Trust.
Classes	Class A Notes, Class B Notes and Class C Notes.
Replenishment	The Seller will ensure that it or a Related Entity subscribes for sufficient Class C Notes to ensure that at all times the aggregate Stated Amount of the Class C Notes will not be less than 10.0% of the aggregate Stated Amount of all of the Class A Notes, Class B Notes and Class C Notes.
Maturity Date	3 years
Optional Redemption	All or some of the Notes at $102.0 after 6 months, $101.0 after 12 months and at $100.0 after 2 years
Coupon	Class A Notes: [9.50%] Quarterly Class B Notes: [11.50%] Quarterly Class C Notes: Equity
Report Undertakings	• Quarterly compliance certificates and management report on SPV activities • Loan Servicer report detailing all loans owned by the Trust.
Events of Defaults	• Non-payment of any Required Payments not cured within 10 business days. • Breach of other representations / covenants / obligations not cured within 90 business days. • A Stop Funding Event not cured within 90 days. • Transaction Documents are voided. • Judgement against the Seller or the Servicer for an amount exceeding $0.5m. • General Security Deed or security interest thereunder ceases to be valid and enforceable. • Insolvency Event of the Trustee where the Trustee is not replaced within 60 days. • Enforcement against assets of the Seller or the Servicer exceeding $0.5m.

Source: AAF Information Memorandum

Appendix 2: Eligibility Criteria

Extraction from the Information Memorandum.

a) the Receivable is due from a qualifying Obligor;
b) the Receivable is repayable only in Australian dollars;
c) the term of the Receivable does not exceed three years;
d) a tripartite agreement exists in relation to the Receivable between the Obligor, the Seller and the aggregator (Type 1: Trail Book Loans), the dealer group (Type 2: Financial Planner Loans), or the property agent trustee (Type 3: Rent Roll Loans) (Tripartite Agreement);
e) if the Receivable is an interest-only loan, the interest-only term of the Receivable does not exceed two year;
f) the Outstanding Amount of the Receivable is either not more than the lower of:
   i. at any time when the aggregate Invested Amount of the Notes is:
   - less than $10.0m, $2.5m; or
   - $10.m or greater, the amount that is 25.0% of the aggregate Invested Amount of the Notes; and
   ii. 1.5 times the size of the Obligor's commission book in any one year;
g) the "average expected life" of an Obligor's commission book is greater than 5 years;
h) the expected sales price of the Obligor's commission book is a minimum of twice the value of the commission book in any one year;
i) the Receivable is secured by a general security agreement over the assets of the relevant Obligor, guarantees from the directors of each Obligor, a charge over the specific receivable pool and a Tripartite Agreement with each Obligor;
j) the Equifax Score of an Obligor and its directors in aggregate is an average of at least 500 at the time of settlement of the underlying loan contract;
k) the Obligor covenants to maintain a maximum debt service ratio in relation to the Receivable of at least 60.0% of its confirmed ongoing income;
l) the Receivable is not in arrears by more than 30 days;
m) the Obligor waives all rights of set-off under the terms of the Receivable;
n) the Receivable was originated in its ordinary course of business and in compliance with all the applicable laws, regulations and any credit acts;
o) the Receivable was originated in accordance with and it satisfies all material requirements of the Origination Guidelines and the Servicing Procedures;
p) the Receivable is freely capable of being dealt with by the Seller as contemplated by this document and the Master Sale and Origination Deed;
q) the relevant Obligor has been subject to income verification;
r) the Receivable is subject to a fixed rate of interest;
s) each Related Security in respect of the Receivable has been stamped with all applicable duty;
t) each Related Security has been registered with a first ranking AllPAAP security on the PPSR (as applicable) in accordance with the Origination Guidelines and Servicing Procedures; and
u) the Receivable is not a regulated consumer receivable.

Appendix 3: Australian Annuity Funding, Key Individuals

Surinder Agnihotri (Managing Director): Surinder has over 20 years' experience in residential and commercial finance, sales and distribution. Having worked for some of Australia's largest mortgage aggregation groups, he has been involved with over $20bn in loan settlements across a diverse range of residential mortgages, commercial property and business loans. Most recently Surinder founded and was Managing Director of Australian Business Credit. Surinder set up ABCredit to specialise in lending niches where the market opportunity is not a priority for other lenders. After divesting of ABCredit Surinder has now established Australian Annuity Funding.

Tony Katsikas (Executive Director): Tony is a management consultant and advisor with over two decades experience working in strategy, transformation and marketing with experience across the US, Europe and Asia Pacific. He has extensive knowledge and experience in strategy, analysis of business performance, technology, risk management and governance as well as being an extensive property investor. Tony provides independence, guidance, and governance contribution to the running of Australian Annuity Funding. Previously Tony has been a Senior Executive of an Australian technology business acquired by Hewlett Packard as well as the Program Manager and Director of a global consulting firm.

Hirdesh Prasad (General Manager, Head of Credit and Operations): Hirdesh has an extensive background in financial services systems and technology involving system integration, provisioning, compliance and management where he has managed client relationships, managed operations, overseen business development, undertaken IT management responsibilities and conducted general business management. Hirdesh has been involved in the finance industry for over 20 years. His experience in software development, especially in the finance industry and he has undertaken customisation and implementation of Salesforce as the software base to run origination, ledger tracking integration and servicing functions of Australian Annuity Funding.

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