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11 June 2009

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Att: Mr Sean Robertson

Our reference: 131/80090861

Dear Sirs

City Pacific First Mortgage Fund - unitholder meeting

We act for Balmain NB Corporation Limited and Trilogy Funds Management Limited. Our clients have provided us with a copy of your letter dated 5 June 2009. We are instructed to respond to the matters raised by you in your letter, adopting your headings, as set out below.

1. **Resolution**
- 1.1 You allege that the resolution included in the notice of meeting and proxy form does not comply with section 601FM(1) of the *Corporations Act 2001*.
- 1.2 We disagree with that assertion. There is no failure to comply with section 601FM.
- 1.3 If we are wrong about that, which is not admitted, then by reason of the operation of section 1322 of the Act, the meeting is not invalidated.
- 1.4 Assuming the resolution was split the 2 resulting resolutions would by their very nature need to be interdependent. That is the passing of the first resolution to remove your client would need to be dependent on the success of the second resolution to appoint Trilogy Funds Management Limited as the new responsible entity. If it were otherwise, the Fund may end up in the position of having no responsible entity appointed to it and, as a consequence, section 601NE(1)(d) would be triggered resulting in a winding up of the Fund. Clearly this was not the intent of those unit holders who questioned the meeting. Practically then the single resolution achieves no different outcome to having two interdependent resolutions.
- 1.5 It follows that, to the extent that there may be a breach of section 601FM(1), which, as noted, is not admitted, then at its highest it is of a technical nature only and both ourselves and our clients are of the view that any irregularity in the form of the resolution would be classified as a procedural irregularity which does not cause substantial injustice.
- 1.6 In the event that your client commences the proceedings threatened in paragraph 40 of your letter, our clients will vigorously oppose such proceedings, and will, if appropriate, bring proceedings by way of cross claim seeking a declaration pursuant to section 1322(4) of the Act that the meeting and the manner of calling it (including the form of notice and proxy) are not invalid.

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2. Return of Proxies

2.1 It is not the case, as you assert, that all proxy forms received by Computershare Investor Services Limited (**Computershare**) are invalid.

2.2 The decisions which you rely on in support of this proposition can and should be distinguished. In particular, they are cases where the proxies were collected by parties who could not be described as "disinterested". In *Bisan Ltd & Anor v Cellante & Ors* [2002] VSC 430, the proxy forms were to be returned to a company associated with at least one of the defendants. In *Portman Iron Ore Limited (ACN 007 871 892), in the matter of Golden West Resources Limited (ACN 102 622 051)* [2008] FCA 1362, the proxy forms were to be returned to the company which had questioned the proposed meeting of shareholders.

2.3 In this instance a reputable independent provider of, among other things, proxy collection services has been nominated. As noted by the Court in *Bisan Ltd*:

The legislation does not expressly state that the nomination of an intermediate recipient will render a notice of meeting or a proxy appointment invalid. However, in my opinion, the legislation's insistence on receipt by the company appears to contemplate a receipt by an entity managed and controlled by persons subject to onerous fiduciary duties in relation to the proxies, which will safeguard the actual and apparent integrity of the corporate voting process. The interception of proxy appointments by an intermediate party who is under no fiduciary duty or other apparent obligations in relation to their safeguarding, entails an inherent exposure to the possibility of filtering or other inappropriate handling."

2.4 *In Re Lion Selection limited (No. 2)* [2008] 66 ACSR 656 undertakings were provided to the Takeovers Panel by the intermediate recipient of the proxies that:

- (a) it would not filter or otherwise inappropriately handle any proxies; and
- (b) if any proxy was given to it prior to the proxy deadline but such that it was too late to lodge it with the company's registry, to use its best endeavours to contact the relevant shareholders and the proxy was too late and that they may vote by attending the meeting.

The Takeovers Panel considered these undertakings adequately resolved the concern raised that the recipient of the proxies may selectively lodge proxies with the company. Our clients have provided undertakings to Members to ensure proxies are properly handled via a deed poll. Such undertakings include those set out in this paragraph 2.4 above.

2.5 In the present situation, to safeguard against the issue raised by the Court in *Bisan Ltd* the agreement which Computershare has entered into for the collection of proxies provides relevantly that Computershare must, amongst other things:

- (a) properly collate and safeguard all proxy forms received by unitholders;
- (b) not tamper with the proxy forms in any way;

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- (c) not filter or otherwise inappropriately handle the proxy forms received by it from unitholders; and
 - (d) exercise due care and skill and act in good faith in all of its dealings with the proxy forms.
- 2.6 In these circumstances, there cannot be said to be in this case any risk, adopting your words, to "*the actual and apparent integrity of the corporate voting process*". Indeed, we understand that in the past, City Pacific has used the services of Computershare for this same purpose, namely the collection of proxies.
- 2.7 In any event, our clients have requested Computershare to provide an undertaking to your client in accordance with paragraph 2.5 above in relation to the collection of proxies. That is, our client has requested Computershare to undertake to your client to:
 - (a) properly collate and safeguard all proxy forms received by unitholders;
 - (b) not tamper with the proxy forms in any way;
 - (c) not filter or otherwise inappropriately handle the proxy forms received by it from unitholders; and
 - (d) exercise due care and skill and act in good faith in all of its dealings with the proxy forms.
- 2.8 Our client is also prepared to arrange for representatives of your client to have a reasonable opportunity to inspect the proxy forms received by Computershare.
- 2.9 Please advise whether your client would like our client to arrange the abovementioned undertaking and access and whether that will address any residual concerns your client might have in relation to the collection of proxy forms.

3. Contents of explanatory memorandum

- 3.1 Our clients do not believe that the contents of the explanatory memorandum are either incomplete or misleading. However, they have prepared a supplement to unit holders (which we understand will be posted on BalmainTrilogy's website) addressing the issues you raise on behalf of your client in your letter. That supplement, a copy of which is **enclosed**, will be mailed out to unit holders tomorrow.
- 3.2 As a result of the supplement we do not propose to address each of the issues you raise in relation to the contents of explanatory memorandum in your letter.

4. Summary

- 4.1 Given the matters set out above and in light of the way our client has proceeded to date in this matter, our clients disagree with your assertion that the resolution proposed at the meeting and the voting process are fatally flawed and that if the meeting were to proceed any resolution adopted would be invalid. Accordingly, our clients do not propose to take up your invitation to advise

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members of the fund that the proposed meeting has been abandoned. Our clients remain firmly of the view that the meeting can and should proceed.

- 4.2 We note that your client in its capacity as responsible entity of the fund has indicated that, in the event that our client does not agree to abandon the meeting, it will have no alternative but to apply to the Court for an injunction restraining the meeting from proceeding. Having regard to the above matters, it would be inappropriate (not to mention in breach of law) for your client to use Fund assets to fund proceedings of this nature which have no proper basis and in which your client has a direct interest.
- 4.3 We assume that once your client considers the matters set out above and the contents of the enclosed supplement, it will not take such action.
- 4.4 In the event that, notwithstanding the contents of this letter, your client does approach the Court for any orders on an ex parte basis, or otherwise, please ensure that a copy of this letter and its enclosure is put before the Court.

Yours faithfully



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10 June 2009

Meeting of Members of City Pacific First Mortgage Fund To be Held on 25 June 2009

Dear Member,

Since members called the Meeting on 20 May 2009, we can report that as at 9 June 2009 proxy votes representing over 328,000,000 units or 37.5% of the fund have been lodged. Of these proxies 97.5% have been voted in favour of the resolution to appoint Trilogy as your responsible entity. However, in order for the resolution to pass we need the holders of 50% of the total number of units to be voted in favour of the resolution.

As such, if you choose not to vote, it will effectively be a vote for City Pacific Limited ("CP") remaining as responsible entity. The success of this proposal remains reliant on Members' voting participation. If you want to **HAVE YOUR SAY** in determining the outcome of this proposal, then please, if you have not done so already, ensure you cast your vote, either in person at the meeting or by proxy prior to the meeting.

Over the last few weeks, BalmainTrilogy has been in communication with members of the Fund ("Members"), such as yourself, in respect of Trilogy's appointment as responsible entity of your Fund.

We are also aware that CP has commenced a campaign to prevent their removal as responsible entity. Given the level of fees CP charges the Fund, we anticipate CP will do what it can to hold on to the responsible entity role. As part of that campaign, it appears CP has provided certain misleading information to Members.

Having regard to that communication, and to refute CP's misrepresentations, we take this opportunity to supplement the original Notice by expanding upon and clarifying various matters concerning the future of your Fund via the attached "Questions and Answers" document.

Rest assured we remain committed to continuing to represent the members of the Fund and to meet their desire to have their investment properly and visibly managed. In particular our management of the Fund will be unfettered by the conflicts inherent in the Fund's loans to entities associated with CP which currently represent over 27% of the Fund's assets.

If you have any further questions in relation to this proposal please call us on 1800 798 896 or visit our website at www.balmaintrilogy.com.au

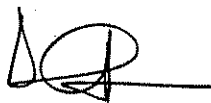
We look forward to working with you.

Yours sincerely



Rodger Bacon
Chairman
Trilogy Funds Management Limited

Level 13, 56 Pitt Street, Sydney NSW 2000



Andrew Griffin
Chief Executive
Balmain NB Corporation Limited

Level 14, 60 Castlereagh Street, Sydney NSW 2000

Questions and Answers

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1. Do Trilogy and Balmain have the required expertise to manage the Fund?

By appointing Trilogy as responsible entity and thereby BalmainTrilogy as asset manager, Members will benefit from the collective expertise and resources of the Balmain and Trilogy groups. As a combined group, BalmainTrilogy:

- Directly employs 130 people with over 400 people employed by their related corporate groups;
- Operates out of 14 offices located around Australia;
- Services mortgages to a value of \$8bn;
- Manages specific mortgage assets of \$900m;
- Holds 2 separate AFS Licences;
- Has an experienced credit team of 12 people; and
- Benefits from over 30 years of relevant experience.

Clearly Balmain and Trilogy have the combined requisite experience and expertise to properly manage all aspects of the Fund.

2. Why are Trilogy and Balmain in joint venture?

Both Trilogy and Balmain were separately approached by members of the Fund to assist in the removal of CP as responsible entity. When Trilogy and Balmain became aware that they were both considering the same thing the joint venture was brought into existence. The Balmain Trilogy joint venture brings together their respective highly complementary skill sets and represents a compelling solution for investors.

Trilogy, for its part, has capability and extensive experience in managing mortgage funds. Directors and senior executives of Trilogy played key roles (including directors of the Responsible Entity, Credit Committee membership including Chair and Compliance Committee) in the management of the Howard Mortgage Trust over a period of some seven-(7) years. During that term the funds under management in that Trust were grown from approximately \$460m to in excess of \$2.06 billion. At the time the fund was regarded as the largest non-bank mortgage trust in Australia.

Other key Trilogy executives have significant prior experience in administering mortgage funds with strong geographic experience in Queensland and sector experience with construction loans.

In addition to managing the Trilogy First Mortgage Income Trust, Trilogy acts as the responsible entity for a number of other managed investment schemes.

Balmain has been a mortgage originator for over 30 years and has been an originator to the mortgage trust industry since the sector's inception. Over the last 10 years Balmain has become a mortgage asset manager and currently acts, either directly or indirectly, for the likes of AXA, CBA and NAB.

In this capacity Balmain can demonstrate deep experience of recoveries and collections on non-performing loans and, more importantly, rectification of non-performing loans to return such loans to 'performing' status.

3. What are the total fees payable by the Fund under Trilogy?

As previously disclosed Trilogy's total management fee payable by the Fund will be 1.5% per annum of the prevailing value of assets under management. To re-assure members of any previously disclosed additional costs to be incurred by the Fund we have established 'caps' for other relevant expenses. For the sake of clarity the Fund, in addition to the management fees, will also meet the costs of:

- The independent Custodian and the independent Registry provider **BUT NOT TO EXCEED 0.12% PER ANNUM** of the prevailing value of assets under management;
- The once-off Asset Review referred to in the Notice of meeting **BUT NOT TO EXCEED \$100,000**; and,
- The once-off Legal Review referred to in the Notice of meeting **BUT NOT TO EXCEED \$100,000**.

Trilogy and **NOT THE FUND** will be liable for the payment of:

- Any fees payable to the independent Custodian and Registry providers in excess of 0.12% per annum;
- Costs of the once-off Asset Review exceeding \$100,000;
- Costs of the once-off Legal Review exceeding \$100,000;
- Costs of the Investor Committee; and
- Costs and fees charged by BalmainTrilogy as asset manager.

Currently CP are charging the Fund 2.5% per annum of the prevailing value of assets under management. They advised members at the members' meeting on 1 May 2009 that they were unable to manage the Fund for 1.5% per annum. Trilogy and BalmainTrilogy can manage the Fund and its assets for 1.5% per annum.

4. Will lower fees (compared to CP) mean fewer resources to manage the Fund?

Absolutely and categorically no. Trilogy and BalmainTrilogy have significant resources and expertise available to manage the Fund and its assets (see questions 1 & 2). The reduced fee reflects prevailing market rates. The fee currently being charged by CP is excessive.

5. What are the advantages and disadvantages of appointing Trilogy as responsible entity?

As the notice of meeting explains in detail, there are numerous advantages to appointing Trilogy as responsible entity and BalmainTrilogy as manager. Members will benefit from a well funded and experienced responsible entity which is free of conflict and able to act in the best interest of Members without fear or favour. In addition by appointing Trilogy, Members will remove management of the Fund from CP which, as responsible entity, has presided over the Fund during a period of decline.

However, we anticipate that there may be transitional issues involved in moving the management of the Fund from CP to Trilogy. Whether this creates logistical difficulties will largely depend on how co-operative CP is and the state of the Fund's books and records. In this regard we note that CP has legal obligations to effectively and efficiently transition the management of the Fund and its assets to Trilogy. As such we believe the transitional issues can be managed effectively.

In addition we note that the change of responsible entity may have consequences under the Fund's loan agreement with CBA. This is discussed further at questions 9 & 10.

6. What is the current proxy vote count?

As at 09 June 2009, proxies representing over 328,000,000 units (or 37% of all units) from over 4,800 individual members have been lodged. Of these, 97.5% are in favour of Trilogy's appointment and CP's removal as responsible entity of the Fund.

However, the resolution requires the support of members holding more than 50% of all of the units in the Fund (over \$440m units). This means that a failure to vote is effectively a vote for CP. Hence BalmainTrilogy encourages all investors to vote on the proposal and have their say on the future of the Fund.

If you require another proxy form, please call 1800 798 896.

7. When will distributions and redemptions commence and how will they be funded?

We are committed to recommencing distributions and redemptions. The timing and funding method will be determined having regard to the best interests of Members following the Asset Review, which we currently estimate will be completed within four-(4) months of Trilogy's appointment as responsible entity.

At this stage we anticipate funding distributions and redemptions from:

- Proper management of the mortgage loans including procuring the payment of outstanding interest and principal from the borrowers;
- Proceeds of sale of security properties where the Asset Review indicates that such properties will be sold at fair value and not heavily discounted (i.e. no fire sales);
- Recovery from guarantors, whether related or not to CP, where insufficient proceeds are recovered from any asset sale; and,
- The additional liquidity available to the Fund resulting from the reduction in management fees.

Members should be aware that there may be a period of time before it is in their interests to recommence distributions and redemptions. The agreement of CBA may be necessary for this to occur however we believe that a reasonable distribution and redemption plan which properly takes into account the financial position of the Fund can be negotiated with CBA.

8. What will the redemption price be?

To ensure Members are not adversely affected, we intend that the redemption price should be a price which properly reflects the value of the Fund (ie prevailing unit value). Due to Fund losses sustained during the period of CP's management, the redemption price may be less than \$1.00. If this is the case, it may be necessary to amend the Constitution to allow redemptions at less than the \$1.00 per unit level. Such an amendment may require a Members' vote.

9. What happens to the CBA Loan to the Fund if Trilogy becomes the responsible entity?

Despite Trilogy's request, to date CP has not made the CBA Loan terms available. Accordingly we do not know whether the Fund is currently or is likely to become in breach of any loan covenant or whether the removal of CP will give rise to a review event or default under the CBA Loan.

On the assumption that the appointment of Trilogy as responsible entity will constitute an event of default or give CBA a right to review the Loan, then BalmainTrilogy anticipates that CBA's reaction to the proposed change of responsible entity will be to consider whether the incoming responsible entity has the expertise and experience to perform its duties as responsible entity in a manner acceptable to CBA.

We believe that there is no reason that CBA should not form a favourable view of the new responsible entity's capacity given that:

- The assets of the Fund are not affected by the change of responsible entity;
- Trilogy, the proposed incoming responsible entity, is in a stronger financial position than CP;
- We believe that the combined expertise and experience of BalmainTrilogy is superior to that of CP;
- Trilogy will work closely with CBA in relation to the CBA Loan; and
- The considerable reduction in management fees charged by Trilogy (compared to CP) will provide additional liquidity to the Fund.

For the sake of clarity CBA has made no commitment to extending the CBA Loan following Trilogy's appointment, however, BalmainTrilogy have had preliminary discussions with CBA in general terms and have no reason to believe that CBA will not extend the loan.

10. What if CBA default the Loan to the Fund?

On the assumption that CBA are able to default the Loan as a consequence of a change of responsible entity then, subject to the terms of the Loan, CBA may require its repayment. Unless the Loan can be refinanced this may result in Fund assets being sold at sub optimal prices. Whilst we do not believe it is likely that this will occur, BalmainTrilogy has commenced preliminary discussions with potential replacement financiers. At this stage it is impossible to progress this matter substantively until we have access to the books, records and assets of the Fund. As such we can give no assurance alternative funding will be available. Our primary goal, however, is to use our best endeavours to retain the existing facility with CBA.

11. What is Balmain's previous history with CP?

Being a long term participant in the mortgage fund arena, it is not surprising that Balmain has had prior experience with CP. Balmain originated (introduced) loans to CP until about May 2006 when Balmain elected to cease originating loans to CP.

Balmain had no credit role whatsoever in relation to these loans and CP was solely responsible for the decision to acquire those loans.

For CP now to suggest that this makes Balmain somehow responsible for the performance of those loans is misleading.

If CP is looking to make someone responsible for the performance of the Fund, we suggest that it look at its own loan credit and management practices, including that under CP's management the Fund lent certain borrowers money to finance significant fees CP (and not the Fund) received for settling the loans.

12. Could the Fund be forced to borrow more money?

We are opposed to any increase in the Fund's current borrowings. In the unlikely event that this becomes necessary to enhance the existing assets we will put such a proposal to members for their approval and the members' decision will be final.

13. Is the Notice of Meeting valid?

Members may be aware that CP (via their lawyers) has threatened "[if the meeting is not abandoned] ... to apply to the court for an injunction restraining the meeting from proceeding." We will contest any such court action to ensure that the meeting proceeds. We believe that this is a clear attempt by CP to continue to ignore the right of the Funds members to have a voice.

Prior to the Notice of Meeting being issued we received detailed legal advice on the conduct and calling of the meeting and we remain of the opinion that the Notice of Meeting is valid.

CP's claims that certain elements of the process of the meeting are "defective", "fatally flawed" and "invalid" are incorrect.

We will continue to use our best endeavours to ensure that the meeting proceeds as scheduled on 25 June 2009.

14. How will the Investor Committee operate, who will be on it?

The Investor Committee will represent members of the Fund. Its composition will be established by an independent auditor who will seek applications from all of the members of the Fund. They will be selected not on "size" or allegiance but their respective ability to both understand matters relating to the Fund and properly communicate (at the responsible entity's expense) to all members of the Fund.

The Investor Committee's final composition will include not less than three members not related to Trilogy or BalmainTrilogy, an independent chair and one representative each from both Balmain and Trilogy. The Investor Committee will meet at the expense of the responsible entity and **NOT AT THE EXPENSE OF THE FUND.**