

1 March 2013

Dear Stephen,

Following our recent discussion, we are pleased to provide further information to assist your understanding of LM, the LM First Mortgage Income Fund, the LM Managed Performance Fund and Maddison Estate.

LM Investment Management Ltd (LM)

LM operates globally, as an Australian fund manager with a 15 year track record in managing Australian assets with a gross realizable value of \$3bn. We manage 9 investment funds which receive investments from investors in more than 75 countries.

We have internationally registered and regulated funds in many of the worlds' most well respected and regulated jurisdictions including Australia, Luxembourg, UK, Canada, Singapore and Ireland (under UCITS IV Compliance) in partnership with highly regarded institutions such as Societe Generale, Deutsche Bank, Price Waterhouse Coopers, SMT Fund Services and Host Capital.

LM does not invite nor take investment directly from the public. Investment in our funds is received via financial institutions or financial advisors. This means that the investor has sought professional advice in relation to investing generally; understanding the nature of their selected investment fund; and makes the investment as part of a properly considered, balanced portfolio designed to meet their needs.

To ensure a proper and thorough understanding of the funds, LM hosts participative due diligence forums for advisors and institutions. These forums cover all aspects of the funds including assets, fund mandates, the asset evaluation and due diligence process. The Australian property market, economy and managed funds sectors are also included, as is LM generally. The forum is hosted by directors, senior executives, senior lending and asset management personnel, and the portfolio manager. In addition, those attending interact fully with all LM staff in the host office.

Advisors are encouraged to raise all queries throughout the day's presentation to enable them to decide whether the funds and LM are suitable to recommend to their client base.

Attached are the 2012 financials for the Responsible Entity, LM Investment Management Ltd as requested.

The LM First Mortgage Income Fund (FMIF)

The GFC impacted fund managers and funds worldwide, with most reporting fund losses as a result of market factors delivering volatility across all investment sectors. It is not unusual to see fluctuations in unit price. In our history, this Fund is the only one to experience negative volatility on its unit price. The LM FMIF extended loans on a first mortgage basis, on a conservative average loan to security value of 65%, across the Australian property market. For over 10 years it delivered its benchmark distributions to investors with no disruption to unit price. We closed the fund to protect value for investors during the GFC.

Throughout closure of the fund, all exit strategies for the assets have been considered with many assets having been sold. Initial feedback from investors and financial advisors was to protect investor capital by avoiding a fire sale at all costs. Assets were held and managed where it was deemed appropriate. Those assets sold have been sold in the proper manner required under the Corporations Act, a process including obtaining independent valuation.

Required provisions have been raised in the fund in the appropriate time and manner.

The regular return of investment capital to investors has commenced and will continue through this year on a quarterly basis as a result of the momentum in the sales process. This is not a fire sale campaign.

As discussed, it is important that the value our funds holds on behalf of investors, be protected from any potential market prejudice created that could disrupt the current asset sales and capital return to investors

Attached are the audited financials of the FMIF for the last 3 years, as requested.

In relation to the matters noted in the audit report for the LM First Mortgage Income Fund for 30 June 2012;

- The Deutsche Bank facility has been successfully renegotiated, to 30 June 2014 with a further option for LM to extend to 30 June 2015. The new facility has a cap of \$25 million with no requirement for amortisation. Therefore this has removed the risk around the expiring facility noted in the 30 June 2012 financial statements which lead to the uncertainty on whether the Scheme has the ability to complete projects and realise assets or continue as a going concern.
- LM has received legal advice on reinvestment of distributions of the feeder funds to establish that the declaration of these distributions is fair and reasonable to all investors.

LM Managed Performance Fund (MPF)

1. The MPF extends a range of debt securities across the Australian property market. In some instances it participates in equity style positions in property. Its current asset focus is on delivery of residential development, where there is a well reported undersupply and high demand for the end product.
2. The MPF is not distributed to Australian retail Mum and Dad investors. It is for the wholesale/sophisticated market, where those investing demonstrate "wholesale" experience and/or demonstrate certain financial hurdles. In Australia, this includes different categories eg. they are a financial institution, they make a minimum investment of \$500,000, they demonstrate an annual income of \$250,000 per annum for 2 years.
3. LM, in managing the investment professionally and transparently, elects to have the fund fully audited on an annual basis by Australia's largest independent firm, Williams Partners (WPAIS). We note there is no requirement for the MPF to be audited.

It is an exhaustive process conducted within Australian and International Accounting Standards. The carrying value of the assets of the fund is substantiated by the audit with evidence of corroborating market evidence being integral.

As discussed we attach further information on the audit process for you.

4. You requested further explanation around the structure of the fund.

In our meeting we discussed the fact that in the MPF, some assets are held by an LM related company. That structure is implemented to protect the tax position of the fund and its investors, to meet the requirements of the fund and investors to receive benefits as income and not profit. It is fully audited to ensure compliance with all legal, regulatory and international accounting standard requirements. The MPF has the beneficial interest. The LM related company derives no beneficial interest from the arrangement.

To ensure that the full asset benefits pass to the MPF, and not to LM, with the investors receiving income, a loan agreement is struck between the Special Purpose Vehicle (SPV) entity (the related party entity) for the transaction and the fund. The interest rate set in that loan agreement is (i) at a rate that is commercial and (ii) importantly, the terms of the loan agreement ensure that no profit is retained in the SPV, ie MPF derives the full benefit, not the SPV. The SPV is a related entity of LM simply because it must be controlled by LM, however, under the mechanism full benefit is passed to MPF, not LM.

The financial benefit LM and Peter Drake derive from the MPF is only its management fee.

5. There appears to be some confusion regarding your understanding of how we promote the MPF. LM does not represent itself as being regulated as a bank and nor is the fund represented as a bank. LM is regulated under the Corporations Act and the advisors attending our due diligence days are briefed fully in this regard as they are in the nature of the funds' investment mandates and assets.

In the history of the fund, we have had one occasion only, where material we circulated to a small group of some 40 financial advisors only, contained a reference to "bank like". That was in the context of an offer being made to class holders with minimum investments of \$500,000 as an alternative to the fund taking a "bank like facility". It was not referred to as an "investment". Further, the offer was not available within Australia. The confusion regarding context was identified almost immediately and it was removed from circulation with an amended document forwarded to those who received the first, to eliminate any possibility that reference may be taken out of the context originally intended.

Maddison Estate

You sought confirmation on certain aspects of Maddison Estate, which we are pleased to provide.

1. The Maddison Estate has been stamped as a project of "State Significance" by the Queensland State Government and Gold Coast City Council. Attached is evidence of both local and State support for the estate.
2. We confirm an exclusive Memorandum of Understanding is in place with the company of 11-time ASP Surfing World Champion Kelly Slater – the Kelly Slater Wave Company – to deliver the world's first continuous wave pool, within the Maddison Estate surf precinct. Full engineering and feasibilities have been undertaken, with favourable results. It is real and further announcements will be forthcoming.

The concept has the strong support of key stakeholders, government representatives and the surfing industry – not only for the proposed wave system, but all of the other inclusions that will make this a total surf experience unlike anywhere in the world. This includes residential apartments, restaurants, 2 hotels and an Eco Resort. AECOM has undertaken a domestic and international tourism and feasibility study, whilst Cox Rayner is the lead architect for the precinct. The AECOM findings confirm the Maddison Estate surf precinct will benefit local and domestic tourism. Signed agreement with the Kelly Slater Wave Company and LM is imminent.

3. Internationally acclaimed landscape designer, Jamie Durie and the Durie Design team are conceptualising, designing and delivering landscape architectural design throughout the entire development. This includes streetscapes and 30 hectares of parkland throughout the development. The first stage of design has been delivered at the Maddison Estate Sales Centre.
4. A Natalie Cook commercially operated beach volleyball centre and training academy will be managed by beach volleyball champion Natalie Cook, Australia's only five time Olympian, winning Gold in 2000 (Sydney), and Bronze in 1996 (Atlanta).
5. A Sam Riley commercially operated swim school and academy, will be managed by breaststroke champion Sam Riley, a 3-time Olympic Medallist (1 x Silver, 2 x Bronze), 2-time World Championship Gold Medallist, 5-time Commonwealth Games Gold Medallist and 9-time Pan Pacific Games Medallist.
6. Major builder partner agreements with four of Australia's leading homebuilders – Plantation Homes, Metricon, Ausbuild and Clarendon Homes – to deliver a selection of designs across a range of price points. These premium homebuilder partners will also actively market Maddison Estate house and land packages through their established buyer networks, enhancing initiatives already in place with principal global marketing agent, Knight Frank.
7. Maddison Estate has drawn significant market interest. In addition to the above we are currently negotiating with the Indian Premier Cricket League who in conjunction with the Council is working on a proposal with us for the location of an IPL Cricket Stadium.

8. You were interested in establishing ball park sales for Maddison Estate. Attached is an example of the information which has been utilised in the audit as corroborating market evidence that the Stage 1 sales projections are formulated reasonably, based on sales of other product in the region.

The marketing campaign for the estate kicks off towards the end of March, when Stage 1 sales will also be released to market.

General Comments

LM's corporate governance is fully compliant in all respects.

LM's commitment is to managing our funds transparently and in the best interests of investors in prevailing market conditions.

The GFC has increased the level of investor complaints across the financial services sectors of the world generally. There are few people it has not affected.

As you would expect, we have properly addressed many complaints during the closure of the FMIF.

There is balance in investor reaction which we would like to share with you. We attach a schedule of some more positive advisor and investor testimonials for your information.

Yours faithfully,



Peter Drake
Chairman and CEO