



**ASX ANNOUNCEMENT  
2 APRIL 2015**

**Notice of Extraordinary General Meeting**

On 2 April 2015, PAYCE Consolidated Limited (**PAYCE**) released a Notice of Extraordinary General Meeting and Explanatory Statement with an Independent Expert's Report.

PAYCE is seeking Shareholder approval to undertake an equal access off-market buy-back of up to 9,915,075 Ordinary Shares, representing one-third of all issued Ordinary Shares in PAYCE (**Buy-Back**).

The consideration for the Buy-Back by PAYCE of each Ordinary Share will be:

- \$0.80 cash paid upon cancellation of the Ordinary Shares;
- \$0.80 cash paid 12 months after the cancellation of the Ordinary Shares;
- \$0.70 cash paid 18 months after the cancellation of the Ordinary Shares and
- one Preference Share issued at \$7.50 on the terms set out in the Explanatory Statement.

The Meeting will be held at 11.30am on 4 May 2015 for Shareholders to vote on the proposal.

All entities associated with PAYCE's Managing Director, Brian Boyd, are excluded from voting on the Resolutions relating to the Buy-Back.

ENDS

Brian Bailison  
Company Secretary



## NOTICE OF EXTRAORDINARY GENERAL MEETING AND EXPLANATORY STATEMENT

In relation to the Extraordinary General Meeting of Shareholders of  
PAYCE Consolidated Limited ABN 19 001 566 310  
to be held as follows:

|                  |  |
|------------------|--|
| <b>Date:</b>     | 4 May 2015   |
| <b>Time:</b>     | 11.30am AEDT   |
| <b>Location:</b> | Pulse, 9 The Crescent, Wentworth Point Sydney, New South Wales |

This Notice of Extraordinary General Meeting and Explanatory Statement should be read in its entirety. If you are in doubt as to how you should vote, you should seek advice from your accountant, solicitor or professional advisor.

This Notice of Extraordinary General Meeting and Explanatory Statement is dated 2 April 2015.

# IMPORTANT NOTICE

## What is this document?

This Notice of Extraordinary General Meeting and Explanatory Statement has been prepared and is issued by PAYCE Consolidated Limited ("**PAYCE**") to allow Shareholders to vote on Resolutions to be put to Shareholders in general meeting.

## No investment advice

The information contained in this Notice of Extraordinary General Meeting and Explanatory Statement does not constitute financial product advice, and has been prepared without reference to Shareholders' particular investment objectives, financial situation, taxation position, and needs. It is important that you read the Notice of Extraordinary General Meeting and Explanatory Statement in its entirety before making any decision on how to vote on the Resolutions. If you are in any doubt, you should consult your professional adviser.

## Responsibility

PAYCE Consolidated Limited has prepared this document.

## Questions

If you have any questions about your holding of Ordinary Shares or the Resolutions, please call + 617 3009 9887 or consult your own professional adviser.

## Date

This Notice of Extraordinary General Meeting and Explanatory Statement is dated 2 April 2015.

# KEY DATES

|                            |  |
|----------------------------|--|
| 2 May 2015<br>11.30am AEDT | Latest date and time for receipt of Proxy Forms for the Extraordinary General Meeting.   |
| 2 May 2015<br>7.00pm AEDT  | Entitlement time and date for determining eligibility to vote at the Extraordinary General Meeting, for the purposes of Corporations Regulation 7.11.37. |
| 4 May 2015<br>11.30am AEDT | Extraordinary General Meeting to be held at Pulse, 9 The Crescent, Wentworth Point Sydney, New South Wales.  |

All references to time in this Notice and Explanatory Statement are to AEDT. This timetable is indicative only. PAYCE reserves the right to vary the timetable set out above.

## GLOSSARY

| Term                          | Definition  |
|-------------------------------|---|
| AEDT                          | Australian Eastern Daylight Time.   |
| Application & Acceptance Form | the personalised acceptance form to be provided to Eligible Shareholders in relation to the Buy-Back  |
| ASIC                          | Australian Securities and Investments Commission  |
| associated entities           | has the meaning given to it in section 50AAA of the Corporations Act, and includes the expression ' <i>entities associated with</i> ' and similar terms   |
| ASX                           | ASX Limited ACN 008 824 691 or the financial market operated by it as the context requires  |
| Buy-Back                      | the proposed off-market equal access share buy-back transaction contemplated by Resolution 1 in the Notice of Extraordinary General Meeting and described in the Explanatory Statement  |
| Buy-Back Limit                | the maximum number of Ordinary Shares which may be bought back, being 9,915,075 Ordinary Shares   |
| Buy-Back Offer Period         | the period during which the Buy-Back is open for acceptance, being from 12 May 2015 to 5.00pm on 1 June 2015  |
| Buy-Back Record Date          | the time and date for determining Shareholders eligible to participate in the Buy-Back, being 7.00pm on 11 May 2015   |
| Closing Date                  | The last day of the Buy-Back Offer Period for the Buy-Back, being 1 June 2015   |
| Corporations Act              | the <i>Corporations Act</i> 2001 (Cth)  |
| Directors                     | the Directors of PAYCE as at the date of the Notice of Extraordinary General Meeting, who include Brian Boyd and the Independent Directors  |
| Dividend                      | cumulative dividends of 6% per annum for the first 12 months, increasing by 1% per annum until the rate reaches 12% per annum, proposed to be paid quarterly on the Preference Shares, subject to such Dividends being declared at the discretion of PAYCE. See Section 2.2(e) for further details. |
| Dividend Payment Date         | the date on which a Dividend is scheduled to be paid on the Preference Shares (being each 3 September, 3 December, 3 March and 3 June), subject to such Dividends being declared at the discretion of PAYCE   |

| Term  | Definition   |
|---|--|
| Dividend Payment Restriction                      | <p>a restriction imposed on PAYCE's ability to:</p> <ul style="list-style-type: none"> <li>• declare or pay dividends on any class of share capital other than Preference Shares; or</li> <li>• redeem, reduce, cancel buy-back or acquire for any consideration any share capital,</li> </ul> <p>as summarised in section 2.2(f) and set out in clause 3.7 of Schedule 1.</p> |
| Eligible Shareholder                              | a Shareholder who is a registered holder of Ordinary Shares on the Buy-Back Record Date  |
| Ex-Entitlement Date                               | the date on which Ordinary Shares commence trading without an entitlement to participate in the Buy-Back, 7 May 2015   |
| Explanatory Statement                             | the Explanatory Statement accompanying the Notice of Extraordinary General Meeting   |
| Extraordinary General Meeting                     | the meeting of Shareholders called for 4 May 2015 as convened by the attached Notice of Extraordinary General Meeting  |
| Independent Directors                             | Mr Roger Short and Mr Christopher Gabriel, who are non-executive Directors of PAYCE  |
| Independent Expert                                | Hanrick Curran Corporate Finance Pty Ltd, being the independent expert engaged by PAYCE to prepare the Independent Expert's Report   |
| Independent Expert's Report                       | the report prepared by the Independent Expert in accordance with ASIC Regulatory Guides 111 and 112 to provide an opinion as to whether the Buy-Back is fair and reasonable to all PAYCE Shareholders, a copy of which is annexed to the Explanatory Statement   |
| Listing Rules                                     | the listing rules of ASX   |
| Non Associated Shareholders                       | those Shareholders who are not associated with Managing Director Mr Brian Boyd   |
| Notice of Extraordinary General Meeting or Notice | the notice of meeting giving notice to Shareholders of the Extraordinary General Meeting, accompanying the Explanatory Statement   |
| Offer   | the offer to Eligible Shareholders to participate in the Buy-Back on the basis set out in Section 6  |
| Offer Document                                    | the document setting out the Offer to Eligible Shareholders, including the   |

| Term                    | Definition  |
|-------------------------|---|
|                         | terms of the Buy-Back, a prospectus for the issue of Preference Shares, and a personalised Application & Acceptance Form  |
| Opening Date            | the first day of the Buy-Back Offer Period for the Buy-Back, being 12 May 2015  |
| Ordinary Resolution     | a resolution passed by at least 50% of total votes cast by Shareholders entitled to vote on the Resolution  |
| Ordinary Share          | an ordinary share in the capital of PAYCE   |
| PAYCE                   | PAYCE Consolidated Limited ABN 19 001 566 310   |
| Preference Shares       | the securities which are to be issued to Shareholders in partial consideration for the Buy-Back, the terms of which are summarised in Section 2.2 and set out in detail in Schedule 1 of this Notice of Extraordinary General Meeting   |
| Preference Share Holder | a registered holder of Preference Shares in PAYCE   |
| Preference Share Terms  | the terms and conditions on which the Preference Shares are to be issued, as set out in in Schedule 1 of this Notice of Extraordinary General Meeting.  |
| Proxy Form              | the proxy form enclosed with this Notice of Extraordinary General Meeting   |
| Register                | the register of members of PAYCE maintained in accordance with the Corporations Act   |
| Registry                | Boardroom Pty Limited, which operates the Register  |
| Resolutions             | the resolutions set out in this Notice of Extraordinary General Meeting   |
| Scale Back              | a proportionate reduction in the number of Ordinary Shares to be bought back from each Eligible Shareholder below the number of Ordinary Shares for which acceptances have been received under the Buy-Back to avoid the Buy-Back Limit being exceeded. ' <b>Scaling Back</b> ' and ' <b>Scaled Back</b> ' have a corresponding meaning. See Section 2.1 for further details. |
| Shareholder             | a registered holder of Ordinary Shares in PAYCE   |
| Special Resolution      | a resolution passed by at least 75% of total votes cast by Shareholders entitled to vote on the Resolution  |

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# LETTER TO SHAREHOLDERS

2 April 2015

Dear Shareholder

## EXTRAORDINARY GENERAL MEETING

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We are pleased to provide you with the Notice of Extraordinary General Meeting and Explanatory Statement in relation to the meeting of Shareholders of PAYCE Consolidated Limited to be held on 4 May 2015.

The Directors of PAYCE Consolidated Limited (**PAYCE**) are seeking Shareholder approval for an equal access off-market buy-back of a maximum of 9,915,075 Ordinary Shares in PAYCE (**Buy-Back**), representing one-third of all issued Ordinary Shares. The Buy-Back will be open to all Shareholders on an equal basis (subject to the Scaling Back provisions), and participation by Shareholders is entirely voluntary.

The consideration for the Buy-Back by PAYCE of each Ordinary Share will be:

- \$0.80 cash paid upon cancellation of the Ordinary Shares;
- \$0.80 cash paid 12 months after the cancellation of the Ordinary Shares;
- \$0.70 cash paid 18 months after the cancellation of the Ordinary Shares and
- one Preference Share issued at \$7.50 on the terms summarised in Section 2.2 and set out in greater detail in Schedule 1 of the Explanatory Statement.

The Independent Directors of PAYCE are of the opinion that the proposal to undertake the Buy-Back of Ordinary Shares, in consideration for a combination of cash and Preference Shares, is in the best interests of Shareholders. An Independent Expert's Report has been prepared in order to provide Shareholders with an independent opinion regarding the fairness and reasonableness of the proposed Buy-Back to Non Associated Shareholders and the value of the consideration being offered. This report concludes that the consideration for the Buy-Back is both fair and reasonable; it is annexed to the Explanatory Statement for your consideration.

All entities associated with PAYCE's Managing Director Brian Boyd, have undertaken to refrain from voting on the Resolutions relating to the Buy-Back.

This document contains a Notice of Extraordinary General Meeting and Explanatory Statement, and is accompanied by a Proxy Form for the Extraordinary General Meeting of PAYCE to be held at 11.30am on 4 May 2015.

### Recommendation for Share Buy-Back

This proposal is being put to Shareholders as part of PAYCE's ongoing commitment to manage its capital structure. The Directors believe that the proposed Ordinary Share Buy-Back and issue of Preference Shares is in the best interests of PAYCE.

The Independent Directors **recommend** that you **vote in favour of the Resolutions to approve the Buy-Back and issue Preference Shares.**

**Your vote is important.** Shareholders are encouraged to vote by completing and returning the **enclosed** Proxy Form in the mail, by fax or online, or alternatively to attend the Meeting itself. Proxy Forms must be received no later than 11.30am on 2 May 2015.

### Further information

If you have any questions in relation to the Extraordinary General Meeting, please call +61 7 3009 9887.

Yours sincerely

**PAYCE Consolidated Limited**



# NOTICE OF EXTRAORDINARY GENERAL MEETING

PAYCE Consolidated Limited ABN 19 001 566 310 gives notice that an Extraordinary General Meeting of Shareholders will be held at Pulse, 9 The Crescent, Wentworth Point, Sydney, New South Wales on 4 May 2015 at 11.30am AEDT to consider the Resolutions set out below:

## BUSINESS OF THE EXTRAORDINARY GENERAL MEETING

### 1. Resolution 1: Approval of Share Buy-Back

To consider and, if thought fit, pass the following resolution as an Ordinary Resolution:

*'That, subject to and conditional upon the passing of Resolution 2, in accordance with section 257C(1) of the Corporations Act and for all other purposes, approval is given for PAYCE to conduct an off-market equal access buy-back of a maximum of 9,915,075 of PAYCE's issued Ordinary Shares on the terms detailed in the Explanatory Statement which accompanies this Notice of Extraordinary General Meeting.'*

#### Voting Exclusion Statement

PAYCE will disregard any votes cast by Brian Boyd and any of his associates, including Lanox Pty Ltd and Ruz Pty Ltd.

The Independent Directors recommend that you vote in favour of the Resolution.

### 2. Resolution 2: Approval for the Issue of Preference Shares

To consider and, if thought fit, pass the following resolution as a Special Resolution:

*'That, subject to and conditional upon the passing of Resolution 1, in accordance with section 254A(2) of the Corporation Act and for all other purposes, approval be and is hereby given to the issue of a maximum of 9,915,075 Preference Shares on the terms and conditions set out in the Explanatory Statement accompanying this Notice of Extraordinary General Meeting.'*

#### Voting Exclusion Statement

PAYCE will disregard any votes cast by Brian Boyd and any of his associates, including Lanox Pty Ltd and Ruz Pty Ltd.

The Independent Directors recommend that you vote in favour of the Resolution.

DATED 2 April 2015

By Order of the Directors

Brian Bailison

Company Secretary

## VOTING & ELIGIBILITY

### How to vote

To vote on the Resolutions, you may either:

- complete the enclosed Proxy Form and return it to the Registry no later than 11.30am AEDT on 2 May 2015; or
- attend the Extraordinary General Meeting to be held at Pulse, 9 The Crescent, Wentworth Point NSW on 4 May 2015 at 11.30am.

Details of how to complete the Proxy Form are set out on the form itself.

### Voting intentions of the Chair

The Chair intends to vote any undirected proxies appointing the Chair as proxy **in favour of the Resolutions**.

### Voting

|              |  |
|--------------|--|
| Resolution 1 | is an Ordinary Resolution which must be passed by at least 50% of total votes cast by Shareholders entitled to vote on the Resolution. |
| Resolution 2 | is a Special Resolution which must be passed by at least 75% of total votes cast by Shareholders entitled to vote on the Resolution.   |

### Entitlement to vote

All Shareholders recorded on the register at 7.00pm on 2 May 2015 are entitled to attend and vote at the Extraordinary General Meeting. Transfers registered after this time will be disregarded in determining entitlements to vote at the Extraordinary General Meeting.

### Jointly held interests

If an interest in PAYCE is held jointly, and more than one Shareholder votes in respect of that interest, only the vote of the Shareholder whose name appears first in the register of Shareholders will be counted.

### Appointment of proxy

If you are entitled to vote at the Extraordinary General Meeting, you have the right to appoint a proxy. A Proxy Form is enclosed with this Notice of Extraordinary General Meeting. The proxy does not need to be a Shareholder in PAYCE.

Instructions regarding completion of the Proxy Form are set out on the form.

## Corporate Representative

If a representative of a corporate Shareholder or proxy is to attend the meeting you will need to provide the appropriate 'Certificate of Appointment of Corporate Representative' prior to admission to the meeting.

A form of the certificate may be obtained from the Registry on request.

Shareholders can vote by proxy or in person. Instructions on how to complete your Proxy Form are set out on the form itself. Your Proxy Form should be:

POSTED TO:                Boardroom Pty Limited  
                                 GPO Box 3993  
                                 SYDNEY NSW 2001

OR FAXED TO:            +61 2 9290 9655

OR DELIVERED TO:      Boardroom Pty Limited  
                                 Level 7, 207 Kent Street  
                                 SYDNEY NSW 2000

OR ONLINE AT:          [www.votingonline.com.au/payceegm2015](http://www.votingonline.com.au/payceegm2015)

# EXPLANATORY STATEMENT

## 1. OVERVIEW

### 1.1. THE OFFER

This Explanatory Statement provides background and information relevant to the consideration of the Resolutions proposed to be considered at PAYCE's meeting to be held on 4 May 2015 concerning the equal access off-market buy-back of a maximum of 9,915,075 Ordinary Shares in PAYCE and the issue of Preference Shares as partial consideration for the Buy-Back.

This Explanatory Statement has been prepared to give Shareholders all information they would reasonably require to enable them to make a fully informed decision about how to vote on the Resolutions.. An Independent Expert's Report has been included with this Explanatory Statement in order to provide Shareholders with an independent opinion regarding the fairness and reasonableness of the proposed Buy-Back and the value of the consideration being offered. The Independent Expert's Report, which concludes that the Buy-Back consideration is fair and reasonable, is annexed to the Explanatory Statement.

You are encouraged to read this Explanatory Statement carefully before deciding how to vote on the Resolutions.

The Resolutions are interdependent, meaning that Shareholders must pass both Resolutions for the Buy-Back to proceed, and the Preference Shares to be issued.

This Explanatory Statement is not intended to provide financial or tax advice and has been prepared without taking into account the personal circumstances of any person. Each Shareholder should obtain their own independent professional advice before making any decisions regarding the content of this Explanatory Statement or the Notice of Extraordinary General Meeting, or how to vote on the Resolutions.

### 1.2. DEFINITIONS AND INTERPRETATION

Capitalised words and expressions used in the Notice of Extraordinary General Meeting and Explanatory Statement are defined in the Glossary section of this document.

### 1.3. PURPOSE

The purpose of this Explanatory Statement is to explain the potential effect and implications of:

- (a) the Resolutions proposed in the Notice of Extraordinary General Meeting; and
- (b) the proposed Buy-Back of Shares and issue of Preference Shares which will take place if the Resolutions are approved.

#### 1.4. TIMETABLE

The indicative timetable for the proposed Buy-Back is set out below. Subject to the Corporations Act and the Listing Rules, PAYCE reserves the right to amend this indicative timetable without prior notice to Shareholders.

| Event  | Date                        |
|--|-----------------------------|
| Extraordinary General Meeting Record Date<br>(Date for determining entitlement to vote at the Extraordinary General Meeting) | 7.00pm on<br>2 May 2015     |
| Proxy cut off time<br>(Proxy Forms and the authority under which they are signed (if any) must be lodged by this time)       | 11.30am on<br>2 May 2015    |
| Extraordinary General Meeting  | 11.30am on<br>4 May 2015    |
| Ex-Entitlement Date for the Buy-Back   | 7 May 2015                  |
| Buy-Back Record Date<br>(Date for determining entitlement to participate in the Buy-Back)                                    | 11 May 2015                 |
| Despatch of Offer Document to Eligible Shareholders  | 12 May 2015                 |
| Opening Date   | 12 May 2015                 |
| Closing Date   | 1 June 2015                 |
| Announcement of the outcome of the Buy-Back and details of any Scale Back  | 2 June 2015                 |
| Transfer to PAYCE of Ordinary Shares bought back and cancellation of those Ordinary Shares                                   | On or before<br>3 June 2015 |
| Payment of initial portion of cash consideration and issue of Preference Shares as consideration for the Buy-Back            | On or before<br>3 June 2015 |
| Despatch of holding statements for Preference Shares   | On or before<br>3 June 2015 |
| Payment of first deferred portion of cash consideration  | 3 June 2016                 |
| Payment of second deferred portion of cash consideration   | 3 December 2016             |

All times are references to AEDT.

## 2. **RESOLUTION 1 – APPROVAL OF SHARE BUY-BACK**

### 2.1 THE PROPOSAL

At the Extraordinary General Meeting, Shareholders will be asked to consider the proposed Buy-Back, the details of which are summarised below. Please refer to Section 6 of this document for further details of the terms and conditions on which PAYCE proposes to undertake the Buy-Back.

By voting in favour of Resolution 1, Shareholders will be authorising PAYCE to offer Shareholders the opportunity to participate in the Buy-Back. Voting in favour of Resolution 1 does not require any Shareholder to sell their Ordinary Shares into the Buy-Back. If Resolution 1 is passed, each Shareholder will still be completely unfettered in their decision to sell all, some or none of their Ordinary Shares to PAYCE as part of the Buy-Back.

If Shareholders approve both Resolutions, a separate Offer Document will be sent to all Eligible Shareholders, setting out the terms of the Buy-Back and incorporating a prospectus for the issue of Preference Shares, and a personalised Application & Acceptance Form.

| Question                            | Answer  |
|-------------------------------------|---|
| (a) What is PAYCE proposing?        | <p>PAYCE is proposing to undertake an off-market equal access buy-back of a maximum of 9,915,075 Ordinary Shares, being one-third of all issued Ordinary Shares.</p> <p>If the Buy-Back proceeds, Eligible Shareholders may elect to participate and, subject to the Scale Back, sell all or some of their Ordinary Shares to PAYCE for a combination of cash and Preference Shares as set out in item (e) below.</p>   |
| (b) What is a buy-back?             | <p>Under a buy-back, a company purchases its own shares back from shareholders who elect to participate in the buy-back offer. Shareholders may elect to participate in the buy-back at their discretion. The shares bought back are cancelled, which reduces the total amount of shares which the company has on issue by the number of shares bought back.</p>  |
| (c) What is an equal access scheme? | <p>An 'equal access' scheme is a type of buy-back. Section 257B of the <i>Corporations Act</i> prescribes that, in an equal access buy-back:</p> <ul style="list-style-type: none"><li>(a) the offers must relate only to ordinary shares;</li><li>(b) the offers must be made to every person who holds ordinary shares to buy-back the same percentage of their ordinary shares;</li><li>(c) all of those persons must have a reasonable opportunity to accept offers made to them;</li></ul> |

| Question  | Answer   |
|---|--|
|   | <p>(d) buy-back agreements must not be entered into until a specified time for acceptance of offers has closed; and</p> <p>(e) the terms of the offers must be the same.</p>   |
| (d) Why is PAYCE proposing the Buy-Back?                        | <p>The Directors of PAYCE have considered a variety of capital management strategies which may offer Shareholders liquidity in an otherwise illiquid stock, and maintain PAYCE's financial position and ability to maintain its business operations. The Directors believe that the proposed Buy-Back is the optimal means of achieving these aims. Further discussion on other alternatives considered by the Directors is set out in Section 2.4.</p>  |
| (e) What is the consideration for the Buy-Back?                 | <p>PAYCE is proposing to undertake an off-market equal access buy-back of a maximum of 9,915,075 Ordinary Shares.</p> <p>In consideration for the buy-back of their Ordinary Shares, Shareholders who elect to participate in the Buy-Back will receive the following for each Ordinary Share bought back:</p> <ul style="list-style-type: none"> <li>• \$0.80 cash paid upon cancellation of the Ordinary Shares;</li> <li>• \$0.80 cash paid 12 months after the cancellation of the Ordinary Shares;</li> <li>• \$0.70 cash paid 18 months after the cancellation of the Ordinary Shares; and</li> <li>• one Preference Share issued at \$7.50 upon cancellation of the Ordinary Shares.</li> </ul> |
| (f) How will the Buy-Back be paid and funded?                   | <p>The cash component of the consideration will be funded from PAYCE's cash reserves. The Preference Shares will be issued subject to approval of Resolution 2.</p>  |
| (g) Are the terms of the proposed Buy-Back fair and reasonable? | <p>To assist PAYCE Shareholders in their consideration of the Buy-Back, PAYCE commissioned the Independent Expert to prepare the Independent Expert's Report, and express an opinion as to whether the Buy-Back is fair and reasonable to all Shareholders.</p> <p>A copy of this report is <b>annexed</b> to the Explanatory</p>  |

| Question  | Answer   |
|---|--|
|   | <p>Statement.</p> <p>In summary, the Independent Expert has determined that the Buy-Back is fair and reasonable to PAYCE Shareholders.</p>   |
| (h) Who may participate in the Buy-Back?                                  | Eligible Shareholders are Shareholders who hold Ordinary Shares in PAYCE on the Buy-Back Record Date, as recorded on the Register. Participation in the Buy-Back is voluntary.   |
| (i) Which Shares may be accepted into the Buy-Back?                       | <p>PAYCE is offering to buy-back a maximum of 9,915,075 Ordinary Shares from Eligible Shareholders.</p> <p>Eligible Shareholders may accept the Buy-Back offer in relation to some or all of the Ordinary Shares held by the Eligible Shareholder on the Buy-Back Record Date, subject to any Scale Back required in order to comply with the Buy-Back Limit of 9,915,075 Ordinary Shares.</p> <p>Ordinary Shares acquired on or after the Ex-Entitlement Date (currently anticipated to be 7 May 2015), will not be registered in the new Shareholder's name in time for the Buy-Back Record Date, and therefore will not be able to participate in the Buy-Back.</p>                             |
| (j) What is the Scale Back?   | <p>The maximum number of PAYCE Ordinary Shares that will be bought back under the Buy-Back is 9,915,075 Ordinary Shares. If the total number of Ordinary Shares accepted into the Buy-Back by Eligible Shareholders exceeds the Buy-Back Limit of 9,915,075 Ordinary Shares, the Scale Back will operate to proportionately reduce acceptances so that the Buy-Back Limit is not exceeded. In calculating the number of Ordinary Shares that will be bought back, all fractions will be rounded down.</p> <p>Shortly following closure of the Buy-Back on 1 June 2015, PAYCE will make an announcement summarising the total acceptances received and outlining the details of any Scale Back.</p> |
| (k) What are the voting intentions of Directors who hold Ordinary Shares? | The interests of Directors in Ordinary Shares as at the date of this Explanatory Statement are detailed in the following table:  |



| Question  | Answer  |                 |                                |                 |            |               |           |            |             |           |                     |                |   |             |                  |        |
|---|---|-----------------|--------------------------------|-----------------|------------|---------------|-----------|------------|-------------|-----------|---------------------|----------------|---|-------------|------------------|--------|
|   | <table><tr><th>Director</th><th>Associated shareholding entity</th><th>Ordinary Shares</th></tr><tr><td>Brian Boyd</td><td>Lanox Pty Ltd</td><td>8,806,799</td></tr><tr><td>Brian Boyd</td><td>Ruz Pty Ltd</td><td>2,718,661</td></tr><tr><td>Christopher Gabriel</td><td>Not applicable</td><td>0</td></tr><tr><td>Roger Short</td><td>Jurocorp Pty Ltd</td><td>65,000</td></tr></table> <p>The entities associated with PAYCE’s Managing Director, Brian Boyd, will refrain from voting on the Resolutions, and in any event, PAYCE will disregard any votes cast by Brian Boyd and his associated entities.</p> <p>Roger Short intends to vote in favour of the Buy-Back in respect of the Ordinary Shares he controls.</p> <p>Christopher Gabriel holds no Ordinary Shares and therefore will not vote on the Resolutions.</p> <p>If Resolution 1, being the approval of the Share Buy-Back is passed, then the entities associated with Brian Boyd and Roger Short will participate in the Buy-Back as follows:</p> <ul style="list-style-type: none"><li>• Lanox Pty Ltd will not participate in the Buy-Back;</li><li>• Ruz Pty Ltd will participate in the Buy-Back for up to 1,660,000 Ordinary Shares; and</li><li>• Jurocorp Pty Ltd will participate in the Buy-Back for 40,000 of Ordinary Shares.</li></ul> | Director        | Associated shareholding entity | Ordinary Shares | Brian Boyd | Lanox Pty Ltd | 8,806,799 | Brian Boyd | Ruz Pty Ltd | 2,718,661 | Christopher Gabriel | Not applicable | 0 | Roger Short | Jurocorp Pty Ltd | 65,000 |
| Director  | Associated shareholding entity  | Ordinary Shares |                                |                 |            |               |           |            |             |           |                     |                |   |             |                  |        |
| Brian Boyd  | Lanox Pty Ltd   | 8,806,799       |                                |                 |            |               |           |            |             |           |                     |                |   |             |                  |        |
| Brian Boyd  | Ruz Pty Ltd   | 2,718,661       |                                |                 |            |               |           |            |             |           |                     |                |   |             |                  |        |
| Christopher Gabriel                               | Not applicable  | 0               |                                |                 |            |               |           |            |             |           |                     |                |   |             |                  |        |
| Roger Short                                       | Jurocorp Pty Ltd  | 65,000          |                                |                 |            |               |           |            |             |           |                     |                |   |             |                  |        |
| (l) What is the process for offer and acceptance? | <p>Subject to the approval of both Resolutions, the Buy-Back period will commence on 12 May 2015, and remain open until 1 June 2015. On 12 May 2015, personalised Application &amp; Acceptance Forms will be sent to Shareholders who are determined to be eligible to participate in the Buy-Back.</p> <p>Eligible Shareholders will have from the Opening Date of 12 May 2015 until the Closing Date of 1 June 2015 to accept the Offer in respect of some or all of their Ordinary Shares.</p> <p>An Offer Document for the Preference Shares to be issued as partial consideration for the Buy-Back will be</p>   |                 |                                |                 |            |               |           |            |             |           |                     |                |   |             |                  |        |

| Question   | Answer  |
|--|---|
|  | <p>distributed to Shareholders in due course. Subject to Shareholder approval of the Resolutions for the Buy-Back and issue of Preference Shares being obtained, personalised Application &amp; Acceptance Forms will be despatched by 12 May 2015 to Eligible Shareholders holding Shares on the Buy-Back Record Date of 11 May 2015.</p> <p>PAYCE reserves the right to withdraw the Offer if the Directors determine it is necessary to do so.</p>   |
| (m) Cancellation of Shares bought back                                   | <p>All Shares bought back by PAYCE will be cancelled upon being bought back. This will reduce the total number of Ordinary Shares on issue.</p>   |
| (n) How does this proposal compare to selling Ordinary Shares on market? | <p>It is possible that Shareholders may be able to sell their Ordinary Shares for cash consideration on the ASX. However, such a sale would incur brokerage. Ordinary Shares accepted into the Buy-Back do not attract brokerage costs.</p> <p>The market price for Ordinary Shares on the ASX may be, or may move, to a price which is lower or higher in value than the consideration being offered under the Buy-Back. It may also vary significantly in the future.</p> <p>PAYCE recommends that all Shareholders seek professional advice before deciding whether or not to participate in the Buy-Back.</p> |
| (o) What are the taxation consequences of the Buy-back?                  | <p>As detailed in section 7.2, the Buy-back price of \$9.80 includes a component of deemed unfranked dividends for taxation purposes (\$8.26 per Ordinary Share) no franking credits will be utilised in relation to the Buy-back.</p> <p><b>Shareholders should seek independent taxation advice.</b></p> <p>It is possible that some Shareholders may have an income tax liability that exceeds the cash component of the Buy-back consideration.</p>   |

## 2.2 FEATURES OF PREFERENCE SHARES

The consideration for the Buy-Back of Shares will comprise a combination of both cash and Preference Shares. Set out below is a summary of the key features of the Preference Shares. Further details are set out in Schedule 1:

| Feature   | Details   |
|---|---|
| (a) Issue price   | <p>Preference Shares will be issued as partial consideration for the Buy-Back of Ordinary Shares in PAYCE. The consideration for the Buy-Back of each Ordinary Share in PAYCE will be:</p> <ul style="list-style-type: none"><li>• \$0.80 cash paid upon cancellation of the Ordinary Shares;</li><li>• \$0.80 cash paid 12 months after the cancellation of the Ordinary Shares;</li><li>• \$0.70 cash paid 18 months after the cancellation of the Ordinary Shares; and</li><li>• one Preference Share issued at \$7.50 upon cancellation of the Ordinary Shares.</li></ul> |
| (b) No right to have Preference Shares purchased or bought back | <ul style="list-style-type: none"><li>• The Preference Shares have no fixed maturity date.</li><li>• Holders of Preference Shares do not have the right to have those securities purchased or bought-back.</li></ul>  |
| (c) Call Option   | <p>Each holder of Preference Shares grants PAYCE an option to purchase or buy back those Preference Shares for a cash consideration of \$7.50 each on any Dividend Payment Date, subject to the requirements of the Corporations Act and Listing Rules. PAYCE must give Preference Share Holders at least 30 days prior notice that it intends to exercise this option.</p>   |
| (d) Change in Control Event                                     | <p>If a Change in Control Event (as defined in clause 1 in Schedule 1) occurs, PAYCE may also exercise its call option to purchase or buy back the Preference Shares for a cash consideration of \$7.50 per Preference Share.</p>   |
| (e) Dividends   | <ul style="list-style-type: none"><li>• Cumulative Dividends of 6% per annum for the first 12 months, proposed to be paid quarterly on the Dividend Payment Dates, subject to such Dividends being declared at the discretion of PAYCE.</li><li>• On each yearly anniversary of the issue of the</li></ul>  |

| Feature                          | Details   |
|----------------------------------|---|
|                                  | <p>Preference Shares, the dividend rate will increase by an additional 1% per annum. For example:</p> <ul style="list-style-type: none"> <li>○ After one year from the date of issue, the dividend rate will increase to 7% per annum.</li> <li>○ After two years from the date of issue, the dividend rate will increase to 8% per annum, until the date which is six years from the date of issue, at which time the dividend rate will be capped at 12% per annum.</li> </ul> <ul style="list-style-type: none"> <li>● If PAYCE elects to pay a Dividend on the Preference Shares, it has the discretion to pay the Dividends by either cash, the issue of additional Preference Shares at \$7.50 each (plus any outstanding dividend entitlement in cash), or a combination of cash and Preference Shares.</li> </ul>   |
| (f) Dividend Payment Restriction | <ul style="list-style-type: none"> <li>● Dividends are proposed to be paid quarterly on the Dividend Payment Dates, subject to such Dividends being declared at the discretion of PAYCE.</li> <li>● If no Dividends are paid on the Preference Shares on the Dividend Payment Date, PAYCE is prohibited from paying dividends or making any other distribution on any class of its share capital other than Preference Shares or reducing or buying back any share capital, unless: <ul style="list-style-type: none"> <li>○ an amount equal to unpaid scheduled Dividends for the period immediately preceding the date of payment of that amount (<b>Optional Dividend</b>) has been paid to Preference Share Holders; or</li> <li>○ all Preference Shares have been purchased or bought-back.</li> </ul> </li> <li>● For the avoidance of doubt, the non-payment of a Dividend on a scheduled Dividend Payment Date, does not constitute a breach of the terms of the Preference Shares. However, if PAYCE elects not to pay a Dividend on a scheduled Dividend Payment Date, PAYCE is restricted from paying dividends on, or buying back, any other class of share capital. If, despite this restriction, PAYCE pays dividends on or buys back another class of shares, this constitutes breach of the Dividend Payment Restriction, the consequences of which are set out below.</li> </ul> |

| Feature  | Details   |
|--|---|
| (g) Consequences of breach of Dividend Payment Restriction | In the event that PAYCE breaches the Dividend Payment Restriction outlined above (for example, by not paying a Dividend on Preference Shares on a scheduled Dividend Payment Date but subsequently paying a dividend on Ordinary Shares), and does not remedy that breach within 90 days, the Preference Shares will be exchanged for redeemable preference shares which are redeemable immediately at the option of holders. Each Preference Share will be exchanged for one redeemable preference share. See clauses 3.8 to 3.10 of Schedule 1 for further details. |
| (h) Status and Ranking                                     | The Preference Shares will rank equally among themselves, and ahead of Ordinary Shares in relation to dividends and the return of capital, but will have no entitlement to share in any surplus in the event of a winding up.   |
| (i) Voting   | Generally, the Preference Shares will carry no right to vote at any general meeting of Shareholders of PAYCE. However, in limited circumstances as set out in the Preference Share Terms in Schedule 1, holders of Preference Shares may vote on the basis of one vote per Preference Share.  |
| (j) Participation  | Preference Shares do not carry any right to participate in issues of securities or capital reconstructions of PAYCE.  |
| (k) Selling Restrictions                                   | Preference Shares will be transferable.   |

## 2.3 EFFECT OF THE BUY-BACK ON PAYCE

### (a) Introduction

This section sets out the implications of the Buy-Back for PAYCE, on the assumption that the Resolutions are approved and the Buy-Back is implemented.

### (b) Effect on PAYCE's financial position

#### *Financial effect of the Buy-Back*

The cash component of the consideration for the Buy-Back will be paid out of PAYCE's cash reserves. Assuming acceptances are received in respect of the maximum number of Ordinary Shares able to be acquired under the Buy-Back (ie. 9,915,075 Ordinary Shares), the Buy-Back will reduce PAYCE's cash reserves by:

- \$7,932,060 upon cancellation of the Ordinary Shares;
- \$7,932,060 twelve months after the cancellation of the Ordinary Shares; and
- a further \$6,940,553 eighteen months after the cancellation of the Ordinary Shares.

If the Buy-Back Limit is not reached, the Buy-Back will reduce PAYCE's cash reserves by a smaller amount. The actual amount of cash that PAYCE will be required to pay to fund the cash component of the Buy-Back may vary depending on the number of Ordinary Shares which participate in the Buy-Back.

As detailed in Section 7.2, the Buy-Back price of \$9.80 includes a component of deemed unfranked dividends for taxation purposes (\$8.26 per Ordinary Share). No franking credits will be utilised in relation to the Buy-Back.

As the major portion of the Buy-Back consideration is represented by the value of Preference Shares, ordinary share capital and retained earnings will be reduced whilst Preference Share capital will increase.

#### *Ability to pay Dividends*

During the financial years ending June 2013 and June 2014, PAYCE declared dividends of 10 cents per share each year on its Ordinary Shares.

Dividends on the Preference Shares being offered as partial consideration for the Buy-Back, are payable quarterly at 6% per annum for the first 12 months, increasing by 1% per annum until the rate reaches 12% per annum, subject to such Dividends being declared at the discretion of PAYCE. Section 2.2(e) describes the nature of these Dividends in greater detail.

Any Dividends paid on the Preference Shares may be by way of cash, the issue of further Preference Shares, or a combination of both.

PAYCE will only declare a cash Dividend where it has the necessary cash to pay the relevant amount. Otherwise, Dividends if declared, will be paid by way of the issue of further Preference Shares, or a combination of both cash and Preference Shares.

**(c) Effect on PAYCE's capital structure**

As at the date of this Explanatory Statement, PAYCE has 29,745,225 fully paid Ordinary Shares on issue. All of the Ordinary Shares that are bought back under the Buy-Back will be cancelled. Consequently, the Buy-Back will reduce the total number of Ordinary Shares on issue.

If PAYCE buys back the maximum number of Ordinary Shares under the Buy-Back, being 9,915,075 Ordinary Shares (or one-third of Ordinary Shares currently on issue), then the number of Ordinary Shares on issue will be reduced to 19,830,150.

Whilst the number of fully paid Ordinary Shares will decrease, the number of Preference Shares will increase by the same number. If PAYCE issues the maximum number of Preference Shares, then the number of Preference Shares on issue will be 9,915,075.

**(d) Effect of the Buy-Back on the control of PAYCE**

If both Resolutions are approved and the Buy-Back proceeds, all of the Ordinary Shares which are bought back will be cancelled. If the Buy-Back Limit is reached, the total number of Ordinary Shares on issue will reduce from 29,745,225 to 19,830,150.

As a consequence of the cancellation of Ordinary Shares bought back by PAYCE, the percentage shareholding and voting power of Shareholders who do not participate in the Buy-Back will increase.

This may materially alter the ownership makeup of PAYCE. At this point, it is not possible to determine the precise extent to which the ownership makeup of PAYCE will change, as that will depend on the level of participation in the Buy-Back. Shareholders should, however, take into account the following considerations:

***(i) Position of PAYCE's largest shareholder***

PAYCE's largest Shareholder is Lanox Pty Ltd, which is associated with Mr Brian Boyd, the Managing Director of PAYCE. Mr Boyd has advised PAYCE that Lanox Pty Ltd, which holds 8,806,799 Ordinary Shares, will not participate in the Buy-Back, but will continue to maintain its shareholding.

Mr Boyd is also associated with Ruz Pty Ltd, which holds 2,718,661 Ordinary Shares. Mr Boyd has advised that this entity intends to participate in the Buy-Back for up to 1,660,000 Ordinary Shares, and will retain a minimum of 1,058,661 Ordinary Shares (without any Scale Back occurring).

Mr Boyd's intentions in relation to participation in the Buy-Back, and the application of any Scale Back, will ensure that following the Buy-Back, entities associated with Mr Boyd will continue to hold less than 50% of the Ordinary Shares in PAYCE in total.



In practical terms, depending on the level of participation by Shareholders in the Buy-Back, the voting power of entities associated with Mr Boyd may increase, giving his associated entities a potentially greater capacity to influence the voting results of resolutions which may be considered by PAYCE Shareholders in the future (by voting for or against such resolutions). Such resolutions could include, for example, resolutions to appoint or remove directors, to amend the constitution of PAYCE, or to increase or decrease the number of shares on issue. Under the Corporations Act entities associated with Mr Boyd would be excluded from voting on resolutions where Mr Boyd or those associated entities may benefit from it or are affected by it.

Any resolutions which could be considered by PAYCE Shareholders in the future would require the approval of a minimum of 50% of total votes cast by Shareholders entitled to vote on the resolution. As Mr Boyd will ensure that, following the Buy-Back, his associated entities will hold less than 50% of the total Ordinary Shares on issue irrespective of the level of participation in the Buy-Back, these entities will not be able to control the results of any resolution, but could have a substantial influence on the outcome of any resolution.

*(ii) Background and experience of PAYCE's largest shareholder*

As noted above, PAYCE's largest Shareholder is Lanox Pty Ltd, which is associated with Mr Boyd. As PAYCE's Managing Director, Mr Boyd has over 32 years' experience in the property development industry and brings a wealth of commercial experience and knowledge to development projects. He has been the Managing Director of PAYCE for more than 25 years. The Independent Directors consider Mr Boyd to be a significant and desired investor in PAYCE.

Lanox Pty Ltd has advised that it will not participate in the Buy-Back, but will continue to maintain its shareholding in PAYCE. Depending on the rate of participation of other Shareholders in the Buy-Back, Lanox Pty Ltd's voting power in PAYCE is anticipated to increase as the Buy-Back is undertaken.

Subject to the level of acceptances by other Shareholders in the Buy-Back, the percentage shareholding of Lanox Pty Ltd in PAYCE is likely to increase to 49.75%. However, it is anticipated that the implications of having Lanox Pty Ltd remain a Shareholder of PAYCE, will not have a material impact on the direction of PAYCE. Mr Boyd, through associated entities, has historically held a significant interest in PAYCE. Mr Boyd has indicated that he will continue to act in the best interests of PAYCE in his capacity as both a Director, and indirectly through his interest in Lanox Pty Ltd. Mr Boyd has advised that he does not intend to use any increased voting power that may be obtained through his associated entities following the Buy-Back to significantly change PAYCE's principal business of undertaking property development projects.

*(iii) Other Shareholders' Intentions*

The intentions of Garry Boyd and his associated entities, being the second largest substantial holder of Ordinary Shares in PAYCE, are to accept the Buy-back offer for 50% of his and his associates' holdings. The intentions of the remaining shareholders are unknown.

**(e) Impact on the liquidity of Ordinary Shares**

As noted above, if the Buy-Back is approved, the Ordinary Shares accepted into the Buy-Back will be transferred to PAYCE and cancelled. Upon completion of the Buy-Back and subsequent cancellation of Ordinary Shares, the total issued capital of PAYCE may be substantially reduced by up to 33 per cent. The cancellation of Ordinary Shares under the Buy-Back, combined with the potential for a significant concentration of ownership of the remaining Ordinary Shares, may reduce the liquidity of those remaining Ordinary Shares, especially if there is a high level of participation in the Buy-Back.

**(f) What are the general tax implications for PAYCE?**

It is unlikely that the Buy-Back will result in any adverse income tax implications for PAYCE.

The Buy-Back may impact upon PAYCE's ability to utilise prior year tax losses against future taxable income of PAYCE.

**(g) PAYCE's intentions following the Buy-Back**

After the Buy-Back, PAYCE intends to continue with its principal activity of undertaking property development projects.

**(h) ASX Spread Requirement**

Under ASX Listing Rule 12.4.1, PAYCE must maintain a spread (that is, dispersion) of Shareholders which, in the opinion of the ASX, is sufficient to ensure that there is an orderly and liquid market in its securities.

As noted above, the Buy-Back may have the effect of concentrating the ownership of Ordinary Shares following the implementation of the Buy-Back. The Directors are of the opinion that the Buy-Back Limit and the Scale Back will ensure that despite any ownership concentration, PAYCE will continue to satisfy the ASX spread requirements. However, there is a risk that if a very high concentration of ownership results from the Buy-Back, ASX may determine that PAYCE does not have a sufficient spread of Shareholders.

The effect of Listing Rule 12.4.1 is that if the ASX determines that PAYCE does not have a sufficient spread of Shareholders, it may require PAYCE to do the following:

- obtain the required spread within 3 months after the date the ASX requires it to do so; and
- inform all Shareholders in writing that if the required spread is not obtained within 3 months, the ASX may suspend quotation of Ordinary Shares.

PAYCE will take all steps necessary to meet the ASX requirements to remain listed, including if necessary, raising additional capital and expanding its shareholder base.

## **2.4 OTHER ALTERNATIVES CONSIDERED BY THE DIRECTORS**

The Directors have considered a variety of capital management strategies which may offer Shareholders liquidity in an otherwise illiquid stock, and maintain PAYCE's financial position and ability to maintain its business operations. As a result of these deliberations, the Directors have determined that the proposed Buy-Back is the most appropriate available option as it provides existing Shareholders with the opportunity to restructure their current investment in PAYCE by participating in the Buy-Back, and receiving:

- a cash payment; and
- discretionary quarterly dividends,

in circumstances where the equity market for Ordinary Shares has historically been illiquid.

The other alternatives considered included a proposal to Buy-Back Shares and issue subordinated unsecured notes. On 14 October 2014, PAYCE issued an ASX Announcement advising that it was seeking amendment to the conditions of secured corporate notes that it had on issue in order to allow for the issue of the proposed subordinated unsecured notes.

As announced to ASX on 31 October 2014, these proposed amendments were not approved by the noteholders.

As a result, PAYCE is limited in terms of the capital management alternatives available at this time.

### 3. ADVANTAGES AND DISADVANTAGES OF THE BUY-BACK FOR SHAREHOLDERS

#### 3.1 INTRODUCTION

The Independent Directors believe that it is in the best interests of Shareholders for the proposed Buy-Back to be put to Shareholders for approval. Although not required by the Corporations Act, Brian Boyd, PAYCE's Managing Director, has voluntarily refrained from voting on the Directors' decision to put forward the Buy-Back proposal to Shareholders, in light of his association with PAYCE's largest Shareholder.

The balance Directors, who are independent, have established an independent Board Committee to consider the Buy-Back proposal, and identified the following advantages and disadvantages of the Buy-Back for Shareholders.

In recognition of the potentially differing objectives of Shareholders, the advantages and the disadvantages are addressed as follows:

- (a) advantages of the Buy-Back for Shareholders who sell their Ordinary Shares;
- (b) disadvantages of the Buy-Back for Shareholders who sell their Ordinary Shares;
- (c) advantages of the Buy-Back for Shareholders who retain their Ordinary Shares; and
- (d) disadvantages of the Buy-Back for Shareholders who retain their Ordinary Shares.

The Independent Directors consider that the Buy-Back is the most appropriate option for PAYCE and its Shareholders given the different objectives of Shareholders. Accordingly, the Independent Directors recommend that Shareholders **vote in favour** of the Buy-Back resolution.

#### 3.2 ADVANTAGES OF THE BUY-BACK FOR SHAREHOLDERS WHO SELL THEIR ORDINARY SHARES

##### (a) Premium to fair market value of Ordinary Shares

The independent Board Committee engaged Hanrick Curran Corporate Finance Pty Ltd to prepare an Independent Expert's Report to opine on whether the Buy-Back proposal is fair and reasonable to those Shareholders of PAYCE not associated with Managing Director, Mr Brian Boyd. The Independent Expert's Report is annexed to this Explanatory Statement.

In assessing whether the Buy-Back proposal is fair and reasonable to Non Associated Shareholders, the Independent Expert considered the advantages and disadvantages of the Buy-Back from the perspective of Non Associated Shareholders.

In considering the advantages and disadvantages of the Buy-Back, the Independent Expert compared the consideration being paid for the Ordinary Shares with its estimate of the fair market value of the Ordinary Shares to be bought back.

In its Report, the Independent Expert has assessed the value of the consideration being offered under the Buy-Back as equivalent to \$9.40 per Ordinary Share. This may alter depending on the level of acceptances in the Buy-Back. If 70% or less of eligible Ordinary Shares accept into the Buy-Back, all accepting Ordinary Shares will receive value of \$9.40 per Ordinary Share. If 100% of eligible Ordinary Shares accept into the Buy-Back, each accepting Ordinary Share will receive \$8.16 per Ordinary Share in value. Depending on the level of acceptances, the total value for Shareholders accepting the Buy-Back will be equivalent to between \$8.16 and \$9.40 per Ordinary Share.

The Independent Expert has assessed the fair market value of a PAYCE Ordinary Share, on a control basis, to be \$7.57. 'Fair market value' is defined as the amount at which the Ordinary Shares would change hands between a knowledgeable willing buyer and a knowledgeable willing seller, neither being under a compulsion to buy or sell. This valuation assumes a hypothetical 'change in control' transaction – that is, where a person (in PAYCE's case, the Managing Director Mr Brian Boyd and his associates), increase their shareholding in PAYCE.

The value of the consideration being offered under the Buy-Back, which the Independent Expert has assessed as equivalent to \$9.40 per Ordinary Share, is greater than the assessed fair market value of the Ordinary Shares prior to the Buy-Back of \$7.57 per Ordinary Share.

The Independent Expert concludes that the Buy-Back is both fair and reasonable to participating Non Associated Shareholders.

Further details are contained in the annexed Independent Expert's Report which Shareholders should read in its entirety.

Given the historical illiquidity of the Ordinary Shares, there is no guarantee that Shareholders could achieve such a return on-market if the Buy-Back does not proceed.

**(b) Independent Expert concludes the Buy-Back is fair and reasonable to Non Associated Shareholders**

The Independent Expert has concluded that the value of the consideration being offered under the Buy-Back, which the Independent Expert has assessed as equivalent to \$9.40 per Ordinary Share, is greater than the value of the Ordinary Shares on a controlling basis prior to the Buy-Back of \$7.57 per Ordinary Share.

Accordingly, the Independent Expert is of the view that, the Buy-Back is fair and reasonable to participating Non Associated Shareholders.

**(c) Premium to market price**

The value of the Buy-Back consideration is a premium compared to the recent share trading price of Ordinary Shares. The PAYCE 45 Day VWAP as at 20 February 2015 was \$5.54, compared to the value of the consideration being offered under the Buy-Back, which the Independent Expert has assessed as equivalent to \$9.40 per Ordinary Share.

**(d) Opportunity to exit in an efficient manner**

Historically, PAYCE's Ordinary Shares have been thinly traded on the ASX. The Buy-Back provides Shareholders with an opportunity to sell their Ordinary Shares in an efficient and cost effective manner, in consideration for a combination of a cash payment and Preference Shares which carry a discretionary Dividend.

In addition, the Buy-Back allows Shareholders to sell a relatively large volume of Ordinary Shares without depressing the market price of Ordinary Shares, and in circumstances where the market for the Ordinary Shares may not otherwise be sufficiently liquid to accommodate such volume.

There is no guarantee that Shareholders could dispose of their current investment in an efficient manner if the Buy-Back does not proceed.

**(e) No brokerage or other selling costs**

Shareholders do not pay brokerage or selling costs under the Buy-Back. In contrast, Ordinary Shares sold on market may attract brokerage and/or other selling costs.

**(f) Discretionary dividends**

By participating in the Buy-Back, Shareholders may, at the discretion of PAYCE, receive a quarterly dividend on their Preference Shares which is paid by either cash, a further issue of Preference Shares, or a combination of cash and Preference Shares.

**(g) Priority in Dividends and Capital Returns**

Shareholders who participate in the Buy-Back will receive Preference Shares as partial consideration. Preference Shares receive priority in the receipt of dividends and the return of capital in the event of windup over Shareholders.

### **3.3 DISADVANTAGES OF THE BUY-BACK FOR SHAREHOLDERS WHO SELL THEIR ORDINARY SHARES**

**(a) Loss of potential benefits**

Shareholders who sell their Ordinary Shares under the Buy-Back will forego, to the extent they sell down their shareholding, any benefits of remaining a holder of Ordinary Shares.

This includes, for example, the right to vote on resolutions considered by members at general meeting.

**(b) Limited voting rights**

Shareholders who sell their Ordinary Shares under the Buy-Back will receive a combination of cash and Preference Shares in return. However, the voting rights attached to the Preference Shares are more limited than the voting rights of Ordinary Shares. Holders of Preference Shares are only able to vote on resolutions which relate to the following:

- (i) on a proposal:
  - (A) to reduce the share capital of PAYCE;
  - (B) that affects rights attached to the Preference Share;
  - (C) to wind up PAYCE; or
  - (D) for the disposal of the whole of the property, business and undertaking of PAYCE;
- (ii) on a resolution to approve the terms of a buy-back agreement;
- (iii) during a period in which a Dividend or part of a Dividend on the Preference Share is in arrears; or
- (iv) during the winding up of PAYCE.

**(c) Potential increase in voting power of major Shareholders**

If a significant number of Shareholders choose to participate in the Buy-Back, their Ordinary Shares will be cancelled, and the shareholding interests of the remaining holders of Ordinary Shares will increase. As outlined in Section 2.3(e), those Shareholders whose retain their Ordinary Shares will therefore have greater voting power on future resolutions which are put to Shareholders.

**(d) Preference Shares received as partial consideration with no public market for resale**

Shareholders who sell their Ordinary Shares under the Buy-Back will receive a Preference Share as the primary portion of their consideration. Whilst transferable, these Preference Shares are likely to be illiquid as they will be unlisted securities with no public market available for resale.

**(e) Dividends on Preference Shares are payable only if so declared at the discretion of PAYCE**

Whilst the Preference Shares offer a fixed rate of return in the form of Dividends, the declaration and payment of these Dividends on the scheduled Dividend Payment Dates remains at the discretion of PAYCE.

- (f) **Dividends on Preference Shares may be paid via the issuance of additional Preference Shares**

When a Dividend is declared as payable on the Preference Shares, PAYCE has the discretion of paying the Dividend through the issue of additional Preference Shares rather than a cash payment.

- (g) **Limit on participation**

Because of the limit on the number of Ordinary Shares which are able to participate in the Buy-Back, there is a risk that the Buy-Back will be oversubscribed and that up to 30% of Ordinary Shares which are accepted into the Buy-Back by each Non Associated Shareholder will not be bought back by PAYCE. This would result in Non Associated Shareholders retaining up to 30% of their Ordinary Shares in PAYCE, which may not necessarily be their desired outcome.

### **3.4 ADVANTAGES OF THE BUY-BACK FOR SHAREHOLDERS WHO RETAIN THEIR ORDINARY SHARES**

- (a) **Flexibility**

Implementation of the Buy-Back does not prevent a Shareholder from deciding in the future that they would like to sell their Ordinary Shares in PAYCE (although the liquidity and market value of Ordinary Shares may be reduced).

- (b) **Increase in voting power**

The cancellation of Ordinary Shares bought back under the Buy-Back will have the effect of increasing the percentage shareholding, and voting power, of Shareholders who do not participate in the Buy-Back. The extent of the increase will depend on the number of Ordinary Shares bought back and cancelled under the Buy-Back.

- (c) **Increase in Earnings Per Ordinary Share (EPS)**

Subject to the level of future profits earned by PAYCE, Shareholders who retain their Ordinary Shares may derive a higher EPS, depending on the level of Ordinary Shares bought back under the Buy-Back.

### **3.5 DISADVANTAGES OF THE BUY-BACK FOR SHAREHOLDERS WHO RETAIN THEIR ORDINARY SHARES**

- (a) **Reduction in cash**

There will be a reduction in the overall cash held by PAYCE following implementation of the Buy-Back, as the consideration for each Ordinary Share will comprise \$2.30 cash (\$0.80 payable on cancellation of the Ordinary Shares, \$0.80 payable 12 months after cancellation and a further \$0.70 payable 18 months after cancellation of the Ordinary



Shares) and Preference Shares issued at \$7.50. The amount of the cash reduction will depend on the level of Shareholder participation in the Buy-Back and the number of Ordinary Shares bought back.

**(b) Potential impact on liquidity**

A reduction in PAYCE's capital base following implementation of the Buy-Back and the potential for additional Ordinary Share ownership concentration in the event that large Shareholders elect not to participate in the Buy-Back may materially adversely affect the trading liquidity in the Ordinary Shares following the implementation of the Buy-Back. This in turn may adversely affect the trading price of the Ordinary Shares.

**(c) Subordination of dividends**

Under the terms of issue for the Preference Shares, PAYCE is prohibited from paying dividends or making any other distribution on any other class of shares (including Ordinary Shares), unless and until holders of Preference Shares have had their dividend entitlements paid, or those Preference Shares have been purchased or bought back by PAYCE.

**(d) Ranking in return of capital**

In the event of a winding-up of PAYCE, Shareholders will rank after holders of Preference Shares in respect of participating in the return of any capital.

## 4. INDEPENDENT DIRECTORS' COMMENTARY REGARDING THE BUY-BACK

### 4.1 INDEPENDENT DIRECTORS

An independent Board Committee was established by PAYCE to consider the Independent Expert's Report and the Buy-Back proposal; the committee did not include Mr Boyd, who is associated with the largest Shareholder in PAYCE. This Section sets out the commentary of the Independent Directors regarding the Buy-Back.

ASIC Regulatory Guide 110 recommends that a commentary of this nature be provided by the Independent Directors of a company undertaking a significant share buy-back.

### 4.2 RECOMMENDATION TO VOTE IN FAVOUR

The Independent Directors consider that the Buy-Back is an appropriate option for PAYCE and its Shareholders, which responds to the different objectives of Shareholders. Accordingly, the Independent Directors **recommend that Shareholders vote in favour of the Buy-Back Resolution**. This recommendation has been made by the Independent Directors having regard to the advantages and disadvantages associated with the Buy-Back.

Although the Independent Directors recommend that Shareholders vote in favour of and approve the Buy-Back Resolution, they make no recommendation to Shareholders as to whether they should accept the Offer to buy-back their Ordinary Shares. Such a decision is a matter for each Shareholder to determine having regard to their own individual circumstances and if appropriate or required, after taking into account professional and financial advice and the contents of this Explanatory Statement.

The Independent Directors also wish to provide the following commentary and guidance regarding the Buy-Back for consideration by Shareholders.

### 4.3 CONSIDERATIONS

The Independent Directors believe that Shareholders should have regard to the following matters:

(a) **advantages of the Buy-Back:**

- (i) opportunity for Shareholders who are seeking to realise their current investment in a relatively illiquid stock, to restructure their investment in Ordinary Shares in PAYCE and receive a cash payment and a discretionary fixed dividend on Preference Shares;
- (ii) no selling costs associated with the Buy-Back; and
- (iii) priority in ranking to Ordinary Shares in return of capital and dividends;

(b) **disadvantages of the Buy-Back:**

- (i) potential for relative increase in shareholding by PAYCE's largest Shareholder, Lanox Pty Ltd, who has indicated it will be retaining its shareholding and not participating in the Buy-Back; and
- (ii) as a result of participating in the Buy-Back, Shareholders could receive a combination of cash and Preference Shares which carry limited voting rights; and
- (iii) no recognised secondary market for the future sale of Preference Shares.

(c) **other factors:**

- (i) decrease in number of Ordinary Shares on issue and potential impact on future liquidity;
- (ii) tax liability for Shareholders; and
- (iii) anticipated ongoing illiquidity in share price of Ordinary Shares in the absence of the proposed Buy-Back.

#### 4.4 THE BUY-BACK

(a) **Introduction**

The Independent Directors believe that the Buy-Back provides a means to appropriately address the differing investment objectives of PAYCE's Shareholder base, by providing the opportunity for the following outcomes:

- **Retain Ordinary Shares and provide other Shareholders with the opportunity to participate in the Buy-Back:** Those Shareholders who wish to retain their Ordinary Shares in PAYCE can consider voting in favour of the Buy-Back to authorise the implementation of a Buy-Back to provide other Shareholders with different investment objectives an opportunity to sell down their current investment in PAYCE.
- **Realise and restructure current investment in PAYCE:** Those Shareholders who wish to sell their Ordinary Shares in PAYCE, can consider voting in favour of the Buy-Back and, if the Buy-Back Resolution is approved at the Extraordinary General Meeting, participate in the Buy-Back. The Buy-Back provides a means for Shareholders to realise their current investment without incurring selling costs, in return for a combination of cash and Preference Shares.
- **Rebalance:** Those Shareholders who wish to rebalance their holding of Ordinary Shares by realising some but not all of their current investment, can consider voting in favour of the Buy-Back and, if the Buy-Back Resolution is approved at the Extraordinary General Meeting, participate in the Buy-Back for some (but not all) of their Ordinary Shares.

Considering each of these possibilities in turn:

**(b) The Buy-Back and Shareholders who wish to retain their Ordinary Shares:**

Shareholders who continue to hold their Ordinary Shares following the implementation of the Buy-Back may have the potential to:

- subject to the level of future profits earned by PAYCE, derive a higher EPS, depending on the level of Ordinary Shares bought back under the Buy-Back; and
- increase their percentage holding of Ordinary Shares and voting power in PAYCE.

Taking into account these considerations, the Independent Directors therefore believe that the Buy-Back may be more acceptable to those Shareholders who are willing to accept the advantages and disadvantages associated with remaining a Shareholder following implementation of the Buy-Back as set out in Section 3, and the risks of such a strategy as summarised in Section 5.

For such Shareholders, the Independent Directors recommend that they vote in favour of the Resolution, and consider not participating (or at least, not participating in full) in the Buy-Back.

**(c) The Buy-Back and Shareholders who wish to realise and restructure their current investment in PAYCE:**

The Independent Directors acknowledge that there are also Shareholders who are seeking to realise their investment in PAYCE. The Buy-Back offers these Shareholders the opportunity to restructure their current investment for consideration which combines a cash payment as well as scheduled (but discretionary) quarterly dividends on Preference Shares paid by either cash, Preference Shares, or a combination of cash and Preference Shares, at the discretion of PAYCE.

The Buy-Back provides these Shareholders with an opportunity to realise their current investment in Ordinary Shares in exchange for combined cash/Preference Share consideration, in circumstances where liquidity in Ordinary Shares has been limited in the past.

Accordingly, for those Shareholders who do not wish to accept the risk and uncertainties of remaining a holder of Ordinary Shares in PAYCE, and agree that the consideration of combined cash and / or Preference Shares carrying discretionary quarterly dividends is fair and reasonable, the Independent Directors recommend that those Shareholders vote in favour of the Resolution and consider participating in the Buy-Back.

(d) The Buy-Back and Shareholders who wish to rebalance their investment:

The Independent Directors also understand that some Shareholders may wish to realise a proportion of their Ordinary Shares in PAYCE, as well as retain some of their holding of Ordinary Shares. The Buy-Back would enable these Shareholders to restructure part of their current investment in PAYCE.

The Independent Directors recommend that such Shareholders vote in favour of the Resolution, and consider participating in the Buy-Back for some, but not all, of their Ordinary Shares.

## **5. RISKS**

### **5.1 INTRODUCTION**

This section describes the material risks in relation to the Buy-Back. Individually or in combination, these risks may adversely affect the future financial position, performance or prospects of PAYCE.

A number of these risks are risks to which Shareholders already have some exposure.

Additional risks and uncertainties not currently known to PAYCE, or which PAYCE currently considers to be immaterial, may also have an adverse effect on the future financial position, performance or prospects of PAYCE or the value of an investment in PAYCE. The information set out below does not purport to be, nor should it be construed as representing, an exhaustive summary of all possible risks.

Shareholders should also take into account the advantages and disadvantages associated with the Buy-Back set out in Section 3 when considering what action they should take in relation to the Buy-Back.

### **5.2 RISKS SPECIFIC TO THE BUY-BACK**

#### **(a) Liquidity Risk – Ordinary Shares**

Section 3 describes the factors which may materially adversely affect the trading liquidity in the Ordinary Shares following the implementation of the Buy-Back. A material adverse effect on liquidity in the Ordinary Shares may in turn adversely affect the trading prices of the Ordinary Shares.

#### **(b) Subordination of dividends**

Under the terms of issue for the Preference Shares, PAYCE is prohibited from paying dividends or making any other distribution on any other class of shares (including Ordinary Shares), unless and until holders of Preference Shares have had their proposed Dividend entitlements paid, or those Preference Shares have been purchased or bought back by PAYCE.

#### **(c) Ranking in return of capital**

In the event of a winding-up of PAYCE, Shareholders will rank after holders of Preference Shares in respect of participating in the return of any capital.

#### **(d) Limit on ability to participate**

The Buy-Back is limited to a maximum of 9,915,075 Ordinary Shares, which equates to one-third of all issued Ordinary Shares. If PAYCE receives acceptances for more than 9,915,075 Ordinary Shares, all acceptances will be Scaled Back.

### 5.3 GENERAL RISKS

Shareholders should also note the following general risks that are associated with an investment in a listed company such as PAYCE. Both holders of Ordinary Shares and holders of Preference Shares may be exposed to these risks:

**(a) Dependence on general economic conditions**

Changes in Australian and international economic conditions may adversely affect PAYCE's financial performance, financial position or prospects, or the value or price of Ordinary Shares. Amongst other things, these general conditions may impact on the availability of new investment opportunities, the availability, terms and costs of funding and PAYCE's operating costs.

**(b) Share market conditions**

There are risks associated with an investment in shares (such as Ordinary Shares in PAYCE) that are listed on a stock exchange. Share price movements can affect the value of an investment in PAYCE. The value of listed shares can be expected to fluctuate depending upon a number of general factors including changes in international and local share markets, changes in the economic conditions, inflation, interest rates, government fiscal, monetary and regulatory policies and investor perceptions. These risk factors are unpredictable and may have implications for the price or value of shares that are unrelated or disproportionate to the operating performance of PAYCE.

**(c) Governmental or regulatory actions**

PAYCE's operations could be affected by government actions. The possible extent of introduction of additional legislation, regulations, standards (including accounting standards), guidelines or amendments to existing legislation that might affect PAYCE's business is difficult to predict.

Any such government action may require increased capital or operating expenditures and could prevent or delay the execution of PAYCE's plans or have a material adverse effect on PAYCE's business and financial condition.

**(d) Taxation**

PAYCE and its group entities are and will be subject to taxation and other imposts in Australia. Future changes in taxation laws, including changes in interpretation or application of existing laws by the courts or taxation authorities, may affect the tax liabilities of PAYCE or its group companies, or the taxation treatment of holding or disposing of Ordinary Shares and Preference Shares.

(e) Disputes and litigation

Disputes or litigation may arise from time to time in the course of PAYCE's business activities. There is a risk that material or costly disputes or litigation which PAYCE may become party to or be required to assist with could adversely affect financial performance. PAYCE has insurance to cover certain risks where it appears appropriate to PAYCE to do so. To the extent that any such claims are not covered by insurance, the costs of responding to the claim and any adverse outcome from any claim may materially adversely affect PAYCE's financial position.



## **6. TERMS ON WHICH THE BUY-BACK WILL BE UNDERTAKEN**

### **6.1 INTRODUCTION**

The Buy-Back will only proceed if both Resolutions are approved by Shareholders at the Extraordinary General Meeting. If both Resolutions are approved, PAYCE will undertake the Buy-Back following the Extraordinary General Meeting on the basis described in this Section 6.

### **6.2 OFFER**

This document summarises the offer to Eligible Shareholders to participate in the Buy-Back on the basis set out in this Section 6 (Offer).

### **6.3 BUY-BACK PROCESS**

- (a) If both Resolutions are approved, PAYCE will be able to proceed with the Buy-Back.
- (b) Subject to Shareholder approval of the Resolutions being obtained, personalised Application & Acceptance Forms will be despatched together with an Offer Document to Eligible Shareholders following the Buy-Back Record Date of 11 May 2015.
- (c) The Buy-Back period will commence on 12 May 2015, and remain open until 1 June 2015.
- (d) Eligible Shareholders may accept the Offer in respect of some or all of their Ordinary Shares on and from 12 May 2015 (Opening Date), by completing and returning the Application & Acceptance Form attached to the Offer Document in accordance with the instructions on that form.
- (e) Eligible Shareholders will have until the Closing Date (1 June 2015) to accept the Offer in respect of some or all of their Ordinary Shares.

### **6.4 SHAREHOLDERS WHO WILL BE ENTITLED TO PARTICIPATE IN THE BUY-BACK**

Shareholders who are listed on the Register on the Buy-Back Record Date (being 7.00pm on 11 May 2015) will be eligible to participate in the Buy-Back. Shareholders entitled to participate in the Buy-Back are referred to as Eligible Shareholders.

Entitlement to participate in the Buy-Back will be personal. An Eligible Shareholder will not be able to transfer their right to participate in the Buy-Back.

### **6.5 PARTICIPATION IS NOT COMPULSORY**

Participation in the Buy-Back will be optional. If an Eligible Shareholder does not wish to participate, they will not need to do anything.

Shareholders who do not participate in the Buy-Back will continue to hold their Ordinary Shares. Shareholders who do not believe they will participate in the Buy-Back should carefully consider

the considerations relevant to, and the risks associated with, remaining a Shareholder in these circumstances.

## **6.6 SHARES THAT MAY BE ACCEPTED INTO THE BUY-BACK**

An Eligible Shareholder may accept the Offer in respect of some or all of the Ordinary Shares held by them on the Buy-Back Record Date, provided that at 7.00pm (Sydney time) on the Closing Date (being 1 June 2015), they hold at least as many Ordinary Shares as they accept into the Offer.

Ordinary Shares acquired on or after the Ex-Entitlement Date (being 7 May 2015) will not be registered in your name by the Buy-Back Record Date (being 11 May 2015) and therefore will not carry an entitlement to participate in the Buy-Back.

If an Eligible Shareholder purports to accept the Offer in respect of more Ordinary Shares than they are the registered holder of at the Buy-Back Record Date, PAYCE may, in its absolute discretion and without prejudice to its other rights or remedies, reject the acceptance or treat the acceptance as relating to the maximum number of Ordinary Shares the Eligible Shareholder is the registered holder of on the Buy-Back Record Date.

Shareholders should note that it will be a term of the Buy-Back that they warrant to PAYCE that:

- any of their Ordinary Shares accepted into the Offer will, at the date of the transfer to PAYCE, be fully paid and free from all mortgages, charges, liens, encumbrances and interests of third parties of any kind, including any restrictions on transfer;
- they have full power and capacity to sell and transfer their Ordinary Shares to PAYCE; and
- they are a person who may lawfully participate in the Buy-Back.

Please see Section 6.10 for further details.

## **6.7 CONSIDERATION FOR THE BUY-BACK**

The consideration which PAYCE will pay for each Ordinary Share bought back will be:

- \$0.80 cash paid upon cancellation of the Ordinary Shares;
- \$0.80 cash paid 12 months after the cancellation of the Ordinary Shares;
- \$0.70 cash paid 18 months after the cancellation of the Ordinary Shares; and
- one Preference Share issued at \$7.50 (refer Section 2.2 for further details).

## 6.8 MAXIMUM LIMIT OF THE BUY-BACK

The maximum number of Ordinary Shares which can be bought back in the Buy-Back is 9,915,075 Ordinary Shares.

## 6.9 BUY-BACK OFFER PERIOD

The Buy-Back Offer Period is currently scheduled to open on the Opening Date of 12 May 2015.

Shareholders may accept the Offer at any time from that date until 7.00pm on the Closing Date. PAYCE may reschedule, withdraw or extend the Buy-Back Offer Period, but does not currently plan to. If the Closing Date is changed, the change will be announced to the ASX.

You will be taken to have submitted your acceptance when the Registry receives your validly signed and completed Application & Acceptance Form. If you have an issuer sponsored holding or, if you have a CHESS Holding, your acceptance is processed by your controlling participant through CHESS.

## 6.10 THE EFFECT OF ACCEPTING THE OFFER

The Application & Acceptance Form will contain detailed instructions for how to accept the Offer.

The effect of participating in the Buy-Back is that you will accept the Offer to sell your Ordinary Shares on the terms and conditions set out below.

An Eligible Shareholder who submits an Application & Acceptance Form will be agreeing to sell to PAYCE the number of Ordinary Shares nominated in the Application & Acceptance Form, or such lesser number of Ordinary Shares as may result from the application of any Scale Back, on the following basis:

- (a) the consideration which PAYCE will pay for each Ordinary Share bought back will be:
  - \$0.80 cash paid upon cancellation of the Ordinary Shares;
  - \$0.80 paid 12 months after the cancellation of the Ordinary Shares;
  - \$0.70 paid 18 months after the cancellation of the Ordinary Shares; and
  - one Preference Share issued at \$7.50.
- (b) on the basis that both Resolutions are approved at the Meeting, a contract to buy-back your Ordinary Shares will be formed upon the Board receiving your Application & Acceptance Form and posting an announcement on its website, and the purchase of the relevant Ordinary Shares is taken to occur at that point (the date being referred to as the Buy-Back Date);
- (c) PAYCE posting an announcement on the ASX website is an effective communication by PAYCE of the agreement to buy-back your Ordinary Shares;

- (d) you waive any requirement to receive further notice or communication from PAYCE of the agreement to buy-back your Ordinary Shares;
- (e) you warrant to PAYCE that:
  - (i) you are the registered holder of the Ordinary Shares and that all your Ordinary Shares (including any rights and entitlements attaching to those Ordinary Shares) that are transferred to PAYCE under the Buy-Back will, at the date of the transfer of them to PAYCE, be fully paid and free from all mortgages, charges, liens, encumbrances and interests of third parties of any kind, whether legal or otherwise, and restrictions on transfer of any kind;
  - (ii) you have full power and capacity to sell and to transfer the Ordinary Shares together with all rights attaching to such Ordinary Shares; and
  - (iii) you are a person to whom the Offer may lawfully be made, can receive the proceeds of the sale of your Ordinary Shares and whose participation in the Buy-Back is permitted under the laws of the jurisdiction in which you are resident;
- (f) you authorise PAYCE (and its officers, agents, contractors and advisers) to correct any error in or omission from your Application & Acceptance Form, and to insert any missing details;
- (g) you undertake not to sell or offer to sell Ordinary Shares to any other person if, as a result, you will at any time after you submit your Application & Acceptance Form until the Buy-Back Date hold fewer Ordinary Shares than the number of Ordinary Shares you have accepted into the Buy-Back;
- (h) you authorise PAYCE to procure the number of Ordinary Shares accepted into the Buy-Back to be transferred to a subposition on the Register which will prevent them from being dealt with following receipt of your Application & Acceptance Form otherwise than in accordance with the Buy-Back;
- (i) you acknowledge that neither PAYCE nor any other party involved in the Buy-Back has provided you with financial product advice, or any securities recommendation, or has any obligation to provide this advice or recommendation, concerning your decision to participate in the Buy-Back;
- (j) you accept the responsibility for fully observing the laws and regulatory requirements of the relevant jurisdiction that applies to you in connection with this Buy-Back, including the obtaining of any governmental, exchange control or other consents, the making of any filings that may be required, the compliance with other necessary formalities and the payment of any taxes or other requisite payments due in such jurisdiction;
- (k) you recognise damages are not an adequate remedy for breach of these covenants, undertakings, agreements, representations and warranties;

- (l) you undertake that if you breach any of these covenants, undertakings, agreements, representations or warranties you will indemnify PAYCE for all its costs or losses arising from the breach; and
- (m) any obligation of PAYCE to buy-back Ordinary Shares from you is conditional on your compliance with the covenants, undertakings, agreements, representations and warranties listed above.

Dispatch of cheques or electronic funds transfer is expected to be completed within five Business Days after the announcement of the outcome of the Buy-Back.

## **6.11 WITHDRAWING OR AMENDING ACCEPTANCES**

Set out below are the procedures for withdrawing or amending your acceptance. The effect of withdrawing or amending one or more of your acceptances will be to withdraw those acceptances, and, in the case of an amendment, to replace the relevant acceptances with new acceptances.

Withdrawals or amendments made in accordance with these procedures may not take immediate effect. You should take this into account if you wish to sell any Ordinary Shares which you have accepted into the Buy-Back.

### **(a) Issuer sponsored holdings**

To withdraw or amend an acceptance that has been received by the Registry, you will need to complete and submit a Withdrawal/Amendment Form, using the procedures set out on the back of the Withdrawal/Amendment Form.

You will need to submit your form to the address noted on the form, so that it is received by no later than 7.00pm (Sydney time) on the Closing Date. Any forms received after this time will not be effective for withdrawing or amending your acceptance.

A copy of the Withdrawal/Amendment Form is available by telephoning the Registry on 1300 737 760 (within Australia) or +61 1300 737 760 (outside Australia).

### **(b) CHESS Holdings**

If you have a CHESS Holding, you will need to instruct your controlling participant in sufficient time for them to process your withdrawal or amendment by 7.00pm (Sydney time) on the Closing Date.

If you have a CHESS Holding, you should NOT send a Withdrawal/Amendment Form to the Registry.

After your controlling participant has withdrawn or amended your acceptance, you will be sent written confirmation from CHESS of the withdrawal/amendment made in relation to your holding by your controlling participant. Irrespective of its wording, this

confirmation is not an acceptance by PAYCE of the withdrawal or amendment of your acceptance.

## **6.12 RESTRICTION ON TRADING ACCEPTED ORDINARY SHARES**

Ordinary Shares accepted into the Buy-Back at any time during the Buy-Back Offer Period must not be sold or otherwise transferred to any other person unless they have first been withdrawn from the Buy-Back pursuant to a withdrawal or amendment made in accordance with the procedures described above.

The number of Ordinary Shares in respect of which an Eligible Shareholder accepts the Offer will be removed from their holding and placed in a "subposition" in the Register. The Eligible Shareholder will not be able to deal with those Ordinary Shares until they have been released from the subposition. For the Ordinary Shares to be released from that subposition, the Eligible Shareholder must withdraw or amend their acceptance in accordance with the procedures described above.

If an Eligible Shareholder sells Ordinary Shares after submitting an acceptance such that at the Buy-Back Date they do not hold at least the number of Ordinary Shares they successfully accepted into the Buy-Back, PAYCE may, in its absolute discretion and without prejudice to its other rights and remedies, reject their acceptance in its entirety or treat the acceptance as if they had accepted the Offer in respect of the number of Ordinary Shares held by them at 7.00pm on the Closing Date.

## **6.13 PAYCE'S RIGHT TO VARY DATES AND TIMES**

While PAYCE does not presently anticipate changing any of the dates and times in relation to the Buy-Back (including the Closing Date and the Buy-Back Date), it reserves the right to vary them where lawful to do so.

Any change in date or time will take effect from the time it is authorised by the Directors and will be publicly announced on the ASX as soon as practicable following the Directors' authorisation. Any such change will be taken to amend this document (and the Application & Acceptance Form and/or Withdrawal/Amendment Form) accordingly.

PAYCE may also decide not to proceed with the Buy-Back. Without limitation, PAYCE reserves the right to terminate the Buy-Back at any time prior to the date on which PAYCE enters into the contracts to buy-back its Ordinary Shares, by making an announcement to the ASX to that effect.

## **6.14 PAYCE'S RIGHT TO ADJUST OR REJECT ACCEPTANCES**

PAYCE may, in its absolute discretion and at any time, deem any acceptance it receives to be a valid acceptance, disregard or not accept any acceptance and may waive any or all of the requirements for making, amending or withdrawing an acceptance, provided that it does so in compliance with the relevant provisions of the Corporations Act 2001 (Cth) (including the equal

access share buy-back provisions) and the ASX Listing Rules. It may do each of these things in relation to some, all or any number of acceptances it receives.

#### **6.15 CANCELLATION OF ORDINARY SHARES ACCEPTED AT THE BUY-BACK**

In accordance with the Corporations Act, all Ordinary Shares bought back under the Buy-Back will be cancelled.

#### **6.16 GOVERNING LAW**

This document is governed by the law in force in New South Wales.

## **7. AUSTRALIAN TAXATION IMPLICATIONS FOR SHAREHOLDERS**

### **7.1 INTRODUCTION**

This Section 7 contains a summary of the potential Australian taxation implications of the Buy-Back for Shareholders that hold Ordinary Shares on capital account.

The tax implications for Shareholders arising from the Buy-Back will vary depending on a Shareholder's particular circumstances.

The information set out below is provided by way of a general guide, and should not be regarded as tax advice in relation to the specific circumstances of Shareholders. The information provided does not represent a complete analysis of all potential tax implications associated with the Buy-Back.

Shareholders should consult their own tax advisors in relation to the potential taxation consequences relevant to their particular circumstances.

### **7.2 INCOME TAX CONSEQUENCES OF THE BUY-BACK FOR AUSTRALIAN RESIDENT SHAREHOLDERS**

Australian Resident Shareholders participating in the Buy-Back will be entitled to receive \$9.80 per Ordinary Share which will comprise a capital component of \$1.54 per Ordinary Share and a deemed unfranked dividend component of \$8.26 per Ordinary Share. As the Buy-Back amount will be applied to the issue of the respective Preference Shares, all income derived from the Buy-Back will be reflected in the 30 June 2015 financial year (see comments below).

To the extent that the market price of the Ordinary Shares (calculated in accordance with the Australian Taxation Office Guidelines) exceeds the \$9.80 per Ordinary Share, then an additional deemed capital component will be included in the income tax returns of the respective participating shareholders. PAYCE will provide all participating Shareholders with details to assist with the preparation of their respective 2015 income tax returns.

Australian Resident Shareholders will make a capital gain where the amount of the capital component of the Buy-Back exceeds the cost base of their Ordinary Shares. Otherwise, they will make a capital loss where the amount of the Buy-Back is less than the reduced cost base of their Ordinary Shares.

Australian Resident Shareholders who have held their Ordinary Shares for at least 12 months prior to the sale (excluding the day of acquisition and the day of disposal) and are individuals, trustees of a trust, or a complying superannuation fund, may be eligible to apply a CGT discount to reduce the amount of the taxable capital gain. Individuals and trusts are entitled to a 50% CGT discount and complying superannuation funds are entitled to a 33⅓% CGT discount. Companies are not entitled to the CGT discount.

Australian Resident PAYCE Shareholders must include the unfranked dividend component of the Buy-Back in their assessable income in the income year of the Buy-Back.



Australian Resident Shareholders who have not supplied their Tax File Number ('TFN') to the Registry prior to the Closing Date for participating in the Buy-Back, will have TFN withholding tax of 49% deducted from the unfranked dividend component of the consideration as well as the interest income. The TFN withholding tax deducted will be remitted to the Australian Taxation Office. Australian Resident Shareholders that have had TFN withholding tax deducted will be able to claim a credit for the TFN withholding tax withheld in their corresponding Income Tax Returns.

### 7.3 INCOME TAX CONSEQUENCES OF THE BUY-BACK FOR NON-RESIDENT SHAREHOLDERS

Non-Resident Shareholders will have dividend withholding tax of 30% (subject to reduction under a Double Tax Agreement and depending on the residency of the shareholder) deducted from the unfranked dividend component of the dividend. The dividend withholding tax deducted will be remitted to the Australian Taxation Office. Non Resident Shareholders may be able to claim a credit for the dividend withholding tax withheld in their country of residence.

Non Resident Shareholders should obtain their own independent tax advice as to the broader tax implications of participating in the buy-back.

### 7.4 GST AND STAMP DUTY

GST and stamp duty will not be payable on the transfer and cancellation of Ordinary Shares following acceptance of Offers.

As detailed in section 7.2, the Buy-back price of \$9.80 includes a component of deemed unfranked dividends for taxation purposes (\$8.26 per Ordinary Share) no franking credits will be utilised in relation to the Buy-back. **Shareholders should seek independent taxation advice.** It is possible that some Shareholders may have an income tax liability that exceeds the cash component of the Buy-back price.

## 8. **RESOLUTION 2 – APPROVAL FOR THE ISSUE OF PREFERENCE SHARES**

### 8.1 BACKGROUND TO RESOLUTION 2

PAYCE is seeking approval to issue Preference Shares pursuant to section 254A(2) of the Corporations Act., so that they may form partial consideration for the Buy-Back proposed in Resolution 1.

Resolution 1 and Resolution 2 are interdependent, meaning that Shareholders must pass both Resolutions for the Buy-Back to proceed, and the Preference Shares to be issued.

### 8.2 INFORMATION REQUIRED UNDER SECTION 254A(2) OF THE CORPORATIONS ACT

Pursuant to and in accordance with section 254A(2) of the Corporation Act, the following information is provided in relation to the proposed issue of Preference Shares:

| Feature                                     | Details   |
|---|---|
| Repayment of capital                        | <ul style="list-style-type: none"><li>• The Preference Shares have no fixed maturity date.</li><li>• Holders of Preference Shares do not have the right to have those securities purchased or bought-back.</li><li>• Each holder of Preference Shares grants PAYCE an option to purchase or buy back those Preference Shares for a cash consideration of \$7.50 each on any Dividend Payment Date, subject to the requirements of the Corporations Act and Listing Rules.</li></ul>   |
| Participation in surplus assets and profits | The Preference Shares have no entitlement to share in any surplus assets or profits in the event of a winding up.   |
| Dividends                                   | <ul style="list-style-type: none"><li>• Cumulative Dividends of 6% per annum for the first 12 months, proposed to be paid quarterly, subject to such Dividends being declared at the discretion of PAYCE.</li><li>• On each yearly anniversary of the issue of the Preference Shares, the dividend rate will increase by an additional 1% per annum. For example:<ul style="list-style-type: none"><li>○ After one year from the date of issue, the dividend rate will increase to 7% per annum.</li><li>○ After two years from the date of issue, the dividend rate will increase to 8% per annum,</li></ul>and thereafter increasing by 1% per annum in each following yearly period), until the date which is six years from the date of issue of the Preference Shares, when the dividend rate increases to 12% per annum, at which time the dividend rate will be capped at 12% per annum.</li></ul> |

| Feature | Details   |
|---------|---|
|         | <ul style="list-style-type: none"> <li>• If PAYCE elects to pay a Dividend on the Preference Shares, it has the discretion to pay the Dividends by either cash, the issue of additional Preference Shares at \$7.50 each (plus any outstanding dividend entitlement in cash), or a combination of cash and Preference Shares.</li> <li>• If no Dividends are paid on the Preference Shares on the Dividend Payment Date, PAYCE is prohibited from paying dividends or making any other distribution on any other class of its share capital or reducing or buying back any share capital until one of the following occurs: <ul style="list-style-type: none"> <li>○ an amount equal to unpaid scheduled Dividends for the period immediately preceding the date of payment of that amount (<b>Optional Dividend</b>) has been paid to Preference Share Holders; or</li> <li>○ all Preference Shares have been purchased or bought-back.</li> </ul> </li> <li>• In the event that PAYCE breaches the Dividend Payment Restriction outlined above, and does not remedy that breach within 90 days, the Preference Shares will be exchanged for redeemable preference shares which are redeemable immediately at the option of holders. Each Preference Share will be exchanged for one redeemable preference share.</li> </ul> |
| Voting  | <p>Generally, the Preference Shares will carry no right to vote at any general meeting of Shareholders of PAYCE. However, holders of Preference Shares may vote on the basis of one vote per Preference Share in the following circumstances:</p> <ul style="list-style-type: none"> <li>(a) on a proposal: <ul style="list-style-type: none"> <li>(i) to reduce the share capital of PAYCE;</li> <li>(ii) that affects rights attached to the Preference Share;</li> <li>(iii) to wind up PAYCE; or</li> <li>(iv) for the disposal of the whole of the property, business and undertaking of PAYCE;</li> </ul> </li> <li>(b) on a resolution to approve the terms of a buy-back agreement;</li> <li>(c) during a period in which a Dividend or part of a Dividend on the Preference Share is in arrears; or</li> <li>(d) during the winding up of PAYCE.</li> </ul>  |

| Feature  | Details  |
|--|--|
| Priority of payment of capital and dividends in relation to other shares or classes of preference shares | The Preference Shares will rank equally among themselves, and ahead of Ordinary Shares in relation to dividends and the return of capital. |

For further information, the terms of the Preference Shares are summarised in section 2.2 and detailed in Schedule 1 of this document.

### 8.3 Recommendation of Directors

Each of the Independent Directors **recommends** that Shareholders **vote in favour of this Resolution**.

## 9. ADDITIONAL INFORMATION

### 9.1 RECENT FINANCIAL INFORMATION

PAYCE released its Financial Report for the half-year ending 31 December 2014 to the ASX on 20 February 2015.

### 9.2 DIRECTORS' INTERESTS

No Director will receive any payment or benefit of any kind as a consequence of the Buy-Back other than in their capacity as a Shareholder in PAYCE.

Directors who hold Ordinary Shares at the Buy-Back Record Date will be able to participate in the Buy-Back to the same extent as all other Shareholders.

As at the date of this document, the Directors either directly or indirectly have the following interests in Ordinary Shares. The intentions of the Directors and/or their associated entities (if any) to participate in the Buy-Back are also indicated below:

| Director            | Ordinary Shares | Percentage of total Ordinary Shares on issue | Intention to accept       | Balance Ordinary Shares held following Buy-Back |
|---------------------|-----------------|--|---------------------------|---|
| Brian Boyd*         | 11,525,460      | 38.7%  | 1,660,000 Ordinary Shares | 9,865,460                                       |
| Roger Short         | 65,000          | 0.2%   | 40,000 Ordinary Shares    | 25,000  |
| Christopher Gabriel | 0               | 0.0%   | N/A                       | N/A   |

### 9.3 DOCUMENTS INCORPORATED BY REFERENCE

All documents that PAYCE has lodged with ASIC or ASX contain important information for Shareholders and their professional advisors. PAYCE also includes by reference the announcements referred to below for full disclosure of relevant information to Shareholders:

| Date       | Title                   | Description of the document   |
|------------|-------------------------|---|
| 09/03/2015 | Kirrawee project update | The Kirrawee project received concept plan approval from the NSW Planning Assessment Commission to increase the gross floor area to 85,000 sqm. |

| Date       | Title   | Description of the document   |
|------------|---|---|
| 20/02/2015 | Half Yearly Report and Accounts                             | Financial Report of PAYCE for the half-year ending 31 December 2014.  |
| 13/01/2015 | TOV: PAY Application Received & Withdrawn                   | The Takeovers Panel consented to a request by ASIC to withdraw its application to the Panel following cancellation by PAYCE of the proposed general meeting.                              |
| 13/01/2015 | TOV: PAYCE - President Makes Interim Orders                 | The Takeovers Panel made interim orders in response to an application by ASIC in relation to the proposed meeting of PAYCE to consider whether to approve an equal access share buy back. |
| 12/01/2015 | Extraordinary General Meeting - Cancelled                   | PAYCE cancelled the general meeting scheduled for 13 January 2015 following application by ASIC to the Takeovers Panel.   |
| 12/01/2015 | Extraordinary Meeting - Update                              | Two entities associated with Managing Director Brian Boyd provided undertakings not to vote at the general meeting scheduled for 13 January 2015.   |
| 22/12/2014 | Offer Document relating to an equal access buy-back         | Offer Document to Shareholders relating to a proposed equal access buy-back of Shares in return for a combination of cash and preference shares   |
| 09/12/2014 | Notice of Extraordinary General Meeting/Off Market Buy-Back | Notice of General Meeting seeking shareholder approval for a proposed equal access share buy back   |
| 28/11/2014 | Completion of acquisition of industrial site                | Advised that PAYCE, along with its joint venture partner Sekisui House, have completed the acquisition of industrial site in Melrose Park, Sydney   |
| 17/11/2014 | Cancellation of Shares                                      | To lodge copies of ASIC Forms from 2011 previously not lodged on ASX Platform.  |
| 11/11/2014 | AGM   | Announcements in relation to the annual general   |

| Date       | Title  | Description of the document   |
|------------|--|---|
|            |  | meeting   |
| 31/10/2014 | Noteholder Resolution Result                             | Advised that the Resolution being voted on by Noteholders to approve changes to the Conditions of the Notes was not passed.                               |
| 29/10/2014 | East Village – Victoria Park, New South Wales            | Provided a further update from ASX Announcement dated 14 October 2014 on progress of 'East Village' project.  |
| 14/10/2014 | Proposed amendment of Conditions of Senior Secured Notes | Advised of PAYCE's intention to seek approval from the holders of the 9.50% Notes due 3 December 2018, to amend the Conditions attaching to those Notes.  |
| 14/10/2014 | East Village – Victoria Park, New South Wales            | Advised that the 206 residential units forming part of the mixed use 'East Village' project had reached practical completion with settlements commencing. |
| 13/10/2014 | Completion of sale of development land                   | Advised of completion of the sale of a development site in Hurstville, Sydney.  |
| 08/10/2014 | Annual Report to Shareholders                            | Financial Report of PAYCE for the year ending 30 June 2014  |

These documents may be accessed via PAYCE'S website at [www.payce.com.au](http://www.payce.com.au). In addition, copies of these documents have been lodged with ASIC and the ASX, and may be obtained from PAYCE's announcement page on ASX ([www.asx.com.au](http://www.asx.com.au)).

#### 9.4 NO OTHER ADDITIONAL INFORMATION

Other than as set out in this Explanatory Statement, there is no other additional information that is known to the Directors that may reasonably be expected to be material to the making of a decision by Shareholders whether or not to vote in favour of the Resolutions.

#### 9.5 APPLICABLE LAW

This document and the Buy-Back are governed by the laws of New South Wales.

## 9.6 LODGMENT

In accordance with section 257C(3) of the *Corporations Act*, a copy of the Notice of Extraordinary General Meeting and the Explanatory Statement has been lodged with ASIC.



# Schedule 1

## TERMS OF PREFERENCE SHARES

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### 1. DEFINITIONS

In these terms of issue for Preference Shares, the following words and expressions have the following meanings:

**'ASIC'** means the Australian Securities and Investments Commission;

**'ASX'** means ASX Limited ACN 008 824 691 or the financial market operated by it as the context requires;

**'Business Day'** has the meaning given to that term in the ASX Listing Rules;

**'Call Option'** means PAYCE's option to Repurchase the Preference Share pursuant to clause 3.8;

**'Change in Control Event'** means, on any date, an event where a person (and its associates) or such persons acting together which held, whether directly or indirectly, 40% or less of the issued Ordinary Shares of PAYCE as at the Issue Date (and including a zero holding) subsequently holds, whether directly or indirectly, more than 40% of the issued Ordinary Shares of PAYCE on that date;

**'PAYCE'** means PAYCE Consolidated Limited ABN 19 001 566 310;

**'Directors'** means the directors of PAYCE from time to time;

**'Dividend'** means a dividend payable at the discretion of PAYCE on the Preference Shares in accordance with clause 3;

**'Dividend Payment Date'** means each 3 September, 3 December, 3 March and 3 June until the Preference Shares are purchased or bought back;

**'Dividend Payment Restriction'** means the restrictions imposed on PAYCE if a Dividend is not paid on the Preference Shares, as set out in clause 3.7;

**'Dividend Period'** means the period from, and including, the Issue Date or the preceding Dividend Payment Date (whichever is later) until, but not including, the next Dividend Payment Date;

**'Dividend Rate'** means:

- (a) from the Issue Date until (but excluding) the day which is 12 months from the Issue Date: 6% per annum;

- (b) on each yearly anniversary of the Issue Date, the Dividend Rate will increase by an additional 1% per annum (for example:
- (i) from the day which is one year from the Issue Date, until (but excluding) the day which is ten years from the Issue Date: 7% per annum;
  - (ii) from the day which is two years from the Issue Date, until (but excluding) the day which is three years from the Issue Date: 8% per annum,
- and thereafter increasing by 1% per annum in each following yearly period),
- until the date which is six years from the Issue Date when the Dividend Rate increases to 12% per annum, at which time the Dividend Rate will be capped at 12% per annum.

**'Issue Date'** means the date on which the Preference Shares are issued;

**'Issue Price'** deemed to be \$7.50 per Preference Share;

**'Law'** and **'Corporations Law'** means the Corporations Act 2001 and the Corporations Regulations;

**'Listing Rules'** means the official listing rules of ASX;

**'Ordinary Shares'** means an ordinary share in the capital of PAYCE;

**'Preference Share'** means a preference share in the capital of PAYCE issued in accordance with these terms and conditions;

**'Preference Share Exchange Date'** has the meaning given to it in clause 3.8(b);

**'Preference Share Holder'** means the registered holder of a Preference Share;

**'Redeemable Preference Shares'** are those shares issued in accordance with clause 3.8;

**'Repurchase'** in relation to a Preference Share means to buy-back or cancel the Preference Share in any manner permitted by the Corporations Law and the Listing Rules;

**'Shareholders'** means the holders of Ordinary Shares in PAYCE.

## **2. DESCRIPTION**

### **2.1 Terms of issue**

These are the terms of issue on which PAYCE will issue the Preference Shares.

### **2.2 Issue Price**

The Preference Shares will be issued as partial consideration for a buy-back of Ordinary Shares undertaken by PAYCE on or around June 2015, with an Issue Price of \$7.50 each.

### 3. DIVIDENDS

#### 3.1 Dividends

Subject to clause 3.2, PAYCE shall pay to Preference Share Holders, on each Dividend Payment Date, a preferential Dividend on each Preference Share. The Dividend per Preference Share will be calculated as follows:

$$\text{DIV} = \frac{\text{DR} \times \text{IP} \times \text{D}}{365}$$

Where:

- **DIV** is the amount of the dividend payable on each Preference Share on the Dividend Payment Date (the '**Dividend Entitlement**');
- **DR** is the Dividend Rate applicable for that Dividend Period;
- **IP** is the Issue Price; and
- **D** is the number of days in that Dividend Period.

#### 3.2 Payment of Dividend

- (a) The Dividend may at the discretion of PAYCE, be paid by either or a combination of:
- (i) a cash payment; and/or
  - (ii) the issue of further Preference Shares with an issue price of \$7.50 each, representing an amount equivalent to the Dividend Entitlement (with any fractional amount remaining paid in cash).
- (b) The payment of a Dividend is subject to:
- (i) the Directors, at their discretion, declaring the Dividend to be payable or otherwise resolving to pay the Dividend;
  - (ii) there being funds legally available for the payment of dividends; and
  - (iii) compliance with these terms of issue, including but not limited to the restriction set out in clause 3.7.

#### 3.3 Record Dates

A Dividend is only payable to those persons registered as holders of Preference Share at the date on which the books of PAYCE close for Preference Share Holders in respect of each relevant Dividend.

#### 3.4 Calculation of Dividends

All calculations to be undertaken with respect to Dividends will be to four decimal places. For the purposes of making a dividend payment in respect of a Preference Share Holder's aggregate holding, any fraction of a cent will be disregarded.

### 3.5 Dividends are cumulative

Dividends are cumulative. If all or any part of a scheduled Dividend is not paid (**Unpaid Dividend**) on the relevant Dividend Payment Date because of the restrictions in clause 3.2(b), PAYCE has an obligation to pay the Unpaid Dividend at the time of Repurchase in accordance with clause 4. No interest accrues on any Unpaid Dividend.

### 3.6 Optional dividend

Without limiting clause 3.2(b) or clause 3.5, PAYCE may at its absolute discretion, elect at any time to pay Preference Share Holders an optional dividend in an amount equal to the unpaid amount of all scheduled (but unpaid) Dividends for the period preceding the payment date of the optional dividend (**Optional Dividend**).

### 3.7 Dividend Payment Restriction

If a scheduled Dividend has not been paid on Preference Shares in full for any reason within five business Days of the relevant Dividend Payment Date, PAYCE must not:

- (a) declare or other determine to pay, or pay, a dividend or make any distribution on any class of its share capital other than Preference Shares; or
  - (b) redeem, reduce, cancel, buy-back or acquire for any consideration any share capital,
- unless:

- (a) where a scheduled Dividend has not been paid in full within five business Days of the relevant Dividend Payment Date, since that date, PAYCE has paid to Preference Share Holders in full an Optional Dividend; or
- (b) all Preference Shares have been purchased or bought back by PAYCE,

provided that nothing in this clause will be taken to prevent a payment by way of pro rata payments to Preference Share Holders and the holders of any security which ranks in respect of dividends or return of capital equally with the Preference Shares.

### 3.8 Consequences of breach of Dividend Payment Restriction

- (a) If PAYCE breaches the Dividend Payment Restriction set out in clause 3.7, and fails to rectify such breach through the payment of Dividends on the Preference Shares within 90 days of such breach, PAYCE must on the expiration of that 90 day period give Preference Share Holders a notice, stating that on the Preference Share Exchange Date, all Preference Shares will be exchanged for redeemable preference shares (**Redeemable Preference Shares**) having the same rights as the Preference Shares with an additional right allowing holders to immediately (or at any time) require PAYCE to redeem those Redeemable Preference Shares. Each Preference Share will be cancelled in exchange and consideration for the issue of one Redeemable Preference Share.
- (b) For the purposes of this clause, '**Preference Share Exchange Date**' means the date which is three Business Days after the date of the notice given under clause 3.8(a).

- (c) Notice given in accordance with clause 3.8(a) is irrevocable once given. Failure to give such notice when required under clause 3.8(a) does not affect the obligation of PAYCE to exchange the Preference Shares for Redeemable Preference Shares when required in accordance with these terms.
- (d) If, on a Preference Share Exchange Date, a Redeemable Preference Share is not issued in exchange for a Preference Share, that Preference Share remains on issue until the Redeemable Preference Share is issued to the holder or the Preference Share is purchased or bought back by PAYCE, and clause 3.7 continues to apply. This clause does not affect the obligation of PAYCE to issue the Redeemable Preference Shares when required in accordance with these terms.

### 3.9 Effect of exchange

- (a) Upon the exchange of Preference Shares for Redeemable Preference Shares on the Preference Share Exchange Date in accordance with clause 3.8, all other rights conferred or restrictions imposed on those Preference Shares will no longer have effect and those Preference Shares will be cancelled.
- (b) Each Preference Share Holder irrevocably:
  - (i) acknowledges and agrees that it is obliged to accept Redeemable Preference Shares upon an exchange of Preference Shares in accordance with these terms notwithstanding anything which might otherwise affect an exchange of Preference Shares for Redeemable Preference Shares, including:
    - A. any change in the financial position of PAYCE since the Issue Date;
    - B. any disruption to capital markets generally;
    - C. any breach by PAYCE of an obligation in connection with the Preference Shares or the Redeemable Preference Shares; or
    - D. it being impossible or impracticable to sell or otherwise dispose of Redeemable Preference Shares;
  - (ii) agrees to provide to PAYCE any information which PAYCE may consider necessary or desirable to give effect to the exchange of a Preference Share for a Redeemable Preference Share in accordance with these terms; and
  - (iii) appoints PAYCE as its agent and attorney with power in its name and on its behalf to do all things necessary to give effect to the exchange of a Preference Share for a Redeemable Preference Share in accordance with these terms, including:
    - A. completing and executing such instruments for and on its behalf as PAYCE considers necessary or desirable to give effect to an exchange of

a Preference Share for a Redeemable Preference Share in accordance with these terms; and

B. appointing in turn its own agent or delegate.

### **3.10 Redemption of Redeemable Preference Shares**

(a) Redeemable Preference Shares issued in accordance with clause 3.8(a) may be redeemed by the holder submitting a redemption notice (**Redemption Notice**) to PAYCE at any time which:

- (i) is in the form made available by PAYCE on request;
- (ii) specifies the Redeemable Preference Shares to which it relates; and
- (iii) is accompanied by evidence of title reasonably satisfactory to PAYCE.

Once the Redemption Notice has been given, the holder of the Redeemable Preference Shares must not deal with, transfer, dispose or otherwise encumber the Redeemable Preference Shares which are the subject of that Redemption Notice.

(b) PAYCE must within 90 days of receipt of a Redemption Notice, redeem the Redeemable Preference Shares the subject of that Redemption Notice and pay to the holder the redemption amount, which is the aggregate of:

- (i) the issue price of the Redeemable Preference Shares (being \$7.50 per Redeemable Preference Share); and
- (ii) an amount equal to the unpaid amount of any scheduled Dividends which have not been paid on the Preference Shares and/or Redeemable Preference Shares for the period preceding the date on which the Redemption Notice is given under clause 3.10(a).

(c) If PAYCE does not redeem the Redeemable Preference Shares when required to do so in accordance with this clause, the Redeemable Preference Shares will remain on issue until they are redeemed, purchased or bought-back by PAYCE.

## **4. CALL OPTION**

### **4.1 Option to Repurchase**

(a) Each Preference Share Holder grants to PAYCE an option to Repurchase on any Dividend Payment Date some or all of the Preference Shares they may hold, for an amount equal to:

- (i) the Issue Price of each Preference Share; plus
- (ii) the unpaid amount of any scheduled Dividends which have not been paid on the Preference Shares during the period prior to the date on which the notice is given under clause 4.1**(b)**.

- (b) At least 30 days (but no more than 3 months) before the relevant Dividend Payment Date, PAYCE may give notice to one or more Preference Share Holders stating that it will exercise its option under clause 4.1(a) to Repurchase a specified number of Preference Shares from that Preference Share Holder in accordance with clause 4.3.

#### 4.2 Repurchase on Change in Control Event

If a Change in Control Event occurs, PAYCE may at its discretion, Repurchase some or all of the Preference Shares, by giving notice to the Preference Share Holders at any time (but no later than 30 days after the date on which the event occurs) after the Change in Control Event occurs.

#### 4.3 Repurchase procedure

- (a) Subject to PAYCE having obtained all necessary approvals and consents required under the Corporations Act, the ASX Listing Rules and PAYCE's constitution, PAYCE may, where it has given a notice pursuant to clause 4.1(b) that it proposes to Repurchase all or some of the Preference Shares, Repurchase the Preference Shares that were the subject of that notice on the relevant date.
- (b) The consideration for any Repurchase of a Preference Share under this clause 4.3 will be a cash payment equal to the Issue Price of \$7.50 per Preference Share.
- (c) Each Preference Share Holder appoints PAYCE and each of the Directors, jointly and all severally, to be the lawful attorneys of the Preference Share Holder to accept all offers and to execute all notices and other documents necessary or desirable to effect a Repurchase of Preference Shares pursuant to this clause 4.3.

### 5. GENERAL RIGHTS AND OBLIGATIONS OF PREFERENCE SHARES

#### 5.1 Ranking

Preference Shares rank equally amongst themselves in all respects.

#### 5.2 Preferential Dividend

Preference Shares rank in priority to Ordinary Shares for the payment of dividends.

#### 5.3 Return of Capital

If there is a return of capital on a winding-up of PAYCE, Preference Share Holders will be entitled to receive out of the assets of PAYCE available for distribution to holders of shares, in respect of each Preference Share held, a cash payment equal to the sum of:

- (a) the amount of any Dividend Entitlement which has not been satisfied in full including any Dividend Entitlement which has accrued for the period from and including the date of the preceding Dividend Payment Date to the date of commencement of the winding-up; and
- (b) the Issue Price,

before any return of capital is made to holders of Ordinary Shares or any other class of shares ranking behind the Preference Shares.

#### **5.4 Shortfall on Winding Up**

If, upon a return of capital, there are insufficient funds to pay in full the amounts referred to in clause 5.3 and the amounts payable in respect of any other shares in PAYCE ranking as to such distribution equally with the Preference Share on a winding-up of PAYCE, the Preference Share Holders and the holders of any such other shares will share in any distribution of assets of PAYCE in proportion to the amounts to which they respectively are entitled.

#### **5.5 Participation in Surplus Assets**

Preference Shares do not confer on their holders the right to participate in the surplus assets of PAYCE on a winding-up beyond the rights set out in clauses 5.3 and 5.4.

#### **5.6 Takeovers and Schemes of Arrangement**

If a takeover bid is made for Ordinary Shares, acceptance of which is recommended by the Directors, or the Directors recommend a member's scheme of arrangement, the Directors will use reasonable endeavours to procure that equivalent takeover offers are made to Preference Share Holders or that they participate in the scheme of arrangement.

#### **5.7 Participation in New Issues**

A Preference Share does not confer rights to subscribe for new securities in PAYCE or to participate in any bonus or rights/entitlement issues.

#### **5.8 Notices**

Preference Share Holders are entitled to the same rights as Ordinary Shareholders to receive notices, reports and audited accounts and to attend meetings.

#### **5.9 Transfers of Preference Shares**

A transfer of a Preference Share will only be accepted as a proper instrument of transfer in registrable form if it complies with the requirements of PAYCE's constitution and the Law.

#### **5.10 Holding statements**

Holding statements in respect of Preference Shares may be provided by PAYCE to members from time to time.

### **6. VOTING RIGHTS**

A Preference Share does not entitle its holder to vote at any general meeting of PAYCE except in the following circumstances:

- (v) on a proposal:
  - (i) to reduce the share capital of PAYCE;
  - (ii) that affects rights attached to the Preference Share;
  - (iii) to wind up PAYCE; or
  - (iv) for the disposal of the whole of the property, business and undertaking of PAYCE;
- (vi) on a resolution to approve the terms of a buy-back agreement;



- (vii) during a period in which a Dividend or part of a Dividend on the Preference Share is in arrears; or
- (viii) during the winding up of PAYCE.

Under these circumstances, Preference Share Holders will be entitled to one vote per Preference Share.

## **7. AMENDMENTS TO THE TERMS OF ISSUE**

Subject to complying with all applicable laws, PAYCE may without the authority, assent or approval of Preference Share Holders amend or add to these terms of issue if such amendment or addition is, in the opinion of PAYCE:

- (a) of a formal, minor or technical nature;
- (b) made to correct a manifest error; or
- (c) not likely (taken as a whole and in conjunction with all other modifications, if any, to be made contemporaneously with that modification) to be materially prejudicial to the interests of Preference Share Holders.

## **8. INTERPRETATION**

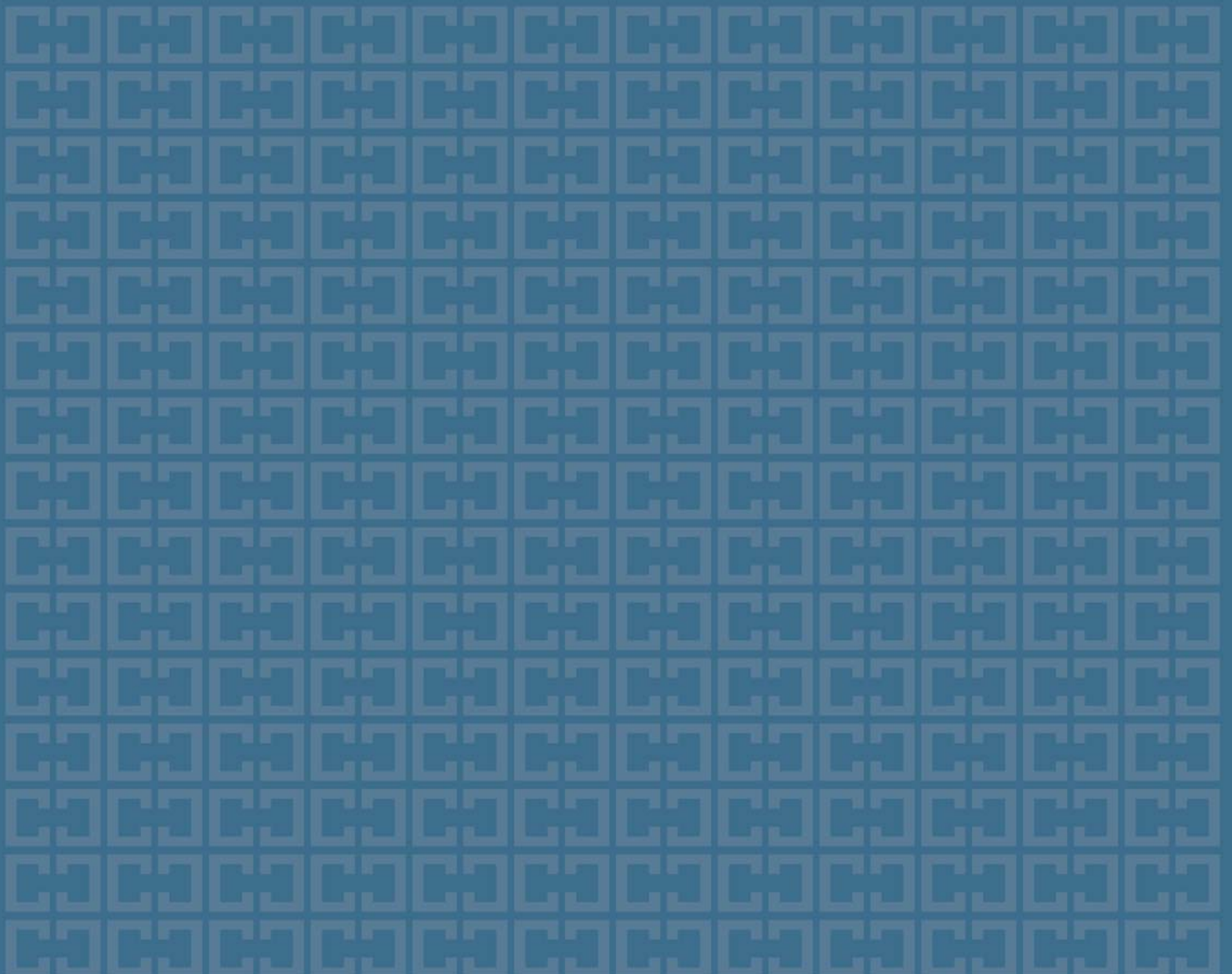
- (a) Unless the context otherwise requires, if there is any inconsistency between the provisions of these terms of issue and PAYCE's constitution, then, to the maximum extent permitted by law, the provisions of these terms of issue will prevail.
- (b) If a calculation is required under these terms of issue, unless the contrary intention is expressed, the calculation will be performed to four decimal places.
- (c) Definitions and interpretation under PAYCE's constitution will also apply to these terms of issue.

## ANNEXURE

### Independent Expert's Report

**Independent Expert's Report and  
Financial Services Guide**

**PAYCE Consolidated Limited  
Proposed Off-Market Buy-back  
2 April 2015**





## Part 1 – Independent Expert's Report

2 April 2015

The Independent Directors  
PAYCE Consolidated Limited  
Level 37, Chifley Tower  
2 Chifley Square  
SYDNEY NSW 2000

Dear Independent Directors,

### **Off-Market Equal Access Share Buy-back – Independent Expert's Report**

#### **Introduction**

By Notice of Extraordinary General Meeting (Notice) dated 2 April 2015, PAYCE Consolidated Limited ("the Company") advised that as part of PAYCE's capital management strategies it would offer Shareholders the opportunity to participate in an equal access off-market share Buy-back. If approved the equal access off-market Buy-back would allow those Shareholders who wanted to reduce their holding of Ordinary Shares, the ability to do so:

- in consideration for cash and Preference Shares; and
- in light of the illiquidity of PAYCE's shares, providing that opportunity without placing downwards pressure on the Company's share price.

The proposed off-market Buy-back is subject to:

- (i) Shareholder approval for an equal access Buy-back of up to 9,915,075 issued Ordinary Shares in PAYCE; and
- (ii) Shareholder approval to issue up to 9,915,075 Preference Shares in partial consideration for the Buy-back proposal, conditional upon approval of (i).

The Resolutions to accomplish the above are to be put to an Extraordinary General Meeting of Shareholders on 4 May 2015 and the Notice is to be accompanied by an Independent Expert's Report ("Report" or "IER").

For each Ordinary Share participating in the Buy-back the overall consideration comprises:

- \$0.80 per share cash paid upon cancellation of the Ordinary Shares participating in the Buy-back;
- \$0.80 per share cash paid 12 months after the cancellation of the Ordinary Shares participating in the Buy-back (second payment);
- \$0.70 per share cash paid 18 months after the cancellation of the Ordinary Shares participating in the Buy-back (third payment);
- A Preference Share issued (with an issue price of \$7.50) upon cancellation of the Ordinary Share and having an assessed fair market value of \$7.23.



In addition, once the Buy-back has been undertaken, Shareholders will continue to hold their remaining Ordinary Shares which will then have an assessed fair market value of between \$5.33 and \$6.06 (depending on the level of scale back).

### **Purpose of Report**

Notwithstanding that there is no legal requirement for the preparation of a Report the Independent Directors of PAYCE have requested Hanrick Curran Corporate Finance Pty Ltd ("HCCF") to prepare a Report expressing our opinion as to whether the Buy-back is fair and reasonable to those Shareholders of PAYCE not associated with Managing Director Mr Brian Boyd (Non Associated Shareholders). The purpose of this report is to assist Non Associated Shareholders in their deliberation on whether to approve (and/or participate in) the Buy-back and consequential issue of Preference Shares as part consideration of the Buy-back. PAYCE is seeking approval from Shareholders for the Buy-back at an Extraordinary General Meeting (the "Meeting"). Our Report is to be included in the Notice being sent to the Shareholders in relation to the Meeting. The Independent Directors have set out their reasons for supporting the Off-Market Equal Access Share Buy-back in the Explanatory Statement.

### **Basis for Evaluation**

In preparing our Report, we have had regard to ASIC Regulatory Guide 110: *Share buy-backs*. (RG 110). Under ASIC Regulatory Guide 110: '*Share buy-backs*' (RG 110) '*if a company proposes to Buy back a significant percentage of shares or the holding of a major shareholder, it should consider providing [...] an independent expert's report with a valuation of the shares*'. Notwithstanding that RG 110 recommends the provision of independent advice from an expert in relation to a proposed Buy-back, it does not provide specific guidance on how to form an opinion, or the factors to consider in forming such an opinion.

Given the lack of specific guidance within RG 110, in considering the approach to adopt with respect to the evaluation of the proposed Buy-back we have considered the ASX Listing Rules, ASIC Regulatory Guides the Corporations Act and common market practice.

Having considered these various sources, we consider it appropriate to assess whether the Buy-back is fair and reasonable to Non Associated Shareholders having regard to the advantages and disadvantages, so far as Non Associated Shareholders are concerned, of the Buy-back. In considering these matters we have, amongst other things, compared the consideration being paid for the Buy-back Shares with our estimate of the fair market value of the Buy-back shares.

In line with the requirements of RG 110 and market practice, in order to assist Non Associated Shareholders with their consideration of whether to approve or participate in the Buy-back, we have also prepared a valuation of PAYCE shares.

This assessment of value has been undertaken on the basis that the Buy-back is approved and implemented by PAYCE. We consider this the appropriate basis of evaluation because the Buy-back will only be available to Shareholders if the Buy-back is approved. In order to assist Non Associated Shareholders in their assessment, we have assessed other factors that Non Associated Shareholders should consider in determining whether to approve or participate in the Buy-back.

The Buy-back represents a transaction in respect of minority interests. That is, the Buy-back relates to 33.3% of the equity interest in PAYCE. Furthermore, whilst it could be argued that a small



number of Non Associated Shareholders already control the majority of PAYCE shares RG 111: *Content of expert reports*, requires that we value PAYCE shares on the basis that the Buy-back is a control transaction whereby a person, in this case the Managing Director Mr Brian Boyd and his associates increases their stake in PAYCE. This is the basis of our analysis of the proposed Buy-back.

In light of the above, and consistent with RG 110 and RG 111 and within our Report, we provide:

- a valuation of a PAYCE Ordinary Share before the off-market equal access Buy-back on the basis that the Buy-back is a control transaction;
- a valuation of the cash and Preference Shares offered in consideration for each PAYCE Ordinary Share;
- an analysis of the advantages and disadvantages to Non Associated Shareholders of the Buy-back offer including a comparison of the consideration which Non Associated Shareholders are expected to receive in each of the following scenarios:
  - (a) for Non Associated Shareholders who participate fully in the Buy-back offer;
  - (b) for Non Associated Shareholders who participate partially in the Buy-back offer; and
  - (c) for Non Associated Shareholders who do not participate at all in the Buy-back offer;
- and an assessment of whether the Buy-back is fair and reasonable to Non Associated Shareholders.

Our valuation has been prepared on a control basis to provide Non Associated Shareholders with an estimate of the fair market value of a PAYCE ordinary share assuming 100% ownership of the Company. Our valuation takes into account PAYCE's current operations and capital structure, and does not reflect the impact of the off market Buy-back proposal. However, in our assessment of the advantages and disadvantages of each of the three possible scenarios, we have simulated the impact of the three scenarios at various levels of participation in the Buy-back on our valuation to provide Non Associated Shareholders with an indication of the range of overall consideration that may be expected.

### **Summary of valuation analysis**

Non-Associated Shareholders have a number of options open to them, namely:

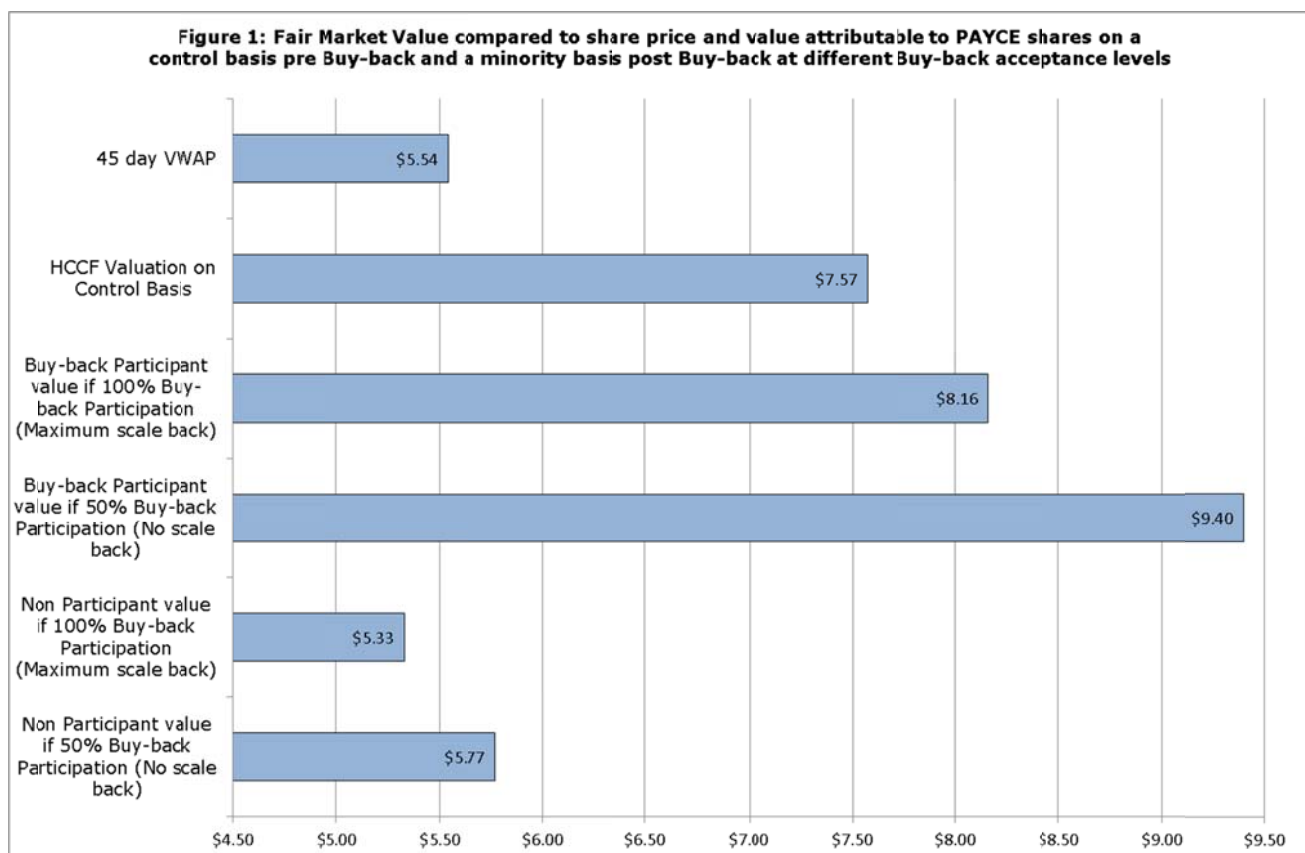
- (a) to reject the equal access off-market Buy-back proposal and continue to own Ordinary Shares in PAYCE;
- (b) to approve the equal access off-market Buy-back proposal and participate fully in the Buy-back offer;
- (c) to approve the equal access off-market Buy-back proposal and participate partially in the Buy-back offer; and
- (d) to approve the equal access off-market Buy-back proposal and not participate at all in the Buy-back offer



The different options available to Non Associated Shareholders will suit the circumstances of different Non Associated Shareholders.

The additional complexity to be taken into account in each Non Associated Shareholder's decision process is that the more appealing the Buy-back is assessed to be by Non Associated Shareholders, the higher the expected overall level of participation and, consequently, the greater the risk that the Buy-back will be fully utilised so that up to 30% of shares accepted into the Buy-back by each Non Associated Shareholder will not be bought back by PAYCE. This would result in Non Associated Shareholders retaining up to 30% of their shares in PAYCE, which may not necessarily be their desired outcome.

The figure below compares our fair market value of a PAYCE share on a control basis of \$7.57 with the indicative value attributable to Non Associated Shareholders under alternatives (b), (c) and (d) outlined above as well as the 45-day volume weighted average price (**VWAP**), for PAYCE shares as at 20 February 2015 of \$5.54. For the purpose of this analysis, we have assessed the value of any residual PAYCE shares owned by Non Associated Shareholders pursuant to each of the scenarios, adjusted for any value accretion or dilution resulting from various levels of participation in the Buy-back and adjusting the value of the Ordinary Shares on a control basis by 20%, to reflect that they will be held on a minority basis after the Buy-back:





We note the following in relation to the graph above:

- we have assessed the fair market value of PAYCE, on a control basis, to be \$225.266 million. This translates into a fair value per share of \$7.57 and is based on our primary valuation methodology, being a sum of the parts valuation of the PAYCE business. Our valuation of PAYCE is discussed in further details in Section 5;
- based on our valuation range of PAYCE under the possible outcomes for the overall value attributable to Non Associated Shareholders **who elect not to participate in the Buy-back**:
  - assuming 50% of available shares participate in the Buy-back there would be no scale back and each PAYCE share post transaction would have a fair value of \$5.77;
  - assuming 100% of available shares participate in the Buy-back there would be the maximum scale back of 30% and each PAYCE share post transaction would have a fair value of \$5.33 per PAYCE share;
- based on our valuation of PAYCE under the possible outcomes for the overall value attributable to shareholders **who elect to participate in the Buy-back**:
  - assuming 50% of available shares participate in the Buy-back there would be no scale back and the overall value attributable to each would be \$9.40. This figure comprises the following:
    - cash consideration (of \$0.80 paid on cancellation, \$0.80 paid 12 months after cancellation and \$0.70 paid 18 months after cancellation) valued at \$2.17 per PAYCE share and;
    - fair value of Preference Share of \$7.23;
  - assuming 100% of available shares participate in the Buy-back, there would be the maximum scale back of 30% and the overall value attributable to each PAYCE share would be \$8.16. This figure comprises the following:
    - cash consideration (of \$0.80 paid on cancellation, \$0.80 paid 12 months after cancellation and \$0.70 paid 18 months after cancellation) valued at \$2.17 per PAYCE share and fair value of Preference Share of \$7.23 multiplied by 70% which is the acceptance level based on scaling;
    - value of a PAYCE share at this acceptance level of \$5.33 multiplied by 30%, which is the remaining shares not bought back as a percentage of the original shareholding prior to the Buy-back.

Subsequent to the implementation of the Buy-back, shareholders may be left with minority equity investments in PAYCE and therefore may not be able to realise a full control value for their PAYCE shares, unless a takeover offer materialises for PAYCE. Minority parcels of shares attract a discount





to their full underlying value and our fair value calculations post Buy-back have been determined utilising a 20 percent discount rate.

### **Valuation of PAYCE shares on a control basis**

HCCF has assessed the fair market value of a PAYCE share, on a control basis, to be \$7.57. For the purpose of our opinion, fair market value is defined as the amount at which the PAYCE shares would change hands between a knowledgeable willing buyer and a knowledgeable willing seller, neither being under a compulsion to buy or sell. We have not considered special value in this assessment.

Our valuation assumes a hypothetical change of control transaction and is undertaken prior to the implementation of the off-market Equal Access Buy-back. That is, our valuation on a control basis reflects neither the cash payments nor the potential dilution/accretion on the share value potentially resulting from the implementation of the Buy-back.

For the purpose of our analysis, we have valued PAYCE as at 20 February 2015 (the Valuation Date). We have estimated the fair market value of PAYCE by aggregating the estimated fair market value of the assets and liabilities of PAYCE on a sum of the parts basis as summarised in the table below.

**Table 2: Valuation of PAYCE**

| <b>Asset Class</b>         | <b>Reference</b> | <b>\$'000</b>  |
|----------------------------|------------------|----------------|
| Property Developments      | Appendix J       | 209,503        |
| Investment Properties      | Appendix J       | 102,256        |
| Other Assets / Liabilities | 5.4.3            | (86,493)       |
| <b>Total</b>               |                  | <b>225,266</b> |

In determining the value of shares in PAYCE, we also considered whether there should be a premium or discount for those shares compared to PAYCE's net asset value (NAV) or net tangible assets (NTA). NAV's and NTA's are two common valuation metrics of Australian Real Estate Investment Trusts (A-REITs). NTA is based on the underlying book value of assets whereas NAV is based on the expected cash flows from the property assets, together with other income generating assets.

The major property assets of PAYCE are stated at contract price, recent valuation (e.g. Kirrawee), based on the underlying cash flows of the investment asset as assessed in a recent valuation (e.g. East Village) or is in the process of development (e.g. Riverwood). PAYCE's property assets have been determined on the basis of NAV. Whilst it may be argued that there is valuation upside in assets under development, those assets represent a small proportion of the overall property assets (7.4%) and in our opinion do not warrant adjusting the overall property portfolio to reflect any premium or discount.



### **Valuation cross-check – Share Trading**

In order to assess the reasonableness of our estimate of the fair market value of a PAYCE share, we have compared our assessed fair market value to recent trading in PAYCE shares. The historical trading performance of PAYCE's shares has also been compared to our estimate of fair value.

Our valuation at \$7.57 implies a premium to recent PAYCE share trading. In particular, our valuation range implies a premium of 36.6% to the PAYCE 45-day VWAP \$5.54 as at the Valuation Date.

Minority parcels of shares would typically trade at a discount to the full underlying value of the relevant entity. Minority discounts observed are generally in the range of 15% to 30%. The level of premium implied by our valuation (which is on a control basis) to the most recent PAYCE share trading over the past twelve months is broadly within this range but is greater when compared to the share trading history before the Valuation Date. In this regard, we observe that PAYCE has features that could exacerbate the magnitude of this discount such as:

- relatively low share trading liquidity
- tightly held share capital whereby the top ten shareholders own approximately 93.7% of PAYCE
- lack of analyst coverage.

### **Valuation Cross-check -Discounted Cash Flow (DCF)**

In order to assess the reasonableness of an estimate of fair market value of a PAYCE share, we have also compared our assessed fair market value to the value on a per share basis utilizing a DCF approach. Our fair market value of \$7.57 implies a premium to the DCF value of \$6.20 of 22.10%. Discounting of projected cash flows has a strong theoretical basis. It is the most commonly used method for valuation in a number of industries. DCF valuations involve calculating the net present value of projected cash flows. The cash flows are discounted using a discount rate which reflects the risk associated with the cash flow stream.

Considerable judgement is required in estimating future cash flows and it is generally necessary to place great reliance on medium to long term projections prepared by management. The discount rate is also not an observable number and must be inferred from other data (usually only historical). As this data is not completely reliable, estimates of the discount rate necessarily involve a substantial element of judgement. In addition, even where cash flow forecasts are available, the terminal or continuing value is usually a high proportion of value. Accordingly, the multiple used in assessing this terminal value becomes the critical determinant in the valuation (i.e. it is a "de facto" cash flow capitalisation valuation).

The net present value is typically extremely sensitive to relatively small changes in underlying assumptions, few of which are capable of being predicted with accuracy, particularly beyond the first two or three years. The arbitrary assumptions that need to be made and the width of any value range mean the results are often not meaningful or reliable. Notwithstanding these limitations, DCF valuations are commonly used and can at least play a role in providing a check on alternative methodologies, not least because explicit and relatively detailed assumptions as to expected future performance need to be made.

A financial model of the operating business has been developed by HCCF based on the long term cash flow models prepared by PAYCE. The model allows the key drivers of revenue, operating costs and capital expenditure to be modelled. The model is based on a number of assumptions and is subject to significant uncertainty and contingencies, many of which are outside the control of PAYCE.



A number of different scenarios have been developed and analysed to reflect the impact on value of various key assumptions. The financial model is discussed in more detail in Section 5 of this report.

The DCF Model projects nominal after tax cash flows from 31 December 2014 to 31 December 2021 (a period of 7 years), with terminal values calculated to represent the value of cash flows in perpetuity (by capitalising net after tax cash flows based on a perpetual growth assumption). Net present values are calculated on an ungeared after tax mid-point discount rate (weighted average cost of capital) of **6.41%** in respect of the rental operation, and **7.75%** in respect of the property development activities. A corporate tax rate of 30% has been assumed.

The DCF Model allows revenue, operating costs and capital expenditure to be modelled by sector. The base DCF Model assumes the business operations continue on an "as is" basis reflecting PAYCE's estimate of future returns. The key general and specific operational assumptions are set out in Section 5 and the value per share on a control basis is **\$6.20** per share.

### **Summary**

The value of PAYCE shares on a control basis has been assessed to be \$7.57. This is in our opinion, fair market value, being the amount at which the PAYCE ordinary shares will change hands between a knowledgeable willing buyer and a knowledgeable willing seller, and assumes a hypothetical change of control transaction.

In order to test the primary valuation methodology we have undertaken two valuation cross-checks. As noted in Regulatory Guide 111 cross-check methodology is to be used to reduce the risk that our opinion as Independent Expert may be distorted by the choice of methodology.

The two cross-check methodologies utilized by us to test our primary valuation methodology were a comparison to share trading and an assessment of value on a discounted cash flow basis.

Both the share trading and DCF methodologies are materially less than our assessment of fair value. The share trading valuation based on the PAYCE 45 day VWAP is \$5.54 which is 36.6% discount to our assessed fair market value of \$7.57. The trading volume over the last three years collectively represent less than 5% of the shares on issue. Whilst utilizing share trading as a cross-check valuation, we have not relied on this as a determinant of fair market value due to the thin nature of the trading over the last three years therefore not being representative of fair market value.

Separately we have undertaken discounted cash flow analysis. The value per share on a control basis is \$6.20 per share. Whilst useful as a cross-check we have excluded the DCF value from our assessment of fair-market value as the methodology is extremely sensitive to relatively small changes in underlying assumptions, a few of which are incapable of being predicted with accuracy particularly beyond the first two or three years, and whilst useful as a cross-check we have formed the opinion that it should not be determinative.



## **Advantages and disadvantages of the Buy-back offer**

The likely advantages and disadvantages to Non Associated Shareholders if the Buy-back is approved are set out below. Where relevant, we have specifically outlined whether the advantage or disadvantage is from the perspective of a participating shareholder (i.e. a shareholder willing to sell their shares under the Buy-back) or a non-participating shareholder (i.e. a shareholder willing to approve the Buy-back but not participate in the Buy-back).

### **Advantages**

#### **1. The Buy-back offers optionality to Non Associated Shareholders (Participating and non-participating Shareholders' perspective)**

If the Buy-back is approved, Non Associated Shareholders will be able to choose whether to participate in the Buy-back having regard to their individual circumstances. The Buy-back therefore provides Non Associated Shareholders with greater flexibility than would a pro-rata return of capital or a special dividend.

Furthermore, approval of the Buy-back could be considered favourably whatever a Non Associated Shareholder's views on the value of a PAYCE share:

- (a) if a Non Associated Shareholder considers the value of a PAYCE share is greater than the consideration payable under the Buy-back, the Non Associated Shareholder could approve the Buy-back since it would offer them the possibility of increasing their interest in PAYCE if other shareholders accept the Buy-back.
- (b) if the Non Associated Shareholder's view on the value of a PAYCE share is less than the consideration payable under the Buy-back, the Non Associated Shareholder could approve the Buy-back so that they would have the opportunity of selling their shares at a premium.

In addition, the Buy-back offers the flexibility to participate only for a portion of a Non Associated Shareholder's holding in the Company. This could allow Non Associated Shareholders to immediately realise some shares while retaining upside potential through the unsold Ordinary Shares.

#### **2. Possibility of achieving greater value in the future (non-Participating Shareholders' perspective)**

To evaluate whether to participate in the Buy-back, Shareholders should consider whether there is a reasonable prospect of being able to achieve greater value by holding their PAYCE shares rather than participating in the Buy-back. The table below sets out the fair market value of PAYCE shares on a minority basis (post Buy-back) assuming various levels of participation.



Sensitivity on value impact from Buy-back on non-Participating Shareholders.

| <b>Table 3: % of available share participation in the Buy-back</b> | <b>Minority value of PAYCE share</b> |
|--|--------------------------------------|
|  | <b>\$</b>                            |
| 0.001%   | 6.06                                 |
| 10%  | 6.01                                 |
| 20%  | 5.95                                 |
| 30%  | 5.90                                 |
| 40%  | 5.83                                 |
| 50%  | 5.77                                 |
| 60%  | 5.69                                 |
| 70%  | 5.61                                 |
| 80%  | 5.53                                 |
| 90%  | 5.43                                 |
| 100%   | 5.33                                 |

1. Based on our fair market value assessment of a PAYCE share of \$7.57 on a control basis, adjusted for a 20% minority discount and the impact of the Buy-back at various participation levels.
2. The total number of shares offered to be bought back is 9,915,075. The maximum number that can participate is 14,268,606 after the intentions of Mr Brian Boyd and Mr Garry Boyd are taken into account.

Moreover, Shareholders that choose to retain their investment in PAYCE may be able to participate in the potential upside.

**3. Participating Shareholders will receive an overall value per share at a premium to PAYCE's recent trading price (Participating Shareholders' perspective)**

The table below demonstrates that at levels of 70% or less participation in the Buy-back, participating shareholders will be able to maximise their value per share in PAYCE. Participating shareholders are able to realise a total value per share of \$9.40 and exit their entire Ordinary Shareholding in PAYCE Buy-back at participation levels of 70% or less. This consideration represents a premium of 69.7% to PAYCE's 45-day VWAP as at the Valuation Date. Accordingly, participating shareholders have the opportunity to achieve a higher value than what may be achieved from a current market transaction. Participating shareholders would be able to successfully accept for a minimum 70% of their shares into the Buy-back, assuming full participation by all other eligible shareholders, and an even greater proportion of their shares if not all eligible shareholders participate.

The table below sets out the proceeds receivable by participating shareholders and the overall value per share for participating shareholders at different levels of participation in the Buy-back.



**Table 4: Total value per share at different levels of participation in the Buy-back**

| Acceptance Level | No. of Shares Participating | Pre Buy-back                         |                                 | Post Buy-back                     |              |                                       |               |                                   |                                       |
|------------------|-----------------------------|--------------------------------------|---------------------------------|-----------------------------------|--------------|---------------------------------------|---------------|-----------------------------------|---------------------------------------|
|                  |                             | Ordinary Share Value (Control Basis) | Preference Share (at Valuation) | Cash Consideration (at Valuation) | Allocation % | Ordinary Share Value (Minority Basis) | Unallocated % | Value: Participating Shareholding | Value: Non-Participating Shareholding |
|                  |                             |                                      | Discount Factor at: 10.25%      | Discount Factor at: 7.50%         |              |                                       |               |                                   |                                       |
| 10%              | 991,507                     | \$7.57                               | \$7.23                          | \$2.17                            | 100.00%      | \$6.01                                | 0.00%         | \$9.40                            | \$6.01                                |
| 20%              | 1,983,015                   | \$7.57                               | \$7.23                          | \$2.17                            | 100.00%      | \$5.95                                | 0.00%         | \$9.40                            | \$ 5.95                               |
| 30%              | 2,974,522                   | \$7.57                               | \$7.23                          | \$2.17                            | 100.00%      | \$5.90                                | 0.00%         | \$9.40                            | \$5.90                                |
| 40%              | 3,966,030                   | \$7.57                               | \$7.23                          | \$2.17                            | 100.00%      | \$5.83                                | 0.00%         | \$9.40                            | \$5.83                                |
| 50%              | 4,957,537                   | \$7.57                               | \$7.23                          | \$2.17                            | 100.00%      | \$5.77                                | 0.00%         | \$9.40                            | \$5.77                                |
| 60%              | 5,949,045                   | \$7.57                               | \$7.23                          | \$2.17                            | 100.00%      | \$5.69                                | 0.00%         | \$9.40                            | \$5.69                                |
| 70%              | 6,940,552                   | \$7.57                               | \$7.23                          | \$2.17                            | 100.00%      | \$5.61                                | 0.00%         | \$9.40                            | \$5.61                                |
| 80%              | 7,932,060                   | \$7.57                               | \$7.23                          | \$2.17                            | 100.00%      | \$5.53                                | 0.00%         | \$9.40                            | \$5.53                                |
| 90%              | 8,923,567                   | \$7.57                               | \$7.23                          | \$2.17                            | 100.00%      | \$5.43                                | 0.00%         | \$9.40                            | \$5.43                                |
| 100%             | 9,915,075                   | \$7.57                               | \$7.23                          | \$2.17                            | 100.00%      | \$5.33                                | 0.00%         | \$9.40                            | \$5.33                                |
| 100%             | 10,906,582                  | \$7.57                               | \$7.23                          | \$2.17                            | 90.91%       | \$5.33                                | 9.09%         | \$9.03                            | \$5.33                                |
| 100%             | 11,898,090                  | \$7.57                               | \$7.23                          | \$2.17                            | 83.33%       | \$5.33                                | 16.67%        | \$8.72                            | \$5.33                                |
| 100%             | 12,889,597                  | \$7.57                               | \$7.23                          | \$2.17                            | 76.92%       | \$5.33                                | 23.08%        | \$8.46                            | \$5.33                                |
| 100%             | 13,881,105                  | \$7.57                               | \$7.23                          | \$2.17                            | 71.43%       | \$5.33                                | 28.57%        | \$8.24                            | \$5.33                                |
| 100%             | 14,268,606                  | \$7.57                               | \$7.23                          | \$2.17                            | 69.49%       | \$5.33                                | 30.51%        | \$8.16                            | \$5.33                                |

**4. Mr Brian Boyd is the largest investor in PAYCE (non-Participating Shareholders' perspective)**

Mr Brian Boyd and his associated entities currently have a 38.74% equity interest in PAYCE, making him PAYCE's largest shareholder. Mr Brian Boyd and his associated entities will hold 49.75% of the equity interest in PAYCE assuming full participation in the Buy-back.

In practical terms, if the voting power of entities associated with Mr Boyd increases, his associated entities will have a potentially greater capacity to influence the voting results of resolutions which may be considered by PAYCE Shareholders in the future (by voting for or against such resolutions). Such resolutions could include, for example, resolutions to appoint or remove directors, to amend the constitution of PAYCE, or to increase or decrease the number of shares on issue. Under the Corporations Act entities associated with Mr Boyd would be excluded from voting on resolutions where Mr Boyd or those associated entities may benefit from it or are affected by it.

Any resolutions which could be considered by PAYCE Shareholders in the future would require the approval of a minimum of 50% of total votes cast by Shareholders entitled to vote on the resolution. As noted above, Mr Brian Boyd and his associated entities will hold 49.75% of the equity interest in PAYCE assuming full participation in the Buy-back.

Mr Brian Boyd has been the Managing Director of PAYCE for over 25 years, and has over 32 years' experience in the property development industry. The independent Directors consider him to be a proactive and experienced property developer and businessman, and therefore a significant and consequently a desired investor in PAYCE.

The independent Directors also believe that the implications of Mr Boyd's associated entities increasing their percentage shareholding in PAYCE will not have a material impact on the direction of PAYCE because Mr Boyd, through associated entities, has historically held a significant interest in



PAYCE. My Boyd has advised the independent Directors that he does not intend to use any increased voting power that may be obtained through his associated entities following the Buy-Back to significantly change PAYCE's principal business of undertaking property development projects.

In any event, the actual effect of the Buy-back on the relative concentration of shareholdings and potential control of the Company will not be known until the transaction is completed, as it is unknown to what extent individual Shareholders will participate in the Buy-back.

5. *Buy-back Consideration is Fair (Participating Shareholders' perspective)*

We have formed the view that the Buy-back is fair in the context that the value of the consideration being offered, which we assess as in the range of between \$8.16 and \$9.40 per Ordinary Share, is greater than the value of PAYCE shares on a controlling basis as it is greater than our assessment of the fair value of PAYCE Ordinary Shares prior to the Buy-back of \$7.57 per Ordinary Share. If 70% or less of eligible Ordinary Shares accept into the Buy-back all accepting shares will receive an assessed value of \$9.40 per Ordinary Share. If 100% of eligible Ordinary Shares accept into the Buy-back, each accepting share will receive \$8.16 per share in our assessed value. Depending on the level of acceptance, the total value for Shareholders accepting the Buy-back will be equivalent to assessed value of between \$8.16 per share and \$9.40 per share.

6. *Opportunity to Exit in an Efficient Manner (Participating Shareholders' perspective)*

Historically, PAYCE's Ordinary Shares have been thinly traded on the ASX. The Buy-back provides Shareholders with an opportunity to sell their Ordinary Shares in an efficient and cost effective manner, in consideration for a combination of a cash payment and Preference Shares which carry a discretionary Dividend.

The Buy-back also allows Shareholders to sell a relatively large volume of Ordinary Shares without depressing the market price of Ordinary Shares, and in circumstances where the market for the Ordinary Shares may not otherwise be sufficiently liquid to accommodate such volume.

7. *Dividends on Preference Shares (Participating Shareholders' perspective)*

Historically, PAYCE's Shareholders had only received dividends twice over the past 10 years. By participating in the Buy-back, Shareholders may, at the discretion of PAYCE, receive scheduled quarterly Dividends on their Preference Shares.

8. *Priority of Dividends (Participating Shareholders' perspective)*

Preference Shares receive priority to Ordinary Shares in the receipt of dividends.

9. *Priority in a Winding Up (Participating Shareholders' perspective)*

Preference Shares receive priority to Ordinary Shares in the event of a winding up.





## Disadvantages

### 1. Concentration of shareholding (non-Participating Shareholders' perspective)

The effect of the Buy-back on the relative concentration of shareholdings and potential control of the Company will not be known until the transaction is completed, as it is unknown to what extent individual Shareholders will participate in the Buy-back.

Individual non-participating shareholders other than Mr Brian Boyd will bear the consequences of a blocking stake in PAYCE as a result of the significant influence exercised by Mr Brian Boyd and may therefore forfeit the opportunity to realise a control value in the future. Furthermore, Mr Brian Boyd and his associates may further consolidate their position by purchasing other shares on-market through the 'creep' provisions of the Corporations Act.

### 2. Reduction in the free float and liquidity of shares (non-Participating Shareholders' perspective)

If the Buy-back is approved, the shares tendered under the Buy-back will be transferred to the Company and cancelled in accordance with the Corporations Act. Upon completion of the Buy-back and subsequent cancellation of the shares, the total issued capital of PAYCE may be substantially reduced by up to 33.3%.

The reduction in the free float and potential effect upon trading liquidity may limit PAYCE shares' attractiveness to institutional investors as it may affect their ability to readily realise large parcels of shares without impacting the share price. This may have the potential to cause a downward re-rating of the PAYCE shares by these investors.

### 3. Impact on Voting (Participating and non-Participating Shareholders' perspective)

Depending on the level of participation by Shareholders in the Buy-Back, the voting power of entities associated with Mr Boyd may increase, giving his associated entities a potentially greater capacity to influence the voting results of resolutions which may be considered by PAYCE Shareholders in the future (by voting for or against such resolutions). Examples of such resolutions could include to appoint or remove directors, to amend the constitution of PAYCE, or to increase or decrease the number of shares on issue. Under the Corporations Act entities associated with Mr Boyd would be excluded from voting on resolutions where Mr Boyd or those associated entities may benefit from it or are affected by it.

Any resolutions which could be considered by PAYCE Shareholders in the future would require the approval of a minimum of 50% of total votes cast by Shareholders entitled to vote on the resolution. As Mr Boyd will ensure that, following the Buy-Back, his associated entities will hold less than 50% of the total Ordinary Shares on issue irrespective of the level of participation in the Buy-Back, these entities will not be able to control the results of any resolution, but could have a substantial influence on the outcome of any resolution.

### 4. Preference Share Risks (Participating Shareholders' perspective)

The Preference Shares are a significant part of the value to be received for those accepting the Buy-back. The features and risks associated with the Preference Shares are set out in detail in Section 1.3 and the disadvantages of the Preference Share features in this section under the heading Disadvantages. Shareholders should clearly understand the features and risks of these shares





before making a decision. We have taken the features and risks of the Preference Shares into account when determining our discount factor of 10.25% to arrive at a fair market value of \$7.23 for the Preference Shares.

5. *Liquidity of Preference Shares (Participating Shareholders' perspective)*

It is assumed the Preference Shares will not be listed on any formal secondary market in which they could be sold.

6. *Market Price of Preference Shares (Participating Shareholders' perspective)*

The price at which Preference Shareholders will be able to sell the Preference Shares is uncertain and there will only be a market in the event that the requirements of an authorised exchange are able to be met after the issue of the Preference Shares.

7. *Dividend is Uncertain (Participating Shareholders' perspective)*

Scheduled Dividends of the Preference Shares are uncertain and subject to Directors' discretion at the time as to whether a dividend is declared and the timing of payments. Additionally, Dividends can be paid via the issue of further Preference Shares at the discretion of Directors.

8. *PAYCE's Option to Repurchase (Participating Shareholders' perspective)*

PAYCE has the option to buy-back Preference Shares at their issued price. Therefore, Preference Shareholders could be unable to realise any appreciation of market price of their Preference Shares if in the case of increased market value of those shares.

9. *Potential Risk of Delisting (non-Participating Shareholders' perspective)*

Potential consequences of the reduction of Ordinary Shares issued include further thin trading and more concentration in holdings of the largest substantial Shareholders. The lack of liquidity and spread increases the risk of PAYCE's Ordinary Shares being delisted by the ASX.

10. *No Voting Rights on Company Matters (Participating Shareholders' perspective)*

Ordinary Shareholders accepting the Buy-back will be exchanging Ordinary Shares with voting rights for cash and Preference Shares with no voting rights, except in relation to issues that directly affect the Preference Shares.

11. *Taxation (Participating Shareholders' perspective)*

The Buy-back price of \$9.80 includes a component of deemed unfranked dividends for taxation purposes, being \$8.26 per Ordinary Share. No franking credits are to be utilised in relation to the Buy-back. It is possible that Shareholders, who participate in the Buy-back, may have an income tax liability that exceeds the cash component of the Buy-back price. It is recommended that Shareholders seek independent taxation advice.



## Summary of advantages and disadvantages

In the context of the above analysis, the table below presents a summary of the main advantages and disadvantages for Non Associated Shareholders who participate in the Buy-back and for Non Associated Shareholders who do not participate in the Buy-back:

|                      | <b>Participation Scenario (from Participating Non Associated Shareholders' perspective)</b>  | <b>Non-Participation Scenario (from non-Participating Non Associated Shareholders' Perspective)</b>   |
|----------------------|--|---|
| <b>Advantages</b>    | <ul style="list-style-type: none"> <li>▪ The Buy-back is not compulsory. Non Associated Shareholders will be able to choose whether to participate in the Buy-back having regard to their individual circumstances.</li> <li>▪ At low levels of participation in the Buy-back, Non-Associated Shareholders may be able to exit their entire investment in Ordinary Shares in PAYCE at a 24.2% premium to fair market value of PAYCE (on a control basis) and at a 69.7% premium to recent trading prices</li> <li>▪ Non Associated Shareholders will have the ability to wholly or partially reduce their holding in PAYCE, should they desire to.</li> <li>▪ Buy-back consideration is assessed as fair</li> <li>▪ Participating Shareholders may receive scheduled quarterly Dividends on Preference Shares at the discretion of PAYCE. These dividends rank in priority to Ordinary Shares.</li> <li>▪ Preference Shares receive priority in a winding up.</li> </ul> | <ul style="list-style-type: none"> <li>▪ Potential value accretion for PAYCE shares which continue to be held</li> <li>▪ Potential for future growth in PAYCE with the Managing Director Mr Brian Boyd having a controlling shareholding</li> </ul>       |
| <b>Disadvantages</b> | <ul style="list-style-type: none"> <li>▪ Adverse impact on share ownership control and voting power</li> <li>▪ At high levels of participation in the Buy-back, Shareholders who wish to exit their entire investment in Ordinary Shares would retain residual shares of up to 30% of</li> </ul>   | <ul style="list-style-type: none"> <li>▪ Adverse impact on share ownership control and voting power</li> <li>▪ Reduced liquidity of Ordinary Shares due to reduced number of Ordinary Shares on issue.</li> <li>▪ Potential risk of de-listing</li> </ul> |



|  |  |  |
|--|--|--|
|  | <p>their current shares in PAYCE</p> <ul style="list-style-type: none"><li>▪ The value received for the Buy-back is part cash and part Preference Shares in PAYCE, which have risks associated with them</li><li>▪ No liquid market for Preference Shares</li><li>▪ Dividends on Preference Shares are uncertain</li><li>▪ PAYCE could re-purchase Preference Shares prior to any appreciation of market price</li><li>▪ Preference Shares have reduced voting rights</li><li>▪ Potential income tax liability</li></ul> |  |
|--|--|--|

### **Other Matters**

Each Shareholders' decision in relation to the Buy-back offer will be influenced by their particular circumstances. In undertaking our assessment, we have considered the Buy-back offer from the perspective of PAYCE's Non Associated Shareholders as a whole. HCCF has not considered the effect of the Buy-back offer or the circumstances, objectives, financial situation or needs of individual securities holders as it is not practicable to consider the implications on individual Shareholders as their circumstances are unknown to HCCF. HCCF has prepared a Financial Services Guide as required by the *Corporations Act 2001*. This is included as Part 2 to our Report.

This letter is a summary of HCCF's valuation extracted from our Independent Expert's Report. Our respective valuations are as at 20 February 2015, and reflect the circumstances and conditions as at that date.

### **Conclusion**

We have assessed the Buy-back to be fair and reasonable to the participating Non Associated Shareholders. In forming this view, we have concluded that the value to participating shareholders is greater than the fair value of a PAYCE share on a control basis and that the advantages of the Buy-back to participating Non Associated Shareholders outweigh the disadvantages.

Yours faithfully,  
Hanrick Curran Corporate Finance Pty Ltd

Alex Fraser  
Director and Representative



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## **Part 2 - Financial Services Guide**



## **1 INTRODUCTION**

### **1.1 Background to the Off-market Equal Access Share Buy-back**

By Notice of Extraordinary General Meeting (Notice) dated 2 April 2015, PAYCE Consolidated Limited ("the Company") advised that as part of PAYCE's capital management strategies it would offer Shareholders the opportunity to participate in an equal access off-market share Buy-back. If approved, the equal access off-market Buy-back would allow those Shareholders who wanted to reduce their holding of Ordinary Shares the ability to do so:

- in consideration for cash and Preference Shares; and
- in light of the illiquidity of PAYCE's shares, providing that opportunity without placing downwards pressure on the Company's share price.

The proposed off market Buy-back is subject to:

- (i) Shareholder approval for an equal access Buy-back of up to 9,915,075 issued Ordinary Shares in PAYCE; and
- (ii) Shareholder approval to issue up to 9,915,075 Preference Shares in partial consideration for the Buy-back proposal, conditional upon approval of (i).

The Resolutions to accomplish the above are to be put to an Extraordinary General Meeting of Shareholders on 4 May, 2015 and the Notice is to be accompanied by an Independent Expert's Report.

### **1.2 Terms of the Buy-back and Issue of Preference Shares**

The terms of the Buy-back proposal are described in full in the Explanatory Statement accompanying the Notice. The following summary outlines key points associated with the proposal.

PAYCE is preparing an off market equal access Buy-back, of up to 9,915,075 Ordinary Shares, representing one third of all issued Ordinary Shares.

For Shareholders participating in the Buy-back, the consideration for the Buy-back would be satisfied by a contribution of cash and Preference Shares, as follows:

For each Ordinary Share participating in the Buy-back the overall consideration comprises:

- \$0.80 per share cash paid upon cancellation of the Ordinary Shares participating in the Buy-back;
- \$0.80 per share cash paid 12 months after the cancellation of the Ordinary Shares participating in the Buy-back (second payment);
- \$0.70 per share cash paid 18 months after the cancellation of the Ordinary Shares participating in the Buy-back (third payment);
- A Preference Share issued (with an issue price of \$7.50) upon cancellation of the Ordinary Share and having an assessed fair market value of \$7.23.





In addition, once the Buy-back has been undertaken, Shareholders will continue to hold their remaining Ordinary Shares which will then have an assessed fair market value of between \$5.33 and \$6.06 (depending on the level of scale back).

The Buy-back offer will be subject to a scale back so that, in the event of acceptance by Shareholders exceeding the maximum limit of 9,915,075 Ordinary Shares, the scale back will proportionally reduce acceptances so that no more than the maximum number of Ordinary Shares are subject to the Buy-back.

### **1.3 Risks Associated with Preference Shares**

There are specific risks which relate directly to the business of PAYCE. In addition, there are other general risks, many of which are largely beyond the control of PAYCE and its Directors. The risks identified in this section, may have a material impact on the value of the Preference Shares.

#### **1.3.1 Illiquidity**

The Preference Shares will not be quoted on an exchange. Accordingly, it is possible that there will be an illiquid market for the Preference Shares.

#### **1.3.2 Dividends may not be paid**

There is a risk that dividends on the Preference Shares will not be paid. The terms of issue of the Preference Shares do not require PAYCE to pay dividends. The payment of dividends is subject to the satisfaction of a number of requirements, including among other things that the Directors, at their absolute discretion, resolve to declare and pay a dividend. There is a risk that a dividend may not be paid in full or at all. Under the terms of the Preference Shares, failure to pay a dividend when scheduled will not constitute an event of default in respect of the Preference Shares. In the event that PAYCE does not pay a dividend when scheduled, a Preference Shareholder:

- has no right to apply for PAYCE to be wound up or placed in administration, or to cause a receiver or a receiver and manager to be appointed in respect of PAYCE, merely on the grounds it does not or may become unable to pay a dividend when scheduled; and
- will have no right of set-off and no off-setting rights or claims on PAYCE under the terms of the Preference Shares.

If PAYCE does not pay a dividend in full on a dividend payment date, then the 'Dividend Payment Restriction' applies to PAYCE unless certain steps are taken to pay dividends to the Preference Shareholders.

Dividends are cumulative. If a scheduled dividend is not paid on the relevant dividend payment date, PAYCE must pay an amount equal to the unpaid dividends if it exercises its option to buy-back the Preference Shares.



### **1.3.3 Dividends may not be paid in cash**

There is a risk that Dividends will be declared but paid as additional Preference Shares. The terms of issue of the Preference Shares do not require PAYCE to pay dividends solely as cash. The issuance of further Preference Shares as consideration for dividends may further expose Preference Shareholders to risk.

### **1.3.4 Call option may not be exercised**

Under the Terms of Issue of the Preference Shares, PAYCE is not required to exercise its option to purchase or buy-back the Preference Shares for a cash consideration of \$7.50 each on any dividend payment date. There is a risk that PAYCE will never exercise its powers under this call option.

### **1.3.5 Risks associated with exchange and conversion**

There is a risk that, in the event that PAYCE breaches the Dividend Payment Restriction, and fails to rectify such breach within 90 days, that it will not exchange the Preference Shares for Redeemable Preference Shares as required in accordance with the Terms of Issue of the Preference Shares.

Even if the Preference Shares are exchanged for Redeemable Preference Shares in accordance with the Terms of Issue, there is no guarantee that PAYCE will be able to fund the redemption of those Redeemable Preference Shares in accordance with the Terms of Issue.

### **1.3.6 Restrictions on rights and ranking in a winding-up**

The Preference Shares are unsecured and not guaranteed.

In the event of a winding-up of PAYCE, Preference Shareholders will have a preference in terms of dividends and the return of any capital ahead of Ordinary Shares, but will have no entitlement to share in any surplus in the event of a winding-up.

### **1.3.7 Future issues by PAYCE**

The Terms of Issue of the Preference Shares do not in any way restrict PAYCE from issuing further securities (except where a Dividend Payment Restriction exists) or from incurring further indebtedness.

PAYCE's obligations under the Preference Shares will rank subordinate and junior in a winding-up to PAYCE's obligations to holders of senior ranking securities and instruments, and all creditors. Accordingly, PAYCE's obligations under the Preference Shares will not be satisfied unless it can satisfy in full all of its obligations ranking senior to the Preference Shares.

In addition, PAYCE may in the future issue securities which:

- rank for dividends or payments of capital equal with, behind or ahead of the Preference Shares;
- have the same or different dividend, interest or distribution rates as those for the Preference Shares;



- have the same or different terms and conditions as the Preference Shares.

PAYCE may incur further indebtedness and may issue further securities including Preference Shares before, during or after the issue of these Preference Shares.

An investment in the Preference Shares carries no right to participate in any future issue of securities, whether equity preference shares, debt or otherwise, by PAYCE.

An investment in Preference Shares carries no right to be redeemed or otherwise repaid at the same time as PAYCE redeems or otherwise repays other securities, whether equity, shares, debt or otherwise.

#### **1.3.8 Dividends may not be franked**

There is no obligation for PAYCE to pay franked dividends.

#### **1.3.9 Amendment of Terms of Issue of the Preference Shares**

PAYCE may amend the Terms of Issue of the Preference Shares without the approval of Preference Shareholders, where such amendments are necessary or desirable amendments which the Directors consider are not likely to be materially prejudicial to the interests of Preference Shareholders as a whole. PAYCE may also amend the Terms of Issue of the Preference Shares if the amendment has been approved by a special resolution of Preference Shareholders.

### **1.4 Intentions of the Directors and Major Shareholders**

As detailed in the Explanatory Statement accompanying the Notice, PAYCE's largest Shareholder is Lanox Pty Ltd which is associated with Mr Brian Boyd, the Company's Managing Director.

Mr Brian Boyd has indicated that Lanox Pty Ltd (which holds 8,806,799 Ordinary Shares) will not participate in the Buy-back; but that Ruz Pty Ltd another entity which is associated with Mr Brian Boyd and holds 2,718,661 Ordinary Shares will participate in the Buy-back to the extent of 1,660,000 shares. Mr Brian Boyd and his associates hold 38.747% of the Ordinary Shares prior to the Buy-back. Mr Boyd and his associates will hold a maximum of 49.75% of the Ordinary Shares after the Buy-back.

Mr Brian Boyd and the entities associated with him, being Lanox Pty Ltd and Ruz Pty Ltd are excluded from voting on the Resolutions to be put to the Meeting.

Jurocorp Pty Ltd, an entity associated with another Director, Mr Roger Short, will be participating in the Buy-back to the extent of 40,000 shares.

The second largest substantial shareholder is Mr Garry Boyd. Mr Garry Boyd has indicated to the Independent Directors that he and his associates' intention is to participate in the Buy-back up to the extent of 5,586,158 shares, which is 50 percent of the Ordinary Shares held by him and his associates.



## **2 SCOPE OF THIS REPORT**

### **2.1 Purpose of this Report**

Hanrick Curran Corporate Finance Pty Ltd ("HCCF") has been appointed by the independent Directors of PAYCE to prepare an Independent Expert's Report ("Report" or "IER") in relation to the Buy-back expressing our opinion as to whether the Buy-back is fair and reasonable to those Shareholders of PAYCE not associated with Managing Director Mr Brian Boyd (Non Associated Shareholders). The intentions of the two largest substantial Shareholders of PAYCE and those associated with them and with the Directors are known. The intentions of all other Shareholders are not known. The purpose of our Report is to assist Non Associated Shareholders in their deliberations on whether to approve the Buy-back (which includes consideration by way of the issue of Preference Shares) and the extent to which Shareholders might participate therein.

### **2.2 Requirements for the Independent Expert's Report**

This Report has been prepared to meet the following regulatory requirements:

#### **2.2.1 Section 257A of the Corporations Act**

Share Buy-backs are controlled by Division 2 of part 25.1 of the Corporations Act 2001. Section 257A of the Corporations Act authorises an Australian company to Buy-back its own shares if the Buy-back does not materially prejudice the company's ability to pay its creditors and it follows the procedures set out in Division 2 of Part 25.1 of the Corporations Act. That Division permits a company to conduct an equal access Buy-back scheme if each of the following conditions set out in subsection 257B(2) is satisfied:

- (a) The offers under the scheme relate only to Ordinary Shares;
- (b) The offers are to be made to every person who holds Ordinary Shares to buy-back the same percentage of their Ordinary Shares;
- (c) All of those persons have a reasonable opportunity to accept the offers made to them;
- (d) Buy-back agreements are not entered into until a specified time for acceptances of offers has closed; and
- (e) The terms of all the offers are the same.

An equal access Buy-back for in excess of 10% of the smallest number of votes attaching to the voting shares during the last 12 months also requires Shareholder approval under section 257C of the Corporations Act by an ordinary resolution. PAYCE currently has 29,745,225 Ordinary Shares on issue. The equal access Buy-back offer is in respect of 9,915,075 or 33.33% of all Ordinary Shares. In accordance with section 257C therefore the Company must obtain approval by a resolution at a general meeting, and the Company must lodge with the Australian Securities and Investments Commission ("ASIC") a copy of the Notice of Meeting and all supporting information, which will include in part this Report.



In addition we note:

- that Preference Shares are offered in part consideration of the Buy-back; and
- the issue of Preference Shares by the Company requires a special resolution by Shareholders, under section 254A(2), and that resolution is also to be presented at the same Extraordinary Meeting.

### **2.2.2 Australian Securities and Investment Commission**

ASIC Regulatory Guide 110: *Share Buy-backs* ("RG110") requires information to be disclosed to Shareholders involved in or affected by share buy-backs. RG110.18 provides that if a company proposes to buy-back a significant percentage of shares or the holdings of a significant Shareholder, it should consider providing:

- a report by its independent directors about whether Shareholders should vote in favour of the Buy-back, particularly regarding how much the company is paying for the shares; and
- an independent expert's report with a valuation of the shares.

In addition, ASIC Regulatory Guide 111: *Content of expert reports* ("RG111") provides guidance regarding the preparation of independent expert's reports and the information which should be provided to Shareholders. Whilst, RG111 does not provide specific guidance in relation to Buy-backs it does provide specific guidance as to control transactions. Mr Brian Boyd and his associates currently hold 38.747% of the Ordinary Shares. After the Buy-back Mr Brian Boyd and his associates will hold a maximum of 49.75% of the Ordinary Shares. The Buy-back therefore is a control transaction and in accordance with RG111 we have valued the Ordinary Shares pre transaction on a control basis.

Under RG110 'if a company proposes to buy back a significant percentage of shares or the holding of a major shareholder, it should consider providing [...] an independent expert's report with a valuation of the shares'. However we understand that there is no compulsory requirement for an independent expert's report in relation to the Buy-back. Notwithstanding this, the Independent Directors of PAYCE have requested HCCF to prepare an independent expert's report expressing our opinion as to whether the Buy-back is fair and reasonable to those Shareholders of PAYCE not associated with Mr Brian Boyd (the Non Associated Shareholders).

Notwithstanding that RG 110 recommends the provision of independent advice from an expert in relation to a proposed buy-back, it does not provide specific guidance on how to form an opinion, or the factors to consider in forming such an opinion.

Given the lack of specific guidance within RG 110, in considering the approach to adopt with respect to the evaluation of the proposed Buy-back we have considered the ASX Listing Rules, ASIC Regulatory Guidance, the Corporations Act and common market practice.

This report has also been prepared to assist Non Associated Shareholders in their assessment of whether to approve or participate in the Buy-back. In order to assist Non Associated Shareholders in their assessment, we have prepared a valuation of PAYCE pre transaction on a control basis and following the Buy-back on a minority basis.



## 2.3 Basis for Valuation

Consistent with RG110, the Independent Directors of PAYCE have requested us to prepare an IER in relation to the Buy-back, the purpose of which is to provide:

- a valuation of PAYCE's Ordinary Shares before the off-market equal access Buy-back;
- a valuation of the Preference shares offered in consideration for each PAYCE share;
- a comparison of the consideration offered (cash and Preference Shares) for the Ordinary Shares which are the subject of the Buy-back;
- an analysis of the advantages and disadvantages of the Buy-back in order to assess whether the offer is reasonable including a comparison of the consideration which Non Associated Shareholders are expected to receive in each of the following scenarios:
  - (a) for Non Associated Shareholders who participate fully in the Buy-back offer;
  - (b) for Non Associated Shareholders who participate partially in the Buy-back offer; and
  - (c) for Non Associated Shareholders who do not participate at all in the Buy-back offer;
- and
- an assessment of whether the Buy-back is fair and reasonable to Non Associated Shareholders.

Our valuation has been prepared on a control basis to provide Non Associated Shareholders with an estimate of the fair market value of a PAYCE Ordinary Share assuming 100% ownership of the Company. Our valuation takes into account PAYCE's current operations and capital structure, and does not reflect the impact of the off market Buy-back proposal. However, in our assessment of the advantages and disadvantages of each of the three possible scenarios, we have simulated the impact of the three scenarios at various levels of participation in the Buy-back on our valuation to provide Non Associated Shareholders with an indication of the range of overall consideration that may be expected.

The appropriate basis of valuation for IER purposes is 'fair value' which is generally defined in Australia as:

*"the price at which an asset could be exchanged between a knowledgeable and willing but not anxious seller and a knowledgeable and willing but not anxious buyer both acting at arm's length".*

Our assessment of the fair value of a PAYCE Ordinary Share has been undertaken on a basis consistent with this definition.

The Buy-back in PAYCE represents 33.3% of the issued share capital of the Company. Mr Brian Boyd and his associates currently hold 38.747% of the Ordinary Shares. After the Buy-back Mr Brian Boyd and his associates will hold a maximum of 49.75% of the Ordinary Shares. The Buy-back therefore is a control transaction and in accordance with RG111 we have valued the Ordinary Shares pre transaction on a control basis.

RG111 provides guidelines, for the purpose of reports relating to takeover offers or change of control transactions, in determining whether a proposed transaction is fair and reasonable. Pursuant to RG 111 fairness relates to price, whereas reasonableness includes the consideration of factors other than price.



Having considered these various sources, we consider it appropriate to assess whether the Buy-back is fair and reasonable to Non Associated Shareholders having regard to the advantages and disadvantages, so far as Non Associated Shareholders are concerned, of the Buy-back noting that there are different options available to Non Associated Shareholders. In considering these matters we have amongst other things, compared the consideration being received by Shareholders for the Buy-back shares with our estimate of the fair market value of the Buy-back consideration and the fair value of the Non Associated Shareholders Ordinary Shares in PAYCE before the Buy-back on a control basis and after the Buy-back on a minority basis.

The additional complexity to be taken into account in each Non Associated Shareholder's decision process is that the more appealing the Buy-back is assessed to be by Non Associated Shareholders, the higher the expected overall level of participation and, consequently, the greater the risk that the Buy-back will be fully utilised so that up to 30% of shares accepted into the Buy-back by each Non Associated Shareholder will not be bought back by PAYCE. This would result in Non Associated Shareholders retaining up to 30% of their Ordinary Shares in PAYCE.

### **2.3.1 Professional Standards**

This Report has been prepared in accordance with APES 225: Valuation Services ("APES 225") issued by the Accounting Professional & Ethical Standards Board Limited in respect of valuation engagements. In accordance with APES 225, we have performed a Valuation Engagement, which is defined as *"an engagement where the valuer is free to choose the valuation approaches, methods and procedures as appropriate to the circumstances. The estimate of value that results in a conclusion of value"*.

We provide our valuation of PAYCE Ordinary Shares in Section 5 of this Report. In Section 6 we consider the valuation of the Preference Shares and in Section 9 we consider the advantages and disadvantages of the Buy-back.

## **2.4 PAYCE Shareholder Decisions**

This Report constitutes general financial product advice only and has been prepared without taking into consideration the individual circumstances of PAYCE Shareholders. The decision as to whether to approve the Buy-back is a matter for consideration by individual Shareholders.

Shareholders should consider the advice in the context of their own circumstances and preferences and if in doubt as to what action to take, they should consult their own financial adviser.

It should be noted that our Report is to be provided to Shareholders to assist them in their assessment of whether to approve or participate in the Buy-back. The Report has not been prepared for, and does not contain any opinion or advice to, PAYCE Shareholders as to whether they should vote in favour or against the proposed resolutions or to sell their PAYCE shares into the Buy-back. It is not possible or practicable for us to consider the impact of the Buy-back on individual Shareholders as many factors may impact on each Shareholder and ultimately the decision of each, including their own financial circumstances, risk profiles, liquidity circumstances, investment strategies and tax positions.





Accordingly, we have prepared a Financial Services Guide in accordance with the Corporations Act 2001 which is included as Part 2 to this Report.

## **2.5 Independence**

Prior to accepting this engagement, we considered our independence with respect to PAYCE with reference to ASIC Regulatory Guide 112: *Independence of experts*. In our opinion, we are independent of PAYCE.

HCCF, and global affiliations, have not provided any services to PAYCE in relation to this Buy-back except for the preparation of this Report. HCCF has no involvement with, or interest in, the outcome of the proposed buy-back other than that of Independent Expert. HCCF is entitled to receive a fee based on commercial rates for the preparation of this Report. Except for those fees, HCCF will receive no other benefit in connection with the issue of this Report. In particular, payment of our fees is not contingent in any way on the success or failure of the proposed Buy-back.

## **2.6 Limitations and reliance on information**

In the preparation of this Report, HCCF was provided with information in respect of PAYCE which is set out in Appendix B.

Our opinion is based on economic, market and other external conditions prevailing at the date of this Report. These conditions can change over relatively short periods of time and these changes can be material.

Our Report is also based upon financial and other information provided by PAYCE in relation to the Buy-back. HCCF has considered and relied upon this information. PAYCE has represented to HCCF that to its knowledge the information provided is correct and that there are no material facts which have been omitted.

The information provided to HCCF has been evaluated through analysis, enquiry and review for the purposes of assisting Shareholders in their deliberation of whether to approve the Buy-back. However, HCCF does not warrant that its enquiries have identified all of the matters that an audit and extensive examination might disclose.

Preparation of this Report does not imply that we have, in any way, audited or conducted an audit review of the financial statements of PAYCE. It is understood that the accounting information that was provided was prepared in accordance with generally accepted accounting principles and Australian equivalents to International Financial Reporting Standards as applicable.

In forming our opinion we have also assumed that:

- Matters such as title, compliance with laws and regulations and contracts in place are in good standing and will remain so, and that there are no material legal proceedings, other than as publicly disclosed;
- The information set out in the Notice to be sent by PAYCE to its Shareholders is complete, accurate and fairly presented in all material aspects;





- The publicly available information relied upon by HCCF in its analysis was accurate and not misleading; and
- The Buy-back will be implemented in accordance with its terms.

To the extent that there are legal issues relating to assets, properties, or business interests or issues relating to compliance with applicable laws, regulations and policies, we assume no responsibility and offer no legal opinion or interpretation on any issue.

The statements and opinion given in this Report are given in good faith and in the belief that such statements and opinions are not false or misleading. This Report should be read in the context of the full qualifications, limitations and consents set out in Appendix C of this Report.

We provided draft copies of this Report to the Independent Directors and management of PAYCE for their comments as to factual accuracy, as opposed to opinions, which are the responsibility of us alone. Amendments made as a result of the review by the Independent Directors and management of PAYCE have not changed the methodology or conclusions reached by HCCF.



## **3 OVERVIEW OF PAYCE**

### **3.1 Company Background**

PAYCE Consolidated Limited (ABN 19 001 566 310) ("PAYCE") which has been listed on the Australian Securities Exchange (ASX) since 1978 is the holding company of a property development group. Its business model focuses on high quality medium density apartment and mixed use (residential/retail/commercial) product and urban renewal projects. It assesses appropriate development opportunities in New South Wales and Queensland.

Since 2002, PAYCE has successfully delivered and sold more than 2,500 high quality residential apartments across Sydney. From its existing portfolio, PAYCE aims to deliver over 7,500 apartments or units over the next five years at Riverwood, Ermington, Kirrawee, Wentworth Point, Auburn and Melrose Park in Sydney NSW, and West End in Brisbane QLD.

PAYCE focuses on providing new, affordable, high quality products, and is committed to building sustainable and vibrant communities. It is supported by a highly experienced management team.

PAYCE aims to be Australia's leading provider of high quality residential and mixed use development product. It intends to continue to acquire and develop property in accordance with a disciplined development timetable and the execution of a financially secure business model.

### **3.2 Executive Team**

#### **3.2.1 Directors**

##### **Brian Boyd – Chairman and Managing Director**

Brian has over 32 years' experience in the property development industry. He brings a wealth of commercial experience and knowledge to development projects. Through his associates he is a substantial shareholder of PAYCE.

Brian was previously a director in Paynter Dixon, a construction company with over 90 years of operations. He was also previously a director of Santa Sabina College in Sydney, where he held the position of chairman of its property committee.

##### **Roger Short – Non-executive Director**

Roger was appointed a non-executive independent director in 1996. He practised as a lawyer for over 33 years, involved in large scale property development projects and commercial and public infrastructure, retiring from practice with McCullough Robertson in 2005.

He has been a director of public companies for more than 26 years and continues to be involved in company governance in the construction and infrastructure industries.

Roger is a member of the PAYCE audit committee.



### **Chris Gabriel – Non-executive Director**

Chris was appointed as a non-executive independent director in 2010. He brings substantial knowledge to PAYCE from over 30 years of advisory, accounting and tax experience to mid-tier businesses across a broad spectrum of industries.

Chris has been a fellow of Chartered Accountants Australia and New Zealand since 1973. He has been a principal in practice since 1976, and is a registered company auditor.

Chris is a member of the PAYCE audit committee.

## **3.2.2 Senior Management**

### **Brian Bailison – Chief Financial Officer and Company Secretary**

Brian has over 15 years' experience in finance, corporate finance and operations from senior roles in listed and unlisted businesses in South Africa and Australia, including Rand Merchant Bank Limited and the Ivany Investment Group.

Brian holds Bachelor of Commerce and Bachelor of Accounting (Cum Laude) degrees from the University of Witwatersrand and is a member Chartered Accountants Australia and New Zealand. He is also a non-executive director of G8 Education Limited, an ASX listed child care operator.

### **Dominic Sullivan – General Manager**

Dominic has nearly 20 years' experience spanning both the public and private sectors in property, legal, commercial and public roles. He is a former commercial lawyer with the Crown Solicitors Office, and also served as Mayor of Randwick City for 6 years. He holds Bachelor of Laws (Hons) and Bachelor of Arts (Hons) degrees.

Dominic has extensive experience in property development, approvals and transactions, as well as in corporate affairs across a number of property sectors, including residential, retail and child care.

Dominic has been with PAYCE since 2004, and has been involved in a number of PAYCE investments and projects across residential and commercial developments, including its flagship mixed use development at Wentworth Point, as well as PAYCE's major housing renewal project with the New South Wales government at Riverwood, Sydney.

*(All information on the company background and executive was sourced from PAYCE Management)*



### 3.3 Financial Information

The financial position of PAYCE as at 31 December 2014 and 30 June 2014 and 30 June 2013 is summarised in the tables below. The audited financial statements for 30 June 2013 and 30 June 2014 are available on the ASX website together with the reviewed financial statements for 31 December 2014.

| <b>PAYCE CONSOLIDATED LIMITED<br/>STATEMENT OF FINANCIAL POSITION<br/>AS AT 31 DECEMBER 2014</b> | <b>Dec-14</b>  | <b>Jun-14</b>  | <b>Jun-13</b>  |
|--|----------------|----------------|----------------|
|  | <b>\$'000</b>  | <b>\$'000</b>  | <b>\$,000</b>  |
| <b>Current Assets</b>  |                |                |                |
| Cash and cash equivalents  | 27,008         | 25,769         | 24,911         |
| Trade and other receivables  | 8,720          | 14,303         | 19,092         |
| Properties held for development and resale   | 89,413         | 216,818        | 0              |
| Investments accounted for using the equity method  | 3,467          | 0              | 0              |
| Other assets   | 5,557          | 7,526          | 4,149          |
| <b>Total Current Assets</b>  | <b>134,165</b> | <b>264,416</b> | <b>48,152</b>  |
| <b>Non-Current Assets</b>  |                |                |                |
| Trade and other receivables  | 19,140         | 9,873          | 2,262          |
| Properties held for development and resale   | 223,885        | 202,807        | 124,349        |
| Investments accounted for using the equity method  | 1,549          | 19,480         | 19,489         |
| Investment property  | 235,000        | 0              | 0              |
| Property, plant and equipment  | 6,999          | 6,269          | 376            |
| Financial assets   | 1,022          | 2,310          | 2,263          |
| Deferred tax asset   | 0              | 13,195         | 11,724         |
| Other assets   | 5,190          | 8,858          | 8,846          |
| <b>Total Non-Current Assets</b>  | <b>492,785</b> | <b>262,792</b> | <b>169,309</b> |
| <b>Total Assets</b>  | <b>626,950</b> | <b>527,208</b> | <b>217,461</b> |
| <b>Current Liabilities</b>   |                |                |                |
| Trade and other payables   | 21,493         | 30,293         | 13,473         |
| Financial liabilities  | 111,512        | 222,276        | 15,664         |
| Short-term provisions  | 1,033          | 986            | 802            |
| <b>Total Current Liabilities</b>   | <b>134,038</b> | <b>253,555</b> | <b>29,939</b>  |



| <b>PAYCE CONSOLIDATED LIMITED<br/>STATEMENT OF FINANCIAL POSITION<br/>AS AT 31 DECEMBER 2014</b> | <b>Dec-14<br/>\$'000</b> | <b>Jun-14<br/>\$'000</b> | <b>Jun 13<br/>\$'000</b> |
|--|--------------------------|--------------------------|--------------------------|
| <b>Non-Current Liabilities</b>   |                          |                          |                          |
| Financial liabilities  | 247,322                  | 132,875                  | 46,379                   |
| Derivative financial liabilities   | 5,532                    | 0                        | 0                        |
| Long-term provisions   | 53                       | 50                       | 40                       |
| Deferred tax liability   | 28,542                   | 7,080                    | 5,133                    |
| <b>Total Non-Current Liabilities</b>   | <b>281,449</b>           | <b>140,005</b>           | <b>51,912</b>            |
| <b>Total Liabilities</b>   | <b>415,487</b>           | <b>393,560</b>           | <b>81,851</b>            |
| <b>Net Assets</b>  | <b>211,463</b>           | <b>133,648</b>           | <b>135,610</b>           |
| <b>Equity</b>  |                          |                          |                          |
| Issued capital   | 45,382                   | 45,382                   | 45,382                   |
| Reserves   | 2,042                    | 2,042                    | 1,756                    |
| Retained earnings  | 160,462                  | 83,756                   | 85,172                   |
| <b>Parent interest</b>   | <b>207,886</b>           | <b>131,180</b>           | <b>132,310</b>           |
| Minority equity interest   | 3,577                    | 2,468                    | 3,300                    |
| <b>Total Equity</b>  | <b>211,463</b>           | <b>133,648</b>           | <b>135,610</b>           |

Source: PAYCE audited and reviewed financial statements

We note that in relation to PAYCE's financial performance in recent periods that the \$77.8m net increase in total equity between 30 June 2014 and 31 December 2014 is primarily due to the completion of the East Village project of which the retail/commercial component has been retained and reclassified as investment property during the period. The movements between current assets and non-current assets relates to the same change. The PAYCE Statement of Financial Position over the three accounting periods show significant growth in net assets and total equity due to the finalisation of the East Village and other projects.



| Consolidated Statement of Comprehensive Income    |          | Half year to<br>Dec 2014 | 30 June<br>2014 | 30 June<br>2013 |
|---|----------|--------------------------|-----------------|-----------------|
| Continuing Operations                             | Note     | \$,000                   | \$,000          | \$,000          |
| Revenue   |          | 234,610                  | 57,018          | 152,169         |
| Cost of sales                                     |          | (175,946)                | (36,606)        | (115,167)       |
| <b>Gross Profit</b>                               | <b>1</b> | <b>58,664</b>            | <b>20,412</b>   | <b>37,002</b>   |
| Other income                                      |          | 61                       | 818             | 205             |
| Gain on fair value of investment property         | <b>2</b> | 67,203                   | 0               | 0               |
| Administration expenses                           | <b>3</b> | (7,467)                  | (9,835)         | (5,606)         |
| Property expenses                                 | <b>3</b> | (1,333)                  | (1,005)         | (708)           |
| Marketing expenses                                | <b>3</b> | (6,942)                  | (5,879)         | (6,196)         |
| Impairment of available for sale financial assets | <b>4</b> | (1,000)                  | -               | -               |
| Total expenses excluding net financing income     |          | (16,742)                 | (16,719)        | (12,510)        |
| <b>Result from operating activities</b>           |          | <b>109,186</b>           | <b>4,511</b>    | <b>24,697</b>   |
| Finance income                                    | <b>5</b> | 1,834                    | 1,489           | 2,258           |
| Finance costs                                     | <b>6</b> | (5,880)                  | (3,821)         | (1,829)         |
| Loss on fair value of derivative instrument       | <b>7</b> | (5,532)                  | 0               | 0               |
| Net financing (expense) / income                  |          | (9,578)                  | (2,332)         | 429             |
| Share of profits of equity accounted investments  | <b>8</b> | 21,455                   | (144)           | 450             |
| Profit before income tax                          |          | 121,063                  | 2,035           | 25,576          |
| Income tax expense                                | <b>9</b> | (34,656)                 | (476)           | (6,554)         |
| <b>Profit for the period</b>                      |          | <b>86,407</b>            | <b>1,559</b>    | <b>19,022</b>   |

**Source: PAYCE audited and reviewed financial statements for 30 June 2013, 30 June 2014 and 31 December 2014**

**Note 1** – Recognition of revenue and cost of sales in a property development company typically occurs with the settlement of a project in each financial period. As such PAYCE's Gross Profit varies from year to year dependent on the timing of project completions. 2013 Revenue and cost of sales relates to contributions from the settlement of the 153 unit APEX project and the sale of a 50% joint venture interest in the Lot 3 project to Sekisui House. 2014 Revenue and cost of sales includes the sale of 50% joint venture interests to Sekisui House in the Ermington, SOPA Ferry Terminal and West End projects. The half-year to December 2014 Revenue and Cost of sales relates to contributions from the settlement of the 206 residential units at East Village and the sale of Hurstville land during the period.

**Note 2** – The gain on fair value of investment property reflects the Fair Market Value adjustment to the retained East Village retail/commercial asset, which is the \$235m Balance Sheet investment property asset.

**Note 3** – Administration expenses have increased due to the administration, property and marketing expenses over the past 2 ½ years increasing proportionally to the increasing size and activity of the PAYCE group and its various projects including relative increases in employee remuneration, head count, office and other administrative expenses.



**Note 4** – The impairment of available for sale financial assets reflects the Fair-Market-Value adjustment to financial assets held by PAYCE at 31 December 2014.

**Note 5** – Finance income is generally generated from interest earned on cash balances and deposits held. Deposit rates have declined over the periods reflected above.

**Note 6** – Finance costs expensed on the profit & loss statement reflects finance costs associated with non-project related liabilities and have increased from 30 June 2014 year due to the issue of \$50m PAYCE corporate Notes and the coupon payments made on those corporate Notes as well as from finance costs associated with the recent refinance of the East Village facility.

**Note 7** – This fair value loss on derivative instrument relates directly to the mark-to-market loss accrued on the interest rate swap arrangement associated with the East Village debt facility.

**Note 8** - Share of profits of equity accounted investments has been immaterial in prior years, but in the half-year to 31 December 2014 reflects PAYCE's share of profits recognised for its 50% interest in the recently completed and settled 322 unit Platinum project.

**Note 9** – Income tax expense reflects the tax accrual for deferred tax in each relevant financial period at the prevailing tax rate and adjusted for known and recognisable timing differences.



### 3.4 Capital Structure and Shareholders

#### 3.4.1 Ordinary Shares

There are 29,745,225 Ordinary Shares on issue. The top 10 Shareholders and their relevant holding percentages are listed below:

| Shareholder                      | No. of Shares     | % of share capital |
|----------------------------------|-------------------|--------------------|
| Lanox Pty Ltd                    | 8,806,799         | 29.607             |
| Lianshare Pty Limited            | 5,200,000         | 17.482             |
| Hurlcla Pty Limited              | 4,063,794         | 13.662             |
| Ruz Pty Limited                  | 2,718,661         | 9.140              |
| CRB Superannuation Pty Limited   | 2,481,339         | 8.342              |
| KMSJ Pty Ltd                     | 1,607,573         | 5.405              |
| Matzel Pty Ltd                   | 750,000           | 2.521              |
| Coetibus Investments Pty Ltd     | 750,000           | 2.521              |
| Tzferes Pty Ltd                  | 750,000           | 2.521              |
| Netzachem Pty Ltd                | 750,000           | 2.521              |
| <b>Total top 10 Shareholders</b> | <b>27,878,712</b> | <b>93.723%</b>     |

We are advised that the three substantial Shareholders (including holdings by their associated entities) are:

| Substantial Shareholder | No. of Shares | % of share capital |
|-------------------------|---------------|--------------------|
| Brian Boyd              | 11,525,460    | 38.747             |
| Garry Boyd              | 11,172,317    | 37.560             |
| Colleen Boyd            | 2,509,183     | 8.436              |

Total percentage holdings of the top 10 Shareholders represent 93.723% of the total share capital. Relevant total percentage holding for the top three substantial holders is 84.743% which indicates that PAYCE shares are relatively closely held with limited free float.

Mr Brian Boyd is not associated with the other substantial Shareholders.





### 3.5 Share Price Performance

The below chart of monthly prices over the past 5 years for PAYCE is extracted from the ASX:



Source: ASX

PAYCE's share price appreciated from approximately \$1.50 to over \$5.55 during the past 5 years. One share traded at \$7.90 in February 2015. This trade has been disregarded as it did not represent a marketable parcel.

The 45 day volume weighted average price at 20 February 2015, being the Valuation Date, was \$5.54.

### 3.6 Dividend History

PAYCE declared two dividends during the past 10 years:

| Payment Date  | Dividend per share | Franking  |
|---------------|--------------------|-----------|
| 28 March 2013 | \$0.1000           | Unfranked |
| 20 March 2014 | \$0.1000           | Unfranked |

### 3.7 Corporate Debt

PAYCE issued \$50 million senior secured notes on 3 December 2013 ("Corporate Notes" or "Notes"). The Notes have a 5 year term, maturing in December 2018. They pay a fixed quarterly coupon at 9.5% per annum.



The valuation of the mark-to-market value of the Notes is included in Section 5.4.5 of this Report.

### **3.8 Project Debt**

Each property development is funded by a mixture of equity (either by PAYCE or in conjunction with a joint venture partner) and project related finance. Project debt is typically non-recourse.



## **4 VALUATION METHODOLOGY AND APPROACH – PAYCE**

### **4.1 Valuation Methodologies**

To estimate the fair market value of the shares in PAYCE we have considered common market practice and the valuation methodologies recommended by RG 111, which provides guidance in respect of the content of independent expert's reports. These are discussed below.

#### **Market based methods**

Market based methods estimate a company's fair market value by considering the market price of transactions in its shares or the market value of comparable companies. Market based methods include:

- capitalisation of maintainable earnings;
- analysis of a company's recent share trading history; and
- industry specific methods.

The capitalisation of maintainable earnings method estimates fair market value based on the company's future maintainable earnings and an appropriate earnings multiple. An appropriate earnings multiple is derived from market transactions involving comparable companies. The capitalisation of maintainable earnings method is appropriate where the company's earnings are relatively stable.

The most recent share trading history provides evidence of the fair market value of the shares in a company where they are publicly traded in an informed and liquid market.

Industry specific methods estimate market value using rules of thumb for a particular industry. Generally rules of thumb provide less persuasive evidence of the market value of a company than other valuation methods because they may not account for company specific factors.

#### **Discounted cash flow methods**

Discounted cash flow methods (DCF) estimate market value by discounting a company's future cash flows to a net present value. These methods are appropriate where a projection of future cash flows can be made with a reasonable degree of confidence. Discounted cash flow methods are commonly used to value early stage companies or projects with a finite life.

#### **Asset based methods**

Asset based methods estimate the market value of a company's shares based on the realisable value of its identifiable net assets. Asset based methods include:

- orderly realisation of assets method
- liquidation of assets method
- net assets on a going concern basis.

The orderly realisation of assets method estimates fair market value by determining the amount that would be distributed to security holders, after payment of all liabilities including realisation costs and taxation charges that arise, assuming the company is wound up in an orderly manner.

The liquidation method is similar to the orderly realisation of assets method except the liquidation method assumes the assets are sold in a shorter time frame. Since wind up or liquidation of the



company may not be contemplated, these methods in their strictest form may not necessarily be appropriate.

The net assets on a going concern basis method estimates the market values of the net assets of a company but does not take account of realisation costs.

We have also adopted a DCF analysis, based on 7 years cash flow projections prepared by PAYCE's management. Our DCF analysis was used as a secondary valuation approach given the significant development component assumed cash flow projections and the relative level of uncertainty over achieving these cash flows.

## 4.2 Assessment of Fair Market Value

For the purposes of Non Associated Shareholders' assessment of the Buy-back we have assessed the fair market value of a share in PAYCE on a control basis at \$7.57. To enable Non Associated Shareholders to make an informed assessment of whether to approve or participate in the Buy-back we have also valued the Ordinary Shares following the Buy-back. We have assessed the valuation range for this purpose on a minority basis to be between \$5.33 and \$6.06 per share depending on the level of acceptance. We have assessed the value of a PAYCE Ordinary Share on a 'fair value' basis, with fair value generally being defined as:

*"the price at which an asset could be exchanged between a knowledgeable and willing but not anxious seller and a knowledgeable and willing but not anxious buyer both acting at arm's length".*

## 4.3 Valuation Approach

In considering the fair value of PAYCE Ordinary Shares and for the purposes of this Report, we have adopted the net realisable value of assets methodology as our primary approach.

In adopting this methodology, we have considered the following key issues:

- PAYCE is a company which is primarily involved in property development focused on residential units in Sydney and more recently the development of a mixed-use site in West End, Brisbane.
- The portfolio of properties is relatively small.
- The Company develops properties within the constraints of its resources.
- Cash flows occur at the time of settlement either upon stage or development completion. Accordingly, cash flows are irregular and can vary considerably. To help mitigate such risks, developments generally commence with substantial or entire pre-sales of commitments on each project.
- PAYCE generally acquires property (either alone or in joint venture) and then seeks to create value by changing the zoning/permitted use of that property, then proceeds to complete the project development. Whilst there is skill in undertaking this process, both the risk and timeframe create considerable uncertainty as to the value of future cash flows where the project portfolio is relatively small.
- Many of the properties have been valued (refer Appendix J). The values attributable to the particular property by the property valuers concerned have been based on the expected cash flows relevant to those properties, once the cash flows, timeframes and risks can be



determined with sufficient accuracy. In other words, once the required approvals are in place and development has commenced. Where this is not the case, the value of the property has generally been referenced to the acquisition cost adjusted (reduced) to remove transaction costs and assessed impairment, if any.

These asset based methods ignore the possibility that the company's value could exceed the realisable value of its assets as they ignore the value of intangible assets such as customer lists, management, supply arrangements and goodwill. Asset based methods are appropriate for companies where, a significant proportion of a company's assets are liquid, or for asset holding companies as is the case with PAYCE.

#### **4.4 Analysis of Valuation Methodologies**

The value of PAYCE ordinary shares on a control basis has been assessed to be \$7.57. This is in our opinion, fair market value, being the amount at which the PAYCE shares will change hands between a knowledgeable willing buyer and a knowledgeable willing seller and assumes a hypothetical change of control transaction.

In order to test the primary valuation methodology we have undertaken two valuation cross-checks. As noted in Regulatory Guide 111 cross-check methodology is to be used to reduce the risk that our opinion as Independent Expert may be distorted by the choice of methodology.

The two cross-check methodologies utilized by us to test our primary valuation methodology were a comparison to share trading and an assessment of value on a discounted cash flow basis.

Both the share trading and DCF methodologies are materially less than our assessment of fair value. The share trading valuation based on the PAYCE 45 day VWAP is \$5.54 which is 36.6% discount to our assessed fair market value of \$7.57. The trading volume over the last three years collectively represent less than 5% of the shares on issue. Whilst utilizing share trading as a cross-check valuation, we have not relied on this as a determinant of fair market value due to the thin nature of the trading over the last three years therefore not being representative of fair market value.

Separately we have undertaken discounted cash flow analysis. The value per share on a control basis is \$6.20 per share. Whilst useful as a cross-check, we have excluded the DCF value from our assessment of fair-market value as the methodology is extremely sensitive to relatively small changes in underlying assumptions, a few of which are incapable of being predicted with accuracy particularly beyond the first two or three years, and whilst useful as a cross-check have formed the opinion that it should not be determinative.

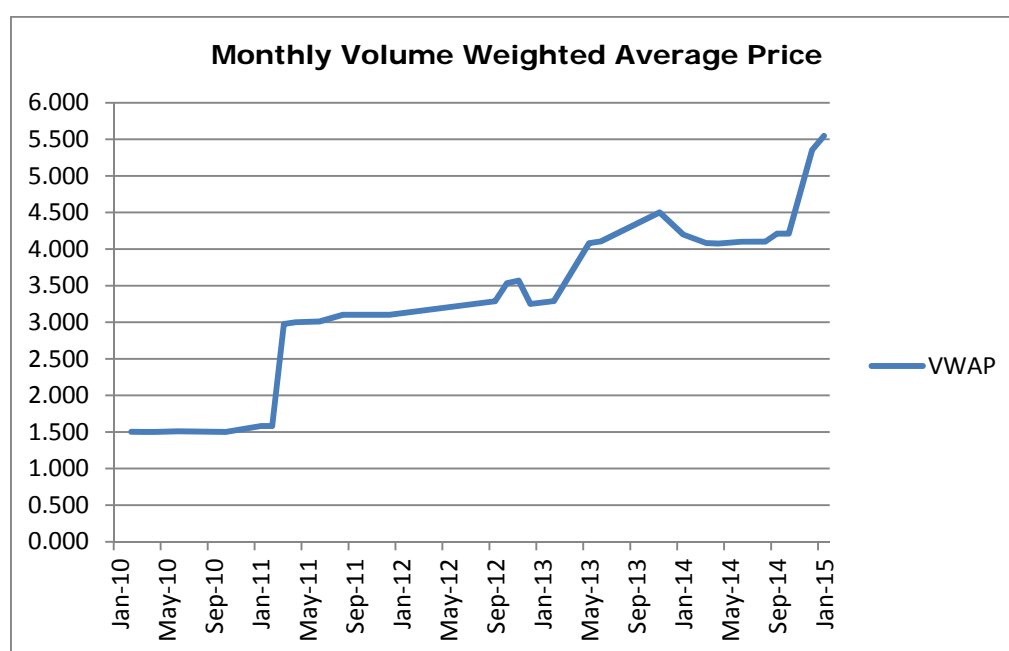


## 5 VALUATION OF PAYCE

### 5.1 Trading Price History of PAYCE Shares

#### 5.1.1 Share Prices

The following graph shows the monthly Volume Weighted Average Price (VWAP) of PAYCE shares over the last 5 years of \$2.49 per PAYCE share:



Source: Hanrick Curran Corporate Finance

In addition, we note the share price range (low – high) for each of those years as follows:

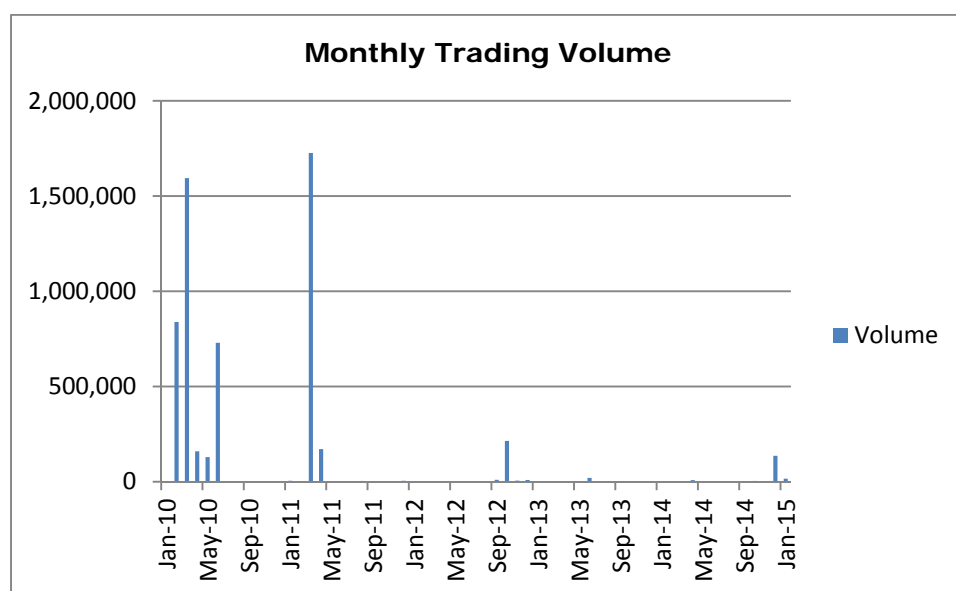
| Calendar<br>Year | Share Price |       |
|------------------|-------------|-------|
|                  | Low         | High  |
| 2010             | 1.000       | 1.580 |
| 2011             | 1.580       | 3.100 |
| 2012             | 3.100       | 3.700 |
| 2013             | 3.250       | 4.500 |
| 2014             | 4.070       | 6.000 |
| 2015 - Jan       | 5.500       | 5.550 |

The Volume Weighted Average Price of PAYCE shares for the 45 days ending 20 February 2015 (Valuation Date) was \$5.54.



### 5.1.2 Trading Volumes – PAYCE Shares

In the graph below, we show the total volume of PAYCE shares traded on a monthly basis over the past 5 years:



## 5.2 Liquidity of PAYCE Shares

Based on the above monthly trading volume together with the spread between the buy/sell price which is currently \$5.00/\$7.90, it is clear that PAYCE shares constitute an illiquid stock. As a result the share price may not reflect the value that may be determined in a more liquid market for PAYCE shares.

## 5.3 Control Premium

When an entity is fully owned by a single shareholder, that shareholder clearly exercises control over the entity. Control generally occurs where a shareholder has 50.1% of the voting rights, but can occur at shareholdings of less than 50%. Mr Brian Boyd and his associates hold 38.75% of the Ordinary Shares prior to the Buy-back. Mr Brian Boyd and his associates will hold a maximum of 49.75% of the Ordinary Shares after the Buy-back.

Various studies (refer to appendix K for recent studies) indicate that:

- Value premiums for control tend to range between 25% and 40% of price with the median for all GICS sectors (2001 to 2014) being 30%.
- Control premiums for illiquid stocks are at the upper end of the control premium.
- Control premiums for property entities are at the lower end of the range. However the GICS categories are broad and include Australian Real Estate Investment Trusts, AREIT's (which generally have a smaller control premium) in the property category.



As detailed in section 3.4.1, Mr Brian Boyd and his associated entities currently own 11,525,460 shares or 38.747% of the Ordinary Share Capital in PAYCE. The maximum number of Ordinary Shares that will be cancelled as a result of the Buy-back is 9,915,075. The table below summarises the top 20 Shareholders together with the balance of Shareholders and the percentage ownership for each:

| <b>Held by</b>              | <b>No of Shares</b> | <b>% held</b> |
|-----------------------------|---------------------|---------------|
| Brian Boyd and Associates   | 11,525,460          | 38.75         |
| Garry Boyd and Associates   | 11,172,317          | 37.56         |
| Colleen Boyd and Associates | 2,509,183           | 8.44          |
| Other top 20 Shareholders   | 3,909,234           | 13.14         |
| Balance of Shareholders     | 629,031             | 2.11          |

A small number of Shareholders control PAYCE. Neither Mr Brian Boyd nor his associates are participating in the Buy-back except to the extent of 1,660,000 shares held by Ruz Pty Ltd. Accordingly, after the Buy-back Mr Brian Boyd will have voting rights to the extent of 9,865,460 shares or 49.75% of issued capital of PAYCE (assuming all 9,915,075 shares are bought back and there is no scale back).

Mr Brian Boyd is the managing director of PAYCE.

PAYCE is an illiquid stock which based on our analysis is undervalued on the ASX. There is a \$2.90 difference (currently) between the buy/sell offers which would only be exacerbated if a significant number of shares were offered for sale.

In addition we note that should the proposed Buy-back proceed the value of shares either on a control or minority basis will likely be reduced for the continuing Shareholders.

The control premium which will be received by Non Associated Shareholders accepting the Buy-back is 24.2%, if 70% or less of the eligible Ordinary Shares participate in the Buy-back. If 100% of the eligible Shareholders participate in the Buy-back the value of the position post Buy-back is 7.8% greater than the value on a control basis of \$7.57 at \$8.16 per ordinary share. Non Associated Shareholders not accepting the Buy-back will continue to hold Ordinary Shares valued at between \$5.33 and \$6.06.

## **5.4 Valuation of PAYCE**

### **5.4.1 Introduction and Summary Conclusions**

For the purposes of Non Associated Shareholders' assessment of the Buy-back, we have estimated the fair market value of a share in PAYCE on a control basis to be \$7.57 prior to the Buy-back.

In order to allow Shareholders to make an informed assessment of whether to approve or participate in the Buy-back, we have also valued the shares following the Buy-back on a minority basis. We have assessed the valuation range for this purpose to be between \$5.33 and \$6.06 per share (assuming various levels of Buy-back as detailed in Section 8.1).





#### 5.4.2 Valuation of the Major Operating Assets of PAYCE

The assets held by PAYCE at 31 December 2014 consist of:

- Property Development Assets held either solely by PAYCE or in joint venture;
- Investment Property Assets; and
- Other assets.

We detail on Appendix J, all property assets held by PAYCE on 20 February 2015, together with the basis of valuation of each of those assets, which form the basis of our valuation of PAYCE's shares as at the date of this Report.

In summary we reviewed and considered:

- (a) the independent valuations prepared for the purposes of assessing fair market value; and
- (b) the contracts for the purchase of the asset and for those assets being developed any additional capitalised development & construction costs;

Further,

- we held discussions with management in respect of any changes to any property to indicate any increases or decreases to valuations or purchase costs / capitalised costs to reflect current value;
- were provided with a reconciliation of these asset values to the financial statements of PAYCE for the six months ended 31 December 2014; and
- conducted a physical inspection of most property assets.

In reviewing the independent valuations we note that:

- (a) the definition of fair market value as per each of the valuation reports was consistent with the definition of fair value within this Report;
- (b) the valuers are large, respectable firms who prima facie have the capability to undertake the relevant valuation being Colliers International, Landmark White and m3property and each valuer has been approved by PAYCE's financiers as a panel valuer for their purposes;
- (c) the valuations appear competently prepared and based on reasonable assumptions and metrics and were in each instance assessing current market value; and
- (d) With the exception of Apex Retail which is immaterial in the context of this report, all other valuations have been undertaken in the last 12 months and generally within the last 6 months. In particular East Village (which approximates 38% of the property assets) was independently valued on 22 October 2014, once it was completed, and Kirrawee (23% of the property assets) on 5 February 2015.

Accordingly and in our opinion, the independent valuations undertaken by specialist property valuers are reasonable for the purposes of this Report.



The table below sets out a summary of the estimated Net Asset Valuations less associated liabilities:

| Asset Class                | Reference  | \$'000         |
|----------------------------|------------|----------------|
| Property Developments      | Appendix J | 209,503        |
| Investment Properties      | Appendix J | 102,256        |
| Other Assets / Liabilities | 5.4.3      | (86,493)       |
| <b>Total</b>               |            | <b>225,266</b> |

In determining the value of shares in PAYCE, we also considered whether there should be a premium or discount of those shares compared to PAYCE's net asset value (NAV) or net tangible assets (NTA). NAV's and NTA's are two common valuation metrics of A-REITs. NTA is based on the underlying book value of assets whereas NAV is based on the expected cash flows from the property assets, together with other income generating assets.

<sup>1</sup> As at 31 October 2013 A-REIT's were trading at a premium to NTA of around 23% and a discount to NAV of 1.5% partly reflecting the expected upward movement in book values of assets when re-valued as compared to a NAV reflective of underlying cash flows.

As 31 December 2014 A-REITs were trading at (discount) / premium range to NTA of (36%) to 42% (with outliers beyond this range). <sup>2</sup> Typically however most A-REITs were trading at a premium of 15% - 30% to NTA.

The major property assets of PAYCE are stated at contract price, recent valuation (e.g. Kirrawee), based on the underlying cash flows of the investment asset as assessed in a recent valuation (e.g. East Village) or is in the process of development (e.g. Riverwood). PAYCE's property assets have been determined on the basis of NAV. Whilst it may be argued that there is valuation upside in assets under development, those assets represent a small proportion of the overall property assets (7.4%) and in our opinion does not warrant adjusting the overall property portfolio to reflect any premium or discount.

<sup>1</sup> Source: UBS

<sup>2</sup> Source: ASX

### Synopsis of Underlying Properties held by PAYCE

Set out below is a synopsis of the underlying properties held by PAYCE. The table describes both the current and intended zoning (if applicable), proposed development, and valuation details. This information has been taken into consideration by HCCF, in conjunction with other relevant details, in order to determine a valuation of PAYCE.

| Property description       | Location                                  | Land area | Planning   | Use                       | PAYCE interest | Basis of Valuation |
|----------------------------|---|-----------|--|---------------------------|----------------|--------------------|
| Marshall Street, Bankstown | 18-24 Marshall Street, Bankstown NSW 2200 | 4,200sqm  | Zoned R4 High Density Residential.<br>DA Approved.<br>Subject to a put | 60 residential apartments | 100%           | Put & Call Option  |



| Property description                 | Location                                       | Land area      | Planning   | Use  | PAYCE interest | Basis of Valuation                                  |
|--------------------------------------|--|----------------|--|--|----------------|---|
|                                      |  |                | and call contract for sale to a third party.   |  |                |   |
| Rasmussen, Townsville                | Lots 27 & 61 Allambie Lane, Rasmussen QLD 4815 | 255.6 hectares | Currently zoned for Rural uses.<br><br>Subject to a Material Change of Use (MCU) application to permit residential uses. | Land lot subdivision   | 100%           | Contract Price                                      |
| Riverwood, Pennsylvania Avenue       | 17-21 Pennsylvania Avenue, Riverwood NSW 2210  | 3,025sqm       | Zoned R4 High Density Residential.<br><br>Early Planning stage – development application to be prepared.                 | Approximately 30 residential apartments  | 100%           | Contract Price                                      |
| Riverwood – Como                     | 3-7 Washington Avenue, Riverwood NSW 2210      | 4,550sqm       | Zoned R4 High Density Residential.<br><br>DA approved, 100% pre-sold, under construction, completion in 2015             | 197 residential apartments   | 100%           | Independent Valuation + subsequent development Cost |
| Riverwood – Fairmont                 | 1 Vermont Crescent, Riverwood NSW 2210         | 5,150sqm       | Zoned R4 High Density Residential.<br><br>DA approved, 100% pre-sold, under construction, completion in 2015             | 192 residential apartments   | 100%           | Independent Valuation + subsequent development Cost |
| Kirrawee – South Village, Sutherland | 566-594 Princes Highway, Kirrawee NSW 2232     | 42,540sqm      | Zoned part B4 Mixed Use and part RE1 Public Recreation.<br><br>Concept Plan approval for 85,000sqm mixed-use development | Currently vacant with preliminary site works in progress.<br><br>Concept Approval is for a mixed | 100%           | Independent valuation                               |



| Property description            | Location                                      | Land area     | Planning  | Use   | PAYCE interest | Basis of Valuation |
|---------------------------------|---|---------------|---|---|----------------|--------------------|
|                                 |   |               | plus open space<br>Development application to be lodged.  | use retail/commercial and residential development, together with associated public open space yielding 749 units and 14,190sqm of retail floor space.                     |                |                    |
| Melrose Park                    | 84 Wharf Road, Melrose Park NSW 2114          | 16.3 hectares | Currently zoned IN1 Industrial. Subject to a rezoning to permit a mixed-used development.   | Current uses comprise older-style industrial warehouses and offices.<br><br>Subject to a future application, rezoning, the site will yield a large mixed-use development. | 50%            | Contract Price     |
| Sydney Olympic Park Ferry Wharf | Lot 1 Burroway Road, Wentworth Point NSW 2127 | 1.79 hectares | Zoned B1 Neighbourhood Centre. Forms part of the Sydney Olympic Park Master Plan.<br><br>DA approved for a mixed-use development. | Currently vacant. Upon completion will comprise 249 units plus ground floor retail/commercial.  | 50%            | Contract Price     |
| Platinum, Victoria Park         | 1 Hutchinson Walk, Zetland NSW                | 8,100sqm      | Project completed in December 2014.   | 322 residential apartments  | 50%            | Contract Price     |



| Property description | Location                                      | Land area     | Planning  | Use   | PAYCE interest | Basis of Valuation    |
|----------------------|---|---------------|---|---|----------------|-----------------------|
| 2017                 |   |               |   | .   |                |                       |
| Baulkham Hills       | Lot 17 Spurway Drive, Baulkham Hills NSW 2153 | 1.88 hectares | Zoned R3 Medium Density Residential. Development application currently being prepared and will be lodged in mid-2015. | Currently vacant. Upon completion will comprise 65 townhouse s.   | 60%            | Contract Price        |
| Auburn               | 300 Manchester Road, Auburn NSW 2144          | 14.12ha       | Currently zoned IN1 Industrial. Subject to a rezoning to permit a mixed-used development.                             | Current uses comprise industrial improvements on 50% of the site, with the other 50% vacant.<br><br>Subject to a future application, rezoning, the site will yield a large mixed-use development. | 60%            | Contract Price        |
| Castle Hill          | 300 Old Northern Road, Castle Hill NSW 2154   | 2.89 hectares | Zoned for Environmental Living.<br><br>DA approved for a large lot subdivision.                                       | 14 large land lots average 1,000sqm each.   | 100%           | Contract price        |
| Ermington            | Silverwater Road, Ermington NSW 2115          | 2.03 hectares | Zoned R4 High Density Residential.<br><br>DA approved with pre-sales campaign underway, completion due in 2016        | 612 residential apartments<br><br>.   | 50%            | Independent valuation |
| West End             | 93 Boundary Street, West                      | 2.56 hectares | Zoned Multi-Purpose Centre  | Current uses  | 50%            | Independent valuation |



| Property description      | Location                                       | Land area     | Planning  | Use  | PAYCE interest | Basis of Valuation    |
|---------------------------|--|---------------|---|--|----------------|-----------------------|
|                           | End QLD 4101                                   |               | MP2 – Major Centre and is subject to the Brisbane Riverside Neighbourhood Plan. Current zoning permits mixed-use development.<br><br>Development applications currently being prepared and will be lodged in mid-2015 with approval expected within 12 months thereafter. | comprise older style industrial warehouse/ factories and offices.<br><br>Upon completion the development will comprise circa 1,100 residential apartments and 10,000sqm retail/commercial. |                |                       |
| Bay Park, Wentworth Point | 23 Bennelong Parkway, Wentworth Point NSW 2127 | 2.56 hectares | Approved Concept Plan for 44,730sqm gross floor area. Currently seeking modification to Concept Plan approval to increase gross floor area.   | Current uses comprise an industrial warehouse subject to a lease expiring in 2015.<br><br>Circa 680 residential apartments upon completion.  | 50%            | Independent valuation |

A description of each of the properties is set out in more detail below:

### Development Properties

#### **Washington Park (Riverwood North) NSW**

Washington Park is a four staged residential development in Sydney's south west producing over 600 apartments. PAYCE has commenced construction of 389 units over the first two stages, called "Como" and "Fairmount", which are expected to be completed in 2015. Progress on the remaining 2 residential stages of the project is progressing with pre-sales and early-works having already commenced.



### **Rasmussen Townsville**

This land comprises 255 hectares of land currently zoned rural, situated at Beck Drive, Rasmussen in Townsville. The land is currently subject to an application for rezoning to residential..

### **Riverwood, Pennsylvania Avenue**

This vacant unimproved land, of approximately 3,000 square meters, is zoned for general residential uses.

### **Marshall St, Bankstown**

Site area of 4,200 square meters, has been recently approved for 60 residential apartments. The site is subject to a put and call contract for sale to a third party.

### **Kirrawee**

The Kirrawee development is situated on 4.2 hectares located on the previous Kirrawee Brick Pit Site in the Sutherland Shire of Sydney. The Company continues to progress the planning and pre-construction activities of a mixed use development, having recently received concept plan approval for up to 749 residential apartments and an open plaza retail of 14,190 square meters.

## **Joint Venture Owned Development Activities**

### **"Royal Shores", Ermington - Joint Venture with Sekisui House**

Royal Shores Ermington, located approximately 15km west of the Sydney CBD, is situated on a 2 hectare site located on the Parramatta River at Ermington. Pre-sales for the projects 612 residential dwellings commenced in late 2014 and construction is due to commence by mid-2015. PAYCE has a 50% economic interest in the project.

### **Melrose Park – Joint Venture with Sekisui House**

In August 2014, PAYCE, in joint venture, acquired two adjacent tenanted industrial sites, totalling 16 hectares, in Melrose Park, Sydney for \$118.5 million. PAYCE has a 50% economic interest in the project.

Long term development opportunities for the sites are currently being assessed.

### **Sydney Olympic Park Ferry Terminal, NSW - Joint Venture with Sekisui House**

This 1.8 hectare mixed use development, located at the Sydney Olympic Park Ferry Terminal, Wentworth Point will deliver up to 250 residential units with ground floor commercial/retail uses. Pre-sales for the project are expected to commence in the second quarter of 2015. The development application has been approved and project commencement is expected following completion of the pre-sale campaign. PAYCE has a 50% economic interest in the project.



#### **West End – Joint Venture with Sekisui House**

Encompasses a 2.6 hectare mixed-use residential and retail development located in South Brisbane to construct over 1,000 residential units and a 10,000 square meter retail precinct. The site was acquired for \$45 million in May 2014. The lodgement of a site master plan is expected to occur in the second quarter of 2015, with approval expected within 12 months thereafter. PAYCE has a 50% economic interest in the project.

#### **Bay Park, Wentworth Point (TNT Site) - Joint Venture with Sekisui House**

Bay Park is 2.6 hectare site (currently tenanted) located within the established "Waterfront" estate at Wentworth Point. Concept Plan approval for the development has been achieved and PAYCE continues to progress the planning and pre-construction activities of the project expected to include circa 680 residential apartments. PAYCE has a 50% economic interest in the project.

#### **Platinum, Victoria Park – Joint Venture with DASCO**

Development of the 322 residential unit 'Platinum' project was completed and settled (with profit recognition occurring) in December 2014 and January 2015. PAYCE has a 50% economic interest in the project.

#### **Auburn - Joint Venture with DASCO**

On 26 August 2014, PAYCE entered into a contract to acquire two adjacent industrial lots (totalling 14 hectares) located in Auburn for \$50 million. Settlement of this transaction occurred in February 2015. PAYCE has a 60% economic interest in the project.

The majority of the site is subject to a 5 year lease. Long term development opportunities for the sites are currently being assessed.

#### **Baulkham Hills - Joint Venture with DASCO**

In late 2014, PAYCE exchanged contracts to acquire, subject to sub-division, a 1.9 hectare site, located at Baulkham Hills. The site is currently zoned for medium density residential development. PAYCE is currently preparing a development application, to be lodged in mid-2015, for the construction of up to 65 residential townhouses. PAYCE has a 60% economic interest in the project.

#### **Castle Hill - Joint Venture with DASCO**

In late 2014, PAYCE acquired a 2.9 hectare site, located at Castle Hill, currently approved for 14 large residential lots. PAYCE are currently reviewing the existing approval. PAYCE has a 60% economic interest in the project.





## Investment Properties

### **East Village**

East Village is located in Zetland; 3km south of the Sydney CBD.

Development of the mixed use 'East Village' site has been completed, with settlement of the 206 residential units and opening of the commercial/retail centre (50 retail stores) having occurred in October 2014.

### **Apex Retail, Victoria Park**

450sqm of ground floor retail, located adjacent to East Village, currently being tenanted.

*(all information on the properties was sourced from PAYCE Management).*

## Joint Venture Agreements

The Company has joint ventures with:

- (a) Sekisui House;
- (b) Wingate; and
- (c) DASCO.

In respect of each of the properties, the subject of a joint venture, we have reviewed the variously titled constituent agreements. In addition we have discussed the agreements with management. Based on those reviews/discussions we are not aware of any clauses in the agreements which would impact on the fair market values of the property asset(s) held by each joint venture.

### **5.4.3 Surplus Assets, Overheads and Net Financial Debt**

We summarise below the surplus assets and net financial debt:

|                              | <b>Ref</b> | <b>\$,000</b>          |
|------------------------------|------------|------------------------|
| Net Financial Debt           | 5.4.7      | (26,992)               |
| Deferred Income Tax          |            |                        |
| Liability (DITL)             |            | (38,807)               |
| Other Assets / (Liabilities) |            | (20,694)               |
| <b>Total</b>                 |            | <b><u>(86,493)</u></b> |

### **5.4.4 Corporate Overheads**

Valuations based on net assets do not take into account the cost structure associated with a listed property vehicle. Based on projections which have been prepared by management and other budget information provided to us, operating expenses (net of project management fees) are estimated at \$954k per annum.



The investment assets of Apex Retail and East Village are independently managed. Accordingly, overhead costs essentially relate to value enhancements in respect of future and current projects and other general corporate expenses. It is also noted that a number of the potential value enhancements created by development activities are expected to offset the annual cost of corporate overheads in the future. Therefore whilst it is appropriate to consider corporate overheads, particularly as Non Associated Shareholders are not in a position to influence the corporate structure, we also considered it appropriate to adjust for such overheads when assessing the discount applicable to minority interest value of the shares they hold in PAYCE.

#### **5.4.5 Corporate Notes**

As detailed in Section 3.7 of this Report the Company has issued fixed rate Notes at a coupon rate of 9.5% with a face value of \$50m.

Between issue in December 2013 to 4 February 2015 there have been 145 trades amounting to \$42.7m. The trades are effected over the counter with the price being determined on a bid and acceptance basis.

On 4 February 2015 the price of the Notes determined on the above basis was \$1.08 - \$1.09. Accordingly in considering the value of the Notes we have adopted \$1.08 as the price of each Note. On this basis the Notes have a value of \$54m which we have used for the purposes of this Report.

#### **5.4.6 SWAPS**

In October 2014, PAYCE entered into two Swap arrangements with an Authorised Deposit-taking Institution. As of 31 January 2015, the two Swaps are in a net loss mark-to-market position of \$8,084,344.

##### **5.4.6.1 7 Year SWAP - \$110m**

PAYCE entered into this Swap arrangement to pay a fixed rate of 3.3750% on a \$110m face value effective from October 2014 to October 2021.

As of 31 January 2015, PAYCE's mark-to-market position on the Swap arrangement is a loss of \$5,739,740.

##### **5.4.6.2 5 Year SWAP - \$50m**

PAYCE entered into this Swap arrangement to pay a fixed rate of 3.6850% on a \$50m face value effective from December 2016 to October 2021.

As of 31 January 2015, PAYCE's mark-to-market position on the Swap arrangement is a loss of \$2,344,604.

For the purpose of this Report we have used the mark-to-market value of these Swaps in valuing those obligations.



#### 5.4.7 Net Financial Debt

PAYCE's net financial debt position as at 31 December 2014 is summarised below:

|                            | \$'000          |
|----------------------------|-----------------|
| Financial borrowings Notes | (54,000)        |
| Cash                       | 27,008          |
| <b>Net financial debt</b>  | <b>(26,992)</b> |

The above figures do not include specific borrowings secured by the development projects which have already been reflected in the nett value of each asset detailed on Appendix J and the mark-to-market adjustment of the Swaps which are included as other liabilities.

#### 5.5 Net Asset Value

We have assessed the value of PAYCE on a control basis using an asset based approach (Net Asset Value), recognising that PAYCE continues as a going concern.

In order to reflect the value of each share on a minority interest basis requires initially determining the premium for control. The minority interest discount is the inverse of the control premium (refer Appendix K for formula).

We attach in Appendix K details of recent control premium studies together with relevant minority interest discount formula and other issues which would give rise to an increased control premium.

The studies indicate that control premiums generally range between 25% - 40%, with the long term median typically around 30% - 35%. Within this range, property entities are generally at the lower end partly as a result of the influence of A-REIT's which generally have low control premiums.

#### 5.6 Reconciliation of PAYCE Statement of Financial Position

We set out below the PAYCE Statement of Financial Position together with our classification of each item into three categories being Development Assets, Investment Assets and Other to show the reconciled adjustments made to the audit reviewed half yearly balance sheet and the values applied by us in determining the net asset value of PAYCE in this report of \$225,226,000. Appendix J sets out additional detail in relation to adjustments to carrying values as at 31 December 2014 to our assessment of fair market value.

| STATEMENT OF FINANCIAL POSITION AS AT<br>31 DECEMBER 2014 | TOTAL<br>\$'000 | Development<br>Assets<br>\$'000 | Investment<br>Assets<br>\$'000 | Other<br>\$'000 |
|---|-----------------|---------------------------------|--------------------------------|-----------------|
| <b>Current Assets</b>                                     |                 |                                 |                                |                 |
| Cash and cash equivalents                                 | 27,008          |                                 |                                | 27,008          |
| Trade and other receivables                               | 8,720           |                                 |                                | 8,720           |
| Properties held for development and resale                | 89,413          | 89,413                          |                                | 0               |
| Investments accounted for using the equity method         | 3,467           | 3,467                           |                                | 0               |
| Other assets  | 5,557           | 4,234                           |                                | 1,323           |
| <b>Total Current Assets</b>                               | <b>134,165</b>  | <b>97,114</b>                   | <b>0</b>                       | <b>37,051</b>   |



| STATEMENT OF FINANCIAL POSITION AS AT<br>31 DECEMBER 2014     | TOTAL<br>\$'000 | Development<br>Assets<br>\$'000 | Investment<br>Assets<br>\$'000 | Other<br>\$'000 |
|---|-----------------|---------------------------------|--------------------------------|-----------------|
| <b>Non-Current Assets</b>                                     |                 |                                 |                                |                 |
| Trade and other receivables                                   | 19,140          | 17,245                          |                                | 1,895           |
| Properties held for development and resale                    | 223,885         | 221,724                         | 2,161                          | 0               |
| Investments accounted for using the equity method             | 1,549           | 1,549                           |                                | 0               |
| Investment property   | 235,000         |                                 | 235,000                        | 0               |
| Property, plant and equipment                                 | 6,999           |                                 |                                | 6,999           |
| Financial assets  | 1,022           |                                 |                                | 1,022           |
| Deferred tax asset  | 0               |                                 |                                | 0               |
| Other assets  | 5,190           | 2,892                           |                                | 2,298           |
| <b>Total Non-Current Assets</b>                               | <b>492,785</b>  | <b>243,410</b>                  | <b>237,161</b>                 | <b>12,214</b>   |
| <b>Total Assets</b>   | <b>626,950</b>  | <b>340,524</b>                  | <b>237,161</b>                 | <b>49,265</b>   |
| <b>Current Liabilities</b>                                    |                 |                                 |                                |                 |
| Trade and other payables                                      | 21,493          |                                 |                                | 21,493          |
| Financial liabilities   | 111,512         | 111,512                         |                                | 0               |
| Short-term provisions   | 1,033           |                                 |                                | 1,033           |
| <b>Total Current Liabilities</b>                              | <b>134,038</b>  | <b>111,512</b>                  | <b>0</b>                       | <b>22,526</b>   |
| <b>Non-Current Liabilities</b>                                |                 |                                 |                                |                 |
| Financial liabilities   | 247,322         | 84,959                          | 110,000                        | 52,363          |
| Derivative financial liabilities                              | 5,532           |                                 | 5,532                          | 0               |
| Long-term provisions  | 53              |                                 |                                | 53              |
| Deferred tax liability  | 28,542          |                                 |                                | 28,542          |
| <b>Total Non-Current Liabilities</b>                          | <b>281,449</b>  | <b>84,959</b>                   | <b>115,532</b>                 | <b>80,958</b>   |
| <b>Total Liabilities</b>                                      | <b>415,487</b>  | <b>196,471</b>                  | <b>115,532</b>                 | <b>103,484</b>  |
| <b>Net Assets</b>   | <b>211,463</b>  | <b>144,053</b>                  | <b>121,629</b>                 | <b>(54,219)</b> |
| <b>Adjustment to NAV</b>                                      | <b>13,803</b>   | <b>65,450</b>                   | <b>(19,373)</b>                | <b>(32,274)</b> |
| Adjustment to Independent Valuation                           | 59,586          | 76,407                          | (16,821)                       |                 |
| Adjustment to Contract Price (net of acquisition costs)       | (18,089)        | (18,089)                        |                                |                 |
| Adjustment to Independent Value and construction value        | 7,132           | 7,132                           |                                |                 |
| Adjustment to Mark-to-Market                                  | (8,690)         |                                 | (2,552)                        | (6,138)         |
| Adjustment to Net Asset Value of other assets                 | (16,886)        |                                 |                                | (16,886)        |
| Adjustment to Tax effect adjustments                          | (9,250)         |                                 |                                | (9,250)         |
| <b>Independent Experts NAV (Section 5.4.2 and Appendix J)</b> | <b>225,266</b>  | <b>209,503</b>                  | <b>102,256</b>                 | <b>(86,493)</b> |



## 5.7 Discounted Cash Flow (DCF) Method

### 5.7.1 Overview

The DCF method estimates market value by discounting future cash flows to their net present value. To value PAYCE using the DCF method requires determination of the following:

- Future cash flows;
- An appropriate discount rate to be applied to the cash flows; and
- An estimate of the terminal value.

PAYCE derives its revenue essentially from property development and property rental. In our opinion each of these business activities has a different risk profile. Accordingly, we have:

- separated the overall cash flows derived by PAYCE into those two revenue streams; and
- determined a discount rate applicable to each cash flow.

The discount rates represent an estimate of the weighted average cost of capital (WACC) appropriate for these assets. HCCF has calculated each WACC based on a weighted average cost of equity and cost of debt applicable to each business unit. This is the relevant rate to apply to ungeared cash flows. Accordingly in determining an appropriate discount rate to be applied to the cash flows the three main elements to the determination are:

- Cost of equity;
- Cost of debt; and
- Debt/equity mix

WACC is a commonly used basis but it should be recognised that it has shortcomings in that it:

- Represents the simplification of what are usually more complex financial structures; and
- Assumes a constant degree of leverage which is seldom correct. Certainly for PAYCE, the leverage can and does change significantly in respect of property developments.

#### a) Cost of Equity

The capital asset pricing model (CAPM) is widely used and accepted as a methodology for determining the cost of equity capital.

However, CAPM has limitations including:

- the CAPM theory is based on expectations but uses historical data as a proxy. That is, the future is not necessarily the same as the past;
- the measurement of historical data is subject to high levels of statistical error;
- the measurement of beta which is used in determining the cost of equity is often based on comparisons with other companies. None of these companies is likely to be directly comparable to the entity for which the discount rate is being calculated;



Parameters such as the debt/equity ratio and risk premium are also based on subjective judgements. In addition, the market upheaval since 2007 has seen a repricing of risk by investors and global interest rates, including long term bond rates, are at very low levels by comparison with historical norms. The CAPM methodology does not readily allow for these types of events.

#### b) Cost of Debt

The cost of debt has been determined by reference to the estimated returns required by debt providers including the yield on the PAYCE Corporate Notes (Notes).

#### c) Debt/Equity Mix

Selection of an appropriate debt/equity mix is a matter of judgement. The debt/equity mix represents an appropriate level of gearing, stated in market value terms, for the business over the forecast period. The relevant proportions of debt and equity have been determined having regard to the covenants contained in the Notes and the target debt levels. However it is to be noted that actual debt levels vary considerably over the course of a property development.

### 5.7.2 Definition and Limitations of the CAPM and WACC

CAPM postulates that the return required on an investment or asset can be estimated by applying to the market risk premium a measure of systematic risk described as the beta factor. The beta for an investment reflects the covariance of the return from that investment with the return from the market as a whole. The beta of an investment represents its systematic risk only. It is not a measure of the total risk of a particular investment. An investment with a beta of more than one is riskier than the market and an investment with a beta of less than one is less risky. The formula for deriving the cost of equity using CAPM is as follows:

$$K_e = R_f + \beta(MRP) + \alpha$$

Where:

- $K_e$  = Cost of Equity
- $R_f$  = Risk Free Rate
- $MRP$  = Market Risk Premium
- $\beta$  = Beta (the systematic risk of a stock relative to the market portfolio)
- $\alpha$  = Alpha (size and other premia)

The beta for a company or business operation is normally estimated by observing the historical relationship between returns from the company or comparable companies and returns from the market in general. The market risk premium is estimated by reference to the actual long run premium earned on equity investments by comparison with the return on risk free investments.



The formula used to calculate a WACC under a classical tax system is as follows:

$$WACC = (R_e \times \frac{E}{V}) + (R_d \times (1 - t) \times \frac{D}{V})$$

Where:

- $E$  = value of equity
- $D$  = value of debt
- $V$  = total value of equity + debt
- $R_e$  = cost of equity
- $R_d$  = cost of debt
- $t$  = corporate tax rate

### 5.7.3 Risk Free Rate

There is no official "risk free" rate but rates on government securities (generally the long term 10 years) Commonwealth Bond Rate) are typically used as a acceptable proxies.

### 5.7.4 Market Risk Premium

The market risk premium ( $R_m - R_f$ ) represents the additional return that investors require to invest in equity securities as a whole over risk free investments. There is no generally accepted approach to estimating a forward looking market risk premium (MRP) and therefore the historical premium is used as the best available proxy measure. Over the short term the market risk premium is highly volatile. Accordingly, in order to smoothe fluctuations, the long term average adjusted for the introduction of dividend imputation is a reasonable proxy for the MRP.

Various studies indicate that the long term average MRP at between 5% to 8%, with most recent studies in Australia indicating that 6% is a reasonable approximation of the MRP.

### 5.7.5 Debt/Equity Mix

The tax deductibility of the cost of debt means that the higher the proportion of debt the lower the WACC, although this would be offset, at least in part, by an increase in the beta factor as leverage increases.

The debt/equity mix assumed in calculating the discount rate should be consistent with the level implicit in the measurement of the beta factor. Typically, the debt/equity mix changes over time and there is significant diversity in the levels of leverage across companies in a sector. However, after discussions with PAYCE management on the target debt structure, PAYCE regards a debt/equity mix of 50% debt and 50% equity as appropriate over the medium-long term. We have also reviewed PAYCE's ability to support this level of debt/equity mix by reference to take underlying cash flows and metrics such as interest coverage.

### 5.7.6 Specific Risk

The WACC is designed to be applied to "expected cash flows" which are effectively a weighted average of the likely scenarios. To the extent that a business is perceived as being particularly risky, this specific risk should be dealt with by adjusting the cash flow scenarios.



## **5.8 Calculation of WACC for PAYCE**

### **5.8.1 Cost of Equity Capital**

The cost of equity capital has been estimated by reference to the CAPM. HCCF has adopted a cost of equity capital in the range of:

- Property Rental - 7.78% to 8.28% (mid point – 8.03%)
- Property Development – 10.18% to 10.68% (mid point - 10.43%)

### **5.8.2 Risk Free Rate**

The current risk free rate (spot rate) is at or near an historical low and in view of the long term nature of the assets being valued is unrepresentative of the risk free rate. Accordingly, we have adopted the historical 5 year average ten-year Australian Government Bond rate as a proxy for the risk free rate in determining the cost of equity for PAYCE. According to data released by the Reserve Bank of Australia, the 5 year average rate is 4.17%.

### **5.8.3 Market Risk Premium**

HCCF has consistently adopted a market risk premium of 6% and believes that this continues to be a reasonable estimate. It:

- is not statistically significantly different to the premium suggested by long term historical data;
- is similar to that used by a wide variety of analysts and practitioners (typically in the range 6-7%); and
- makes no explicit allowance for the impact of Australia's dividend imputation system.

### **5.8.4 Beta Factor**

HCCF has adopted the following beta factors in respect of each of PAYCE's business unit:

- Property Rental - 0.31
- Property Development – 0.71

HCCF has considered the beta factors for a range of Australian entities in determining an appropriate beta for PAYCE's business operations. A summary of betas for selected comparable listed entities is set out in Appendix H.

### **5.8.5 Calculation**

Using the estimates set out above, the cost of equity capital can be calculated as follows:





a) Property Rental

Low

$$\begin{aligned} Re &= R_f + \text{Beta} (R_m - R_f) \\ &= 4.17\% + 0.31(6\%) + 1.75\% \\ &= 7.78\% \end{aligned}$$

High

$$\begin{aligned} Re &= R_f + \text{Beta} (R_m - R_f) \\ &= 4.17\% + 0.31(6\%) + 2.25\% \\ &= 8.28\% \end{aligned}$$

b) Property Development

Low

$$\begin{aligned} Re &= R_f + \text{Beta} (R_m - R_f) \\ &= 4.17\% + 0.71(6\%) + 1.75\% \\ &= 10.18\% \end{aligned}$$

High

$$\begin{aligned} Re &= R_f + \text{Beta} (R_m - R_f) \\ &= 4.17\% + 0.71(6\%) + 2.25\% \\ &= 10.68\% \end{aligned}$$

### 5.8.6 Cost of Debt

A cost of debt in the range of 6.85% to 7.25% has been adopted based on existing debt issued, debt facilities and the margins reflected therein..

### 5.8.7 Debt/Equity Mix

The selection of the appropriate debt/equity ratio involves perhaps the most subjectivity of discount rate selection analysis. In determining an appropriate debt/equity mix, regard was had to gearing levels of PAYCE and the peer group entities used in the beta analysis.

PAYCE has a current debt covenant in relation to its issued corporate notes. At any time during the term of the Notes, PAYCE's leverage is not to exceed 62% under the terms of the Notes. We are advised that the management of the Company intends to maintain the leverage at approximately 50%. This translates to a debt to equity ratio of 100%.

### 5.8.8 WACC

The formula to determine WACC is as follows:

$$WACC = (R_e \times \frac{E}{V}) + (R_d \times (1 - t) \times \frac{D}{V})$$

Where:

- $E$  = value of equity
- $D$  = value of debt
- $V$  = total value of equity + debt
- $R_e$  = cost of equity
- $R_d$  = cost of debt
- $t$  = corporate tax rate

On the basis of the parameters outlined and assuming a corporate tax rate of 30%, the nominal WACC is calculated to be:



a) Property Rental

Low

$$\text{WACC} = (7.78\% \times 50\%) + (6.85\% \times (1-30\%) \times 50\%) \\ = 6.29\%$$

High

$$\text{WACC} = (8.28\% \times 50\%) + (6.85\% \times (1-30\%) \times 50\%) \\ = 6.54\%$$

(Mid point – 6.61%)

b) Property Development

Low

$$\text{WACC} = (10.18\% \times 50\%) + (7.25\% \times (1-30\%) \times 50\%) \\ = 7.63\%$$

High

$$\text{WACC} = (10.68\% \times 50\%) + (7.25\% \times (1-30\%) \times 50\%) \\ = 7.88\%$$

(Mid point – 7.75%)

This is an after tax discount rate to be applied to nominal ungeared after tax cash flows. However, it must be recognised that this is a calculation based on statistics of limited reliability and involving a multitude of assumptions. In this regard, HCCF's view is that the selected cost of capital should incorporate a margin over the calculated WACC range. In addition, we have considered the size of PAYCE relative to its peers and consistent with studies on the impact of size on risk, we have adjusted the overall cost of equity by 1.75% - 2.25% to allow for specific risk attributable to PAYCE and its size (market capitalisation).

### 5.8.9 Assumptions

The key assumptions adopted by PAYCE in the preparation of the projections and our adjustments thereto consist of the following:

- Growth in the forecast period of 2.5% in respect of property rental and in line with inflation thereafter;
- Settlements in respect of property developments are based on the time frame for each property to be developed and settled;
- Proceeds from property developments which are funded by debt are shown as a net settlement after repayment of the specific project debt. In addition, the cost of these property developments is accounted for at settlement;
- Based on discussions with management, it is not possible to predict with a requisite degree of certainty the timing and amounts to be spent on properties which are outside the forecast period. Accordingly they have been treated as a land bank property which for the purposes of this report are regarded as a surplus asset.



## 5.9 Valuation Summary – DCF

The DCF method has generated a value per PAYCE Ordinary Share on a control basis summarised as below:

|  | \$'000         |
|--|----------------|
| <u>DCF of Operations</u>               |                |
| Property Rental                        | 342,864        |
| Property Development                   | 110,497        |
| <b>Value of Operating Assets</b>       | <b>453,361</b> |
| <u>Add: Surplus Assets</u>             |                |
| <b>Cash</b>                            | 2,008          |
| <b>Properties (Land- banked)</b>       | 102,097        |
| <b>Value of Firm</b>                   | <b>557,466</b> |
| <u>Less: Value of Debt</u>             |                |
| Corporate Notes                        | (54,000)       |
| Mark-to-Market - Swaps                 | (8,084)        |
| Financial Liabilities                  | (310,973)      |
| <b>Equity Value</b>                    | <b>184,408</b> |
| Shares on Issue                        | 29,745,225     |
| <b>Value per Share (Control basis)</b> | <b>\$ 6.20</b> |

## 5.10 Valuation of PAYCE Shares

The secondary valuation methods of DCF and share trading whilst a useful crosscheck have been excluded in our final assessment as they do not, in our opinion, represent the fair market value of PAYCE shares. The primary valuation method has been used to assess the value of PAYCE shares at \$7.57 per Ordinary Share.

|   | Ref   |               |
|---|-------|---------------|
| Net Asset Value of PAYCE (net of other liabilities) | 5.4.2 | \$225,266,000 |
| No. of shares on issue                              |       | 29,745,225    |
| <b>Value per Share (control basis)</b>              |       | <b>\$7.57</b> |



## **6 VALUATION OF PREFERENCE SHARES**

### **6.1 Key Terms of Preference Shares**

Set out below are the key terms of the Preference Shares:

#### **6.1.1 Issue Price**

The Preference Shares have an Issue Price of \$7.50 each.

#### **6.1.2 Dividends**

##### **6.1.2.1 Rates**

Dividends of 6% per annum are proposed to be paid quarterly, subject to such Dividends being declared at the discretion of PAYCE. On each yearly anniversary of the issue of the Preference Shares, the dividend rate will increase by an additional 1% per annum. For example:

- After one year from the date of issue, the dividend rate will increase to 7% per annum.
- After two years from the date of issue, the dividend rate will increase to 8% per annum, and
- thereafter increasing by 1% per annum in each following yearly period,
- until the date which is six years from the date of issue of the Preference Shares, when the dividend rate increases to 12% per annum, at which time the dividend rate will be capped at 12% per annum.

##### Calculation

All calculations to be undertaken with respect to Dividends will be to four decimal places, by applying the formula below:

$$\text{DIV} = \frac{\text{DR} \times \text{IP} \times \text{D}}{365}$$

Where:

- DIV is the amount of the dividend payable on each Preference Share on the Dividend Payment Date (the 'Dividend Entitlement');
- DR is the Dividend Rate applicable for that Dividend Period;
- IP is the Issue Price; and
- D is the number of days in that Dividend Period.

##### **6.1.2.2 Payments**

The Dividend is at the discretion of PAYCE, be paid by either or of:

- (i) a cash payment; and/or
- (ii) the issue of further Preference Shares with a face value of \$7.50 each, representing an amount equivalent to the Dividend Entitlement (with any fractional amount remaining paid in cash).



#### **6.1.2.3 Cumulative Dividends**

Dividends are cumulative. If all or any part of a scheduled Dividend is not paid (Unpaid Dividend) on the relevant Dividend Payment Date, PAYCE has an obligation to pay the Unpaid Dividend at the time of Repurchase. No interest accrues on any Unpaid Dividend.

#### **6.1.2.4 Optional Dividend**

PAYCE may, at its absolute discretion, elect at any time to pay Preference Shareholders an optional dividend in an amount equal to the unpaid amount of all scheduled (but unpaid) dividends for the period preceding the payment date of the optional dividend.

#### **6.1.2.5 Dividend Payment Restriction**

If a scheduled dividend has not been paid on Preference Shares in full for any reason within five business Days of the relevant Dividend Payment Date, PAYCE must not:

- (i) declare or otherwise determine to pay, or pay, a dividend or make any distribution on any class of its share capital other than Preference Shares; or
- (ii) redeem, reduce, cancel, Buy-back or acquire for any consideration any share capital.

#### **6.1.3 Return of Capital**

If there is a return of capital on a winding-up of PAYCE, Preference Shareholders will be entitled to receive out of the assets of PAYCE available for distribution to holders of shares, in respect of each Preference Share held, a cash payment equal to the sum of:

- (i) the amount of any Dividend Entitlement which has not been satisfied in full including any Dividend Entitlement which has accrued for the period from and including the date of the preceding Dividend Payment Date to the date of commencement of the winding-up; and
- (ii) the Face Value,

before any return of capital is made to holders of Ordinary Shares or any other class of shares ranking behind the Preference Shares.

If, upon a return of capital, there are insufficient funds to pay in full the amounts set out above, the Preference Shareholders and the holders of any such other shares will share in any distribution of assets of PAYCE in proportion to the amounts to which they respectively are entitled.

#### **6.1.4 Voting Rights**

A Preference Share **does not entitle its holder to vote at any general meeting of PAYCE except** in the circumstances detailed in the full terms of the Preference Shares.

#### **6.1.5 Participation in Surplus Assets**

Preference Shares do not confer on their holders the right to participate in the surplus assets of PAYCE on a winding-up beyond the rights set out above.



### **6.1.6 Transfers of Preference Shares**

Preference Shares are transferrable by means a proper instrument of transfer in registrable form in compliance with the requirements of PAYCE's constitution and the Law. The Preference Shares will not be listed on the ASX.

### **6.1.7 Option to Repurchase**

Each Preference Share Holder grants to PAYCE an option to repurchase, on any Dividend Payment Date, some or all of the Preference Shares they may hold, for an amount equal to:

- (iii) the Face Value of each Preference Share; plus
- (iv) the unpaid amount of any scheduled dividends which have not been paid on the Preference Shares during the period prior to the date.

At least 30 days (but no more than 3 months) before the relevant Dividend Payment Date, PAYCE may give notice to one or more Preference Shareholders stating that it will exercise its option to repurchase a specified number of Preference Shares from that Preference Share Holder.

## **6.2 Risk Associated with Preference Shares**

There are specific risks which relate directly to the business of PAYCE. In addition, there are other general risks, many of which are largely beyond the control of PAYCE and its Directors. The risks identified in this section, may have a material impact on the value of the Preference Shares.

### **6.2.1 Illiquidity**

The Preference Shares will not be quoted on an exchange. Accordingly, it is possible that there will be an illiquid market for the Preference Shares.

### **6.2.2 Dividends may not be paid**

There is a risk that dividends on the Preference Shares will not be paid. The terms of issue of the Preference Shares do not require PAYCE to pay dividends. The payment of dividends is subject to the satisfaction of a number of requirements, including among other things that the Directors, at their absolute discretion, resolve to declare and pay a dividend. There is a risk that a dividend may not be paid in full or at all. Under the terms of the Preference Shares, failure to pay a dividend when scheduled will not constitute an event of default in respect of the Preference Shares. In the event that PAYCE does not pay a dividend when scheduled, a Preference shareholder:

- has no right to apply for PAYCE to be wound up or placed in administration, or to cause a receiver or a receiver and manager to be appointed in respect of PAYCE, merely on the grounds it does not or may become unable to pay a dividend when scheduled; and
- will have no right of set-off and no off-setting rights or claims on PAYCE under the terms of the Preference Shares.



If PAYCE does not pay a dividend in full on a dividend payment date, then the dividend payment restriction applies to PAYCE unless certain steps are taken to pay dividends to the Preference Shareholders.

Dividends are cumulative. If a scheduled dividend is not paid on the relevant dividend payment date, PAYCE must pay an amount equal to the unpaid dividends if it exercises its option to buy-back the Preference Shares.

#### **6.2.3 Dividends may not be paid in cash**

There is a risk that Dividends will be declared but paid as additional Preference Shares. The terms of issue of the Preference Shares do not require PAYCE to pay dividends solely as cash. The issuance of further Preference Shares as consideration for dividends may further expose Preference Shareholders to risk.

#### **6.2.4 Call option may not be exercised**

Under the terms of Issue of the Preference Shares, PAYCE is not required to exercise its option to purchase or buy-back the Preference Shares for a cash consideration of \$7.50 each on any dividend payment date. There is a risk that PAYCE will never exercise its powers under this call option.

#### **6.2.5 Risks associated with exchange and conversion**

There is a risk that, in the event that PAYCE breaches the Dividend Payment Restriction, and fails to rectify such breach within 90 days, that it will not exchange the Preference Shares for Redeemable Preference Shares as required in accordance with the Terms of Issue of the Preference Shares.

Even if the Preference Shares are exchanged for Redeemable Preference Shares in accordance with the terms of issue, there is no guarantee that PAYCE will be able to fund the redemption of those Redeemable Preference Shares in accordance with the Terms of Issue.

#### **6.2.6 Restrictions on rights and ranking in a winding-up**

The Preference Shares are unsecured and not guaranteed.

In the event of a winding-up of PAYCE, Preference Shareholders will have a preference in terms of dividends and the return of any capital ahead of Ordinary Shares, but will have no entitlement to share in any surplus in the event of a winding-up.

#### **6.2.7 Future issues by PAYCE**

The terms of issue of the Preference Shares do not in any way restrict PAYCE from issuing further securities (except where a Dividend Payment Restriction exists) or from incurring further indebtedness.

PAYCE's obligations under the Preference Shares will rank subordinate and junior in a winding-up to PAYCE's obligations to holders of senior ranking securities and instruments, and all creditors. Accordingly, PAYCE's obligations under the Preference Shares will not be satisfied unless it can satisfy in full all of its obligations ranking senior to the Preference Shares.



In addition, PAYCE may in the future issue securities which:

- rank for dividends or payments of capital equal with, behind or ahead of the Preference Shares;
- have the same or different dividend, interest or distribution rates as those for the Preference Shares;
- have the same or different terms and conditions as the Preference Shares.

PAYCE may incur further indebtedness and may issue further securities including Preference Shares before, during or after the issue of these Preference Shares.

An investment in the Preference Shares carries no right to participate in any future issue of securities, whether equity preference shares, debt or otherwise, by PAYCE.

An investment in Preference Shares carries no right to be redeemed or otherwise repaid at the same time as PAYCE redeems or otherwise repays other securities, whether equity, shares, debt or otherwise.

#### **6.2.8 Dividends may not be franked**

There is no obligation for PAYCE to pay franked dividends.

#### **6.2.9 Amendment of Terms of Issue of the Preference Shares**

PAYCE may amend the Terms of Issue of the Preference Shares without the approval of Preference Shareholders, where such amendments are necessary or desirable amendments which the Directors consider are not likely to be materially prejudicial to the interests of Preference Shareholders as a whole. PAYCE may also amend the Terms of Issue of the Preference Shares if the amendment has been approved by a special resolution of Preference Shareholders.

### **6.3 Valuation Approach**

Upon our assessment on the terms of the Preference Shares, we have identified two major components of the Preference Shares:

- (i) expected Cash Flows from Scheduled Dividends; and
- (ii) an Option to Repurchase

After taken into consideration various characteristics of the Preference Shares, we have adopted the following valuation methods respectively:

- (i) Expected Cash Flow from Scheduled Dividends – Dividend Discount Model (Appendix F); and
- (ii) Option to Repurchase – Binomial Option Pricing Model (Appendix G)





### 6.3.1 Expected Cash Flow from Scheduled Dividends

#### 6.3.1.1 Scheduled Dividends

For simplicity, our assessment of the expected cash flow from Scheduled Dividends will be on the basis of 4 equal payments quarterly. We are aware that the dividend calculation method under the terms of Preference Shares is on a number-of-days basis. The resultant difference will be immaterial and negligible for the purpose of our assessment.

Expected Cash Flow from the Scheduled Dividends are as follows:

| Quarter | Coupon Rate<br>(p.a.) | Coupon<br>(quarter) |
|---------|-----------------------|---------------------|
| 1       | 6%                    | \$0.1125            |
| 2       | 6%                    | \$0.1125            |
| 3       | 6%                    | \$0.1125            |
| 4       | 6%                    | \$0.1125            |
| 5       | 7%                    | \$0.1313            |
| 6       | 7%                    | \$0.1313            |
| 7       | 7%                    | \$0.1313            |
| 8       | 7%                    | \$0.1313            |
| 9       | 8%                    | \$0.1500            |
| 10      | 8%                    | \$0.1500            |
| 11      | 8%                    | \$0.1500            |
| 12      | 8%                    | \$0.1500            |
| 13      | 9%                    | \$0.1688            |
| 14      | 9%                    | \$0.1688            |
| 15      | 9%                    | \$0.1688            |
| 16      | 9%                    | \$0.1688            |
| 17      | 10%                   | \$0.1875            |
| 18      | 10%                   | \$0.1875            |
| 19      | 10%                   | \$0.1875            |
| 20      | 10%                   | \$0.1875            |
| 21      | 11%                   | \$0.2063            |
| 22      | 11%                   | \$0.2063            |
| 23      | 11%                   | \$0.2063            |
| 24      | 11%                   | \$0.2063            |
| 25      | 12%                   | \$0.2250            |
| 26      | 12%                   | \$0.2250            |
| 27      | 12%                   | \$0.2250            |
| 28      | 12%                   | \$0.2250            |

From the 29<sup>th</sup> quarter and onwards, Scheduled Dividends are \$0.2250 per quarter.

In our valuation assessment, we will assume the above dividends are paid as scheduled. We have made this assumption following a review of historical financial performance for the last 5 years and management cash flow estimates for the next five years. The risk of Scheduled Dividends not being paid or not being paid according to the above schedule is to be adjusted by means of risk factor discounting.



### 6.3.1.2 Discount Rate

In determining an appropriate discount rate on the above Scheduled Dividends, we have considered risks set out in this section 6 which we summarise as follows:

- (i) Risk of Dividends not being Declared  
Terms of the Preference Shares allow Scheduled Dividend not to be declared according to discretion of the Board of Directors of PAYCE.
- (ii) Timing of Scheduled Dividends  
Similar to the above, the Directors of PAYCE are able to determine the timing of payments on any Unpaid Dividends. There is risk of dividends being paid later than the scheduled dates.
- (iii) Default Risk  
This refers to risk of the Scheduled Dividends not being paid despite being declared.
- (iv) Liquidity  
The Preference Shares are transferrable but may not be listed on an exchange. We have assumed there is no formal secondary market for the Preference Shares.
- (v) Payments of Scheduled Dividends as additional Preference Share  
The terms of the Preference Shares allow Scheduled Dividends to be paid in the form of additional Preference Shares at a deemed value of \$7.50 per share. The issued Preference Shares will have all the above stated risks attached. There is also a risk that the market value of the Preference Shares is less than the deemed value at the time.

Taken into consideration the above risk factors in addition to the risk free rate, our assessed range of discount rate for compensation of risks attached to the Scheduled Dividends cash flows is 10.10% to 10.40%. For the purpose of Valuing the Preference Share, we have applied the mid point discount rate of 10.25%.

### 6.3.1.3 Reference Range of Discount Rate

To assess the reasonableness of the range of discount rate above, we have considered the relative risk profile of the Preference Shares against:

- (i) PAYCE Notes; and
- (ii) PAYCE Ordinary Equity

In our opinion, risks attached to the Preference Shares as set out in this section 6 are lower than ordinary equities in view of its priority in dividends and share capital upon a wind-up event. Alternatively, the risks are higher than secured debt due to its non-secured structure and uncertainties on the interest payments (in this case the Scheduled Dividends), and also in respect of both the payment amounts and the timing of those payments.

As discussed in earlier sections, PAYCE currently has \$50 million secured notes on issue (Notes). The Notes are traded in the market and the mark-to-market yield for the Notes is between 6.8% to 6.9% or approximately 6.85% as of 4 February 2015.

We have also assessed the cost of equity based on industry average over 15 listed companies in the property development industry. Within the listed property development companies detailed on Appendix H, there are no companies directly relevant to PAYCE in respect of its products and target market. However, as part of our analysis, we have also



selected several companies which have greater relativity to PAYCE. The analysis was performed using the Capital Asset Pricing Model (CAPM). Details of the analysis and calculations are included in Appendix H. The assessed cost of equity is 10.43%.

Accordingly, the reference range of the discount rate is between 6.85% and 10.43%. Based on our assessment of the relevant risk factors compared to the Corporate notes and PAYCE ordinary equity (refer 6.2.1.2) our assessed range of 10.10% to 10.40% with a midpoint of 10.25% is within the reference range and reflects the particular risks associated with the Preference Shares.

#### **6.3.1.4 Discounted Scheduled Dividends Calculations**

We have applied the above discount rate to the Scheduled Dividends cash flows. Calculations are detailed on Appendices H & I, and they are on the following basis:

- (i) Discounting is performed on a quarterly compounding basis.
- (ii) A perpetuity on the Scheduled Dividends from the 29<sup>th</sup> quarter onwards is computed representing the discounted value of all future dividends as at the 29<sup>th</sup> quarter.

The calculated present value of the Scheduled Dividends is \$7.41.

#### **6.3.2 Option to Repurchase**

In order to determine the value of the option to repurchase the Preference Shares at \$7.50, we have considered the structure and characteristics of the Preference Shares. They have similar structure and characteristics to those of a callable bond.

General options valuation methods include the Binomial Option Pricing Model and the Black Scholes Option Pricing Model. We have adopted the Binomial Option Pricing Model as opposed to the Black Scholes Model which is more appropriate for pricing European style options.

(Please refer to Appendix G for a detailed description of the Binomial Option Pricing Model.)

We have taken into consideration the following parameters:

- (i) Price Volatility
- (ii) Up and Down Movements
- (iii) Discount Rate
- (iv) Risk-neutral Probabilities of Movements

For the purpose of valuing the Option to Repurchase, we will be utilising the concept of a hypothetical bond, hypothetical option-free bond and hypothetical option-bearing bond in the following sections. Our application of the Model is in quarterly steps covering 28 quarters (7 years) and a total of 405 possible scenarios. This, in our opinion, should generate sufficient accuracy without having to overly expand the number of scenarios in the assessment.

We have calculated an implied option value based on the following relationship:

$$\text{Value of Callable Bond} = \text{Value of an Option-Free Bond} - \text{Value of Call Option}$$



#### 6.3.2.1 Volatility ( $\sigma$ )

There is a lack of market trading on comparable securities which have a similar structure or characteristics to the Preference Shares. We have considered the Preference Shares sharing a lot of similarities with a typical callable bond. Prices of callable bonds are generally affected by yield movements of similar corporate debt instruments.

Considering the above, as a proxy for the price volatility of the Preference Shares, we have computed the weekly volatility of the 5-year Bank Bill Swap Rate for BBB rated debts over the past 10 years (source: Bloomberg). The weekly volatility has then been annualised and standardised to quarter volatility.

The computed weekly volatility is 2.24%, which represents an annualised volatility of 16.22%, or a standardised quarterly volatility of 8.11%.

#### 6.3.2.2 Up and Down Movements ( $u$ , $d$ )

The volatility obtained above is used to compute an appropriate up or down quarterly movement. The calculated 'up' and 'down' factors are as below:

|           |        |                         |
|-----------|--------|-------------------------|
| (i) Up    | 1.0845 | <b>(<math>u</math>)</b> |
| (ii) Down | 0.9221 | <b>(<math>d</math>)</b> |

(Refer Appendix G for formulae in computing the above.)

#### 6.3.2.3 Discount Rate ( $r$ )

As set out in Section 6.2.1.2, we have assessed an appropriate discount rate to be within a range of 10.10% to 10.40% for the purposes of valuing the Preference Shares we have taken the midpoint of 10.25%.

#### 6.3.2.4 Risk-neutral Probabilities of Movements ( $P(u)$ , $P(d)$ )

By applying the formula for risk-neutral probabilities as listed in Appendix G using the up and down factors and the discount rates above, we have computed the relevant probabilities as follows:

|                       |        |                          |
|-----------------------|--------|--------------------------|
| (i) Up Probability    | 0.6396 | <b><math>P(u)</math></b> |
| (ii) Down Probability | 0.3604 | <b><math>P(d)</math></b> |

#### 6.3.2.5 Binomial Tree – Discount Rates

A binomial tree which captures the above quarterly movements of the discount rate is generated by applying the relevant up and down movement factors:

|           |        |                         |
|-----------|--------|-------------------------|
| (i) Up    | 1.0845 | <b>(<math>u</math>)</b> |
| (ii) Down | 0.9221 | <b>(<math>d</math>)</b> |

These discount rates will be applied as yields for calculation of prices of the hypothetical bonds for the relevant quarters and scenarios in the following sections.



(Please refer to Appendix L for full binomial trees for discount rates.)

#### 6.3.2.6 Binomial Trees – Hypothetical Option-Free Bond

Application of the Binomial Model involves the 'backward induction' technique. In simple terms, this technique requires calculation starting at the open end of the binomial tree and in this case, the 28<sup>th</sup> quarter. Steps for such calculations are detailed as follows:

- 1) The bond prices for the hypothetical option-free bond at the 28<sup>th</sup> quarter are computed by applying the perpetuity formula as follow:

$$P = \frac{D}{(1+r)^1} + \frac{D}{(1+r)^2} + \dots + \frac{D}{(1+r)^n} = \frac{D}{r}$$

Where:

- P = Bond price as at the 28<sup>th</sup> quarter.
- D = Expected future coupons. (In simulation to the Preference Shares' Scheduled Dividends, D = \$0.2250)
- r - Discount rate for the relevant scenario. (refer Appendix L and as set out in the above section)

- 2) The expected values at the 27<sup>th</sup> quarter are calculated by applying the formula as follows:

$$P_{27} = P_{u28} P(u) + P_{d28} P(d)$$

Where:

- P<sub>27</sub> = Expected Value for the 27<sup>th</sup> quarter.
- P<sub>u28</sub> = Bond price as at the 28<sup>th</sup> quarter for the 'up' scenario
- P<sub>d28</sub> = Bond price as at the 28<sup>th</sup> quarter for the 'down' scenario
- P(u) = Up probability (refer Section 6.3.2.4)
- P(d) = Down probability (refer Section 6.3.2.4)

- 3) The relevant coupon, in simulation to the Preference Shares' Scheduled Dividends set out in Section 6.2.1.1, is added to the computed expected value in Step 2).
- 4) The relevant discount rate as set out in Section 6.2.1.2 is applied to the sum computed in Step 3).
- 5) The above steps are repeated for each node.

Please refer to Appendix L for the full binomial tree generated by repeating Steps 1) to 5) above.

Calculated price of the hypothetical option-free bond is \$5.20.



### 6.3.2.7 Binomial Trees - Hypothetical Option-Bearing Bond

Similar to the above section, the 'backward induction' technique is applied in generating the binomial trees for the hypothetical option-bearing bond. Starting at the open end of the binomial tree and in this case, the 28<sup>th</sup> quarter, the steps for calculations are detailed as follows:

- 1) The bond prices,  $P$ , for the hypothetical option-free bond at the 28<sup>th</sup> quarter are adopted with the exception that any values which are higher than \$7.50 are replaced with \$7.50. These represent the option holder (PAYCE) exercising the option to repurchase at \$7.50 in its favour.
- 2) The expected values at the 27<sup>th</sup> quarter are calculated by applying the formula as follows:

$$P_{27} = P_{u28} P(u) + P_{d28} P(d)$$

Where:

- $P_{27}$  = Expected Value for the 27<sup>th</sup> quarter.
  - $P_{u28}$  = Bond price as at the 28<sup>th</sup> quarter for the 'up' scenario
  - $P_{d28}$  = Bond price as at the 28<sup>th</sup> quarter for the 'down' scenario
  - $P(u)$  = Up probability (refer Section 6.3.2.4)
  - $P(d)$  = Down probability (refer Section 6.3.2.4)
- 3) The relevant coupon, in simulation to the Preference Shares' Scheduled Dividends set out in Section 6.3.1.1, is added to the computed expected value in Step 2).
  - 4) The relevant discount rate as set out in Appendix L is applied to the sum computed in Step 3).
  - 5) Any values obtained in Step 4) above which are higher than \$7.50 are replaced with \$7.50 for the same reason as stated in Step 1).
  - 6) The above steps are repeated for each node.

Please refer to Appendix L for the full binomial tree generated by repeating Steps 1) to 6) above.

Calculated price of the hypothetical option-bearing bond is \$5.02.

### 6.3.2.8 Option Value

By subtracting the value of the hypothetical option-bearing bond (\$5.02) from the value of the hypothetical option-free bond (\$5.20), we have assessed the option value to be \$0.18.



## 6.4 Value of Preference Shares

By subtracting the above option value from the valuations previously computed by the Dividend Discount Model in Section 6.3.1.4, we have assessed the **value of the Preference Shares to be \$7.23.**



## **7 VALUATION OF CASH CONSIDERATIONS**

Shareholders who elect to participate in the Buy-back will receive the following cash considerations for each Ordinary Share bought back:

- \$0.80 paid upon cancellation of the Ordinary Shares;
- \$0.80 paid 12 months after the cancellation of the Ordinary Shares; and
- \$0.70 paid 18 months after the cancellation of the Ordinary Shares.

Our assessed present value of the cash considerations for each Ordinary Share is **\$2.17**, which is made up of the discounted value of the three payments as detailed below.

### **7.1 Cash Consideration – 1<sup>st</sup> Payment**

The first cash consideration of \$0.80 per Ordinary Share is to be paid upon cancellation of the Ordinary Shares. We consider the timing and risk to be immaterial and therefore no discount is applied.

Our assessed valuation for the first cash consideration is \$0.80 per Ordinary Share.

### **7.2 Cash Consideration – 2<sup>nd</sup> Payment**

The second cash consideration of \$0.80 per Ordinary Share is to be paid in 12 months after cancellation of the relevant Ordinary Shares. We have applied a discount rate of 7.5%, which is in line with PAYCE's cost of debt.

Our assessed valuation for the second cash consideration is \$0.74 per Ordinary Share.

### **7.3 Cash Consideration – 3<sup>rd</sup> Payment**

The third cash consideration of \$0.70 per Ordinary Share is to be paid 18 months after cancellation of the relevant Ordinary Shares. We have applied a discount rate of 7.5%, which is in line with PAYCE's cost of debt.

Our assessed valuation for the second cash consideration is \$0.63 per Ordinary Share.





## 8 IMPACT OF SHARE BUY-BACK

### 8.1 Pro-Forma Statement of Financial Position

| Pro-Forma Statement of Financial Position<br>(AS AT 31 DECEMBER 2014) | Pre Buy-back   | Post Buy-back  |                |                |                |                |                |                |                |                |                |
|---|----------------|----------------|----------------|----------------|----------------|----------------|----------------|----------------|----------------|----------------|----------------|
|   |                | 10%            | 20%            | 30%            | 40%            | 50%            | 60%            | 70%            | 80%            | 90%            | 100%           |
|   |                | Acceptance     | Acceptance     | Acceptance     | Acceptance     | Acceptance     | Acceptance     | Acceptance     | Acceptance     | Acceptance     | Acceptance     |
|   | \$'000         | \$'000         | \$'000         | \$'000         | \$'000         | \$'000         | \$'000         | \$'000         | \$'000         | \$'000         | \$'000         |
| <b>Assets</b>   |                |                |                |                |                |                |                |                |                |                |                |
| Cash and cash equivalents   | 27,008         | 26,215         | 25,422         | 24,628         | 23,835         | 23,042         | 22,249         | 21,456         | 20,662         | 19,869         | 19,076         |
| Net Properties Value (Incl. project liabilities)                      | 311,758        | 311,758        | 311,758        | 311,758        | 311,758        | 311,758        | 311,758        | 311,758        | 311,758        | 311,758        | 311,758        |
| Other assets  | 8,938          | 8,938          | 8,938          | 8,938          | 8,938          | 8,938          | 8,938          | 8,938          | 8,938          | 8,938          | 8,938          |
| <b>Total Assets</b>   | <b>347,704</b> | <b>346,911</b> | <b>346,118</b> | <b>345,324</b> | <b>344,531</b> | <b>343,738</b> | <b>342,945</b> | <b>342,152</b> | <b>341,358</b> | <b>340,565</b> | <b>339,772</b> |
| <b>Liabilities</b>  |                |                |                |                |                |                |                |                |                |                |                |
| Financial liabilities   | 54,502         | 54,502         | 54,502         | 54,502         | 54,502         | 54,502         | 54,502         | 54,502         | 54,502         | 54,502         | 54,502         |
| Mark-to-market adjustment - FIIG Notes                                | 4,000          | 4,000          | 4,000          | 4,000          | 4,000          | 4,000          | 4,000          | 4,000          | 4,000          | 4,000          | 4,000          |
| Mark-to-market adjustment - Swaps                                     | 8,084          | 8,084          | 8,084          | 8,084          | 8,084          | 8,084          | 8,084          | 8,084          | 8,084          | 8,084          | 8,084          |
| Other liabilities   | 55,854         | 55,854         | 55,854         | 55,854         | 55,854         | 55,854         | 55,854         | 55,854         | 55,854         | 55,854         | 55,854         |
| Buy-back Cash Payable (at Valuation)                                  | 0              | 1,361          | 2,721          | 4,082          | 5,442          | 6,803          | 8,163          | 9,524          | 10,885         | 12,245         | 13,606         |
| Preference Shares (at Valuation)                                      | 0              | 7,169          | 14,337         | 21,506         | 28,674         | 35,843         | 43,012         | 50,180         | 57,349         | 64,517         | 71,686         |
| <b>Total Liabilities</b>  | <b>122,440</b> | <b>130,969</b> | <b>139,498</b> | <b>148,028</b> | <b>156,557</b> | <b>165,086</b> | <b>173,615</b> | <b>182,144</b> | <b>190,673</b> | <b>199,203</b> | <b>207,732</b> |
| <b>Net Assets / Equity</b>  | <b>225,264</b> | <b>215,942</b> | <b>206,619</b> | <b>197,297</b> | <b>187,975</b> | <b>178,652</b> | <b>169,330</b> | <b>160,007</b> | <b>150,685</b> | <b>141,363</b> | <b>132,040</b> |
| <b>Ordinary Shares</b>  |                |                |                |                |                |                |                |                |                |                |                |
| No. of Ordinary Shares  | 29,745,225     | 28,753,718     | 27,762,210     | 26,770,703     | 25,779,195     | 24,787,688     | 23,796,180     | 22,804,673     | 21,813,165     | 20,821,658     | 19,830,150     |
| <b>Net Assets per Ordinary Share</b>                                  | <b>\$ 7.57</b> | <b>\$ 7.51</b> | <b>\$ 7.44</b> | <b>\$ 7.37</b> | <b>\$ 7.29</b> | <b>\$ 7.21</b> | <b>\$ 7.12</b> | <b>\$ 7.02</b> | <b>\$ 6.91</b> | <b>\$ 6.79</b> | <b>\$ 6.66</b> |
| Minority Discount (mid-point)   | 20.00%         | 20.00%         | 20.00%         | 20.00%         | 20.00%         | 20.00%         | 20.00%         | 20.00%         | 20.00%         | 20.00%         | 20.00%         |
| <b>Value per Ordinary Share</b>                                       | <b>\$ 6.06</b> | <b>\$ 6.01</b> | <b>\$ 5.95</b> | <b>\$ 5.90</b> | <b>\$ 5.83</b> | <b>\$ 5.77</b> | <b>\$ 5.69</b> | <b>\$ 5.61</b> | <b>\$ 5.53</b> | <b>\$ 5.43</b> | <b>\$ 5.33</b> |



In order to reflect the value of each share on a minority interest basis requires initially determining the premium for control. The minority interest discount is the inverse of the control premium (refer Appendix K for formula).

We attach in Appendix K details of recent control premium studies together with relevant minority interest discount formula and other issues which would give rise to an increased control premium.

The studies indicate that control premiums generally range between 25% - 40%, with the long term median typically around 30% - 35%. Within this range, property entities are generally at the lower end partly as a result of the influence of A-REIT's which generally have low control premiums.

In considering the control premium and its inverse, the discount for minority interest, we understand that PAYCE is a well-managed company, its strategic focus has remained on property development in its target markets (Sydney and more recently Brisbane), it has continued to use retained earnings to facilitate project funding (rather than distribute dividends) and has a reasonably "lean" cost structure.

Based on our review of cash flow projections, corporate overheads are forecasted to be of the order of \$11.5m per annum (net of project fee income).

Accordingly, we consider that the opportunity for cost savings and other synergies is limited, and that the control premium for PAYCE is in the range between 25% - 30%. Consequently the minority discount is in the range between 17% - 23%.

The Pro-Forma Statement of Financial Position is prepared on the following basis:

i. Adjusted Dec-14

The pre Buy-back column is based on information supplied by PAYCE with adjustments for the following items according to the assessed valuations discussed in earlier sections of this Report:

- Net Properties Value
- Mark-to-Market of Corporate Notes
- Mark-to-Market of Swaps

The "Adjusted Dec-14" position is an indicative scenario of the proposed share Buy-back not proceeding.

ii. Buy-back Acceptance levels

These scenarios assume relevant percentages of the proposed 9,915,075 Buy-back shares are accepted into the Buy-back by Ordinary Shareholders.

iii. Cash and cash equivalents

This account is adjusted by the number of buy-back shares accepted, times the value of cash consideration of the Buy-back assessed in Section 7.



iv. Net properties value

This represents the assessed value stated in Appendix J.

v. Mark-to-market values for the Notes and Swaps

These are detailed in Section 5.4.3 and Section 5.4.4 of the Report respectively.

vi. Preference Shares (at Valuation)

The value of the Preference Shares assessed in Section 6.3 is applied. That is, valuation per Preference Share, times accepted number of buy-back shares.

vii. No. of Ordinary Shares

This represents total number of ordinary shares outstanding less accepted number of buy-back shares.

The Pro-Forma Statement of Financial Position shows a reduction of up to \$0.91 Net Assets per share on the basis of 100% acceptance. After taking into account the minority discount, valuation per share is \$5.33 compared to the pre Buy-back control value of \$7.57.

## 8.2 Summary of Conclusions

**We have assessed the Buy-back to be fair and reasonable to the participating Non Associated Shareholders. In forming this view, we have concluded that the advantages of the Buy-back to Non Associated Shareholders outweigh the disadvantages.** The key considerations are summarised below.

Non-Associated Shareholders have a number of options open to them, namely:

- (a) to reject the equal access off-market Buy-back proposal and continue to own Ordinary Shares in PAYCE;
- (b) to approve the equal access off-market Buy-back proposal and participate fully in the Buy-back offer;
- (c) to approve the equal access off-market Buy-back proposal and participate partially in the Buy-back offer; and
- (d) to approve the equal access off-market Buy-back proposal and not participate at all in the Buy-back offer

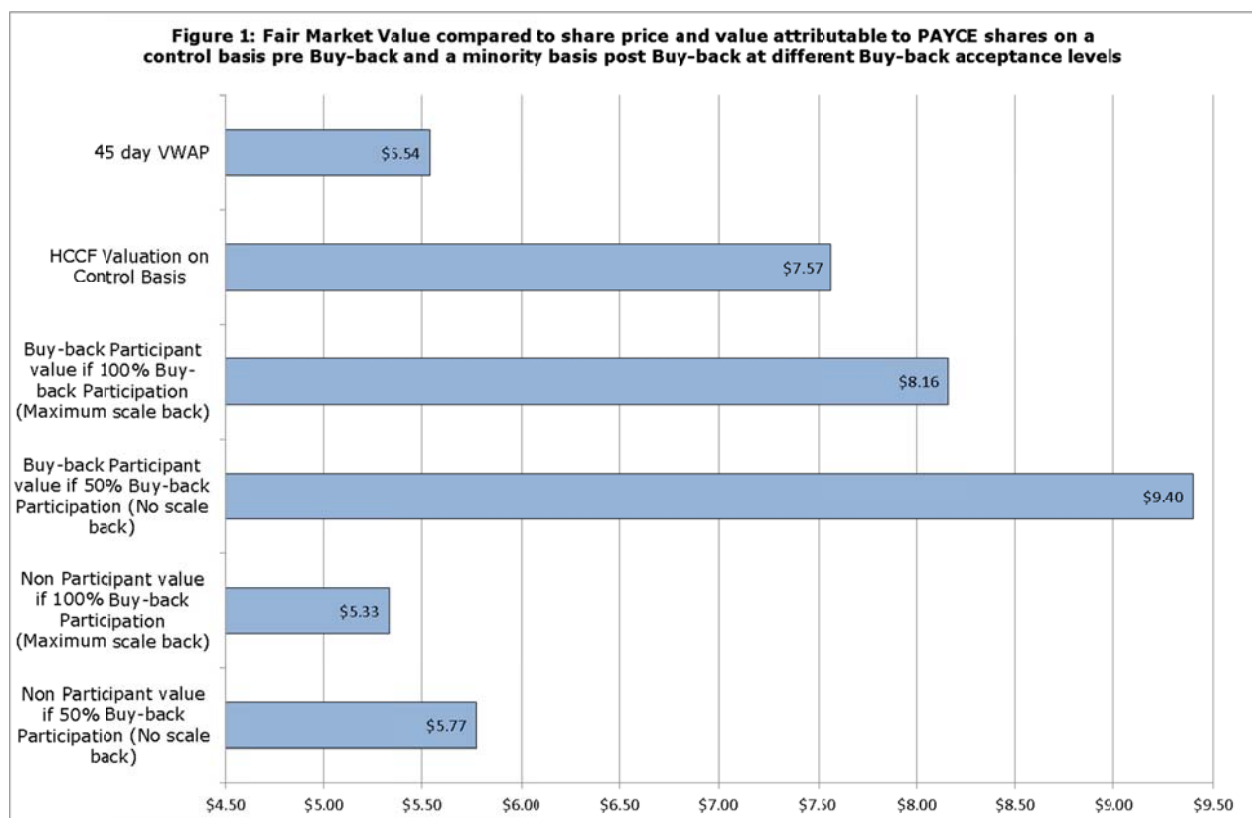
The different options available to Non Associated Shareholders will suit different Non Associated Shareholders.

The additional complexity to be taken into account in each Non Associated Shareholder's decision process is that the more appealing the Buy-back is assessed to be by Non Associated Shareholders, the higher the expected overall level of participation and, consequently, the greater the risk that the Buy-back will be fully utilised so that up to 30% of shares accepted into the Buy-back by each Non Associated Shareholder will not be bought back by PAYCE. This



would result in Non Associated Shareholders retaining up to 30% of their shares in PAYCE, which may not necessarily be their desired outcome.

The figure below compares our fair market value of a PAYCE share on a control basis of \$7.57 with the indicative value attributable to Non Associated Shareholders under alternatives (b), (c) and (d) outlined above as well as the 45-day volume weighted average price (**VWAP**), for PAYCE shares as at 20 February 2015 of \$5.54. For the purpose of this analysis, we have decided that the value of any residual PAYCE shares owned by Non Associated Shareholders pursuant to each of the scenarios is adjusting for any value accretion or dilution resulting from various levels of participation in the Buy-back and adjusted to the value of the Ordinary Shares on a control basis by 20% to reflect that they will be held on a minority basis after the Buy-back;



We note the following in relation to the graph above:

- we have assessed the fair market value of PAYCE, on a control basis, to be \$225.266 million. This translates into a fair value per share of \$7.57 and is based on our primary valuation methodology, being a valuation a sum of the parts valuation of the PAYCE business. Our valuation of PAYCE is discussed in further details in Section 5;



- based on our valuation range of PAYCE under the possible outcomes for the overall value attributable to Non Associated Shareholders **who elect not to participate in the Buy-back:**
  - assuming 50% of available shares participate in the Buy-back each PAYCE share post transaction would have a fair value of \$5.77;
  - assuming 100% of available shares participate in the Buy-back each PAYCE share post transaction would have a fair value of \$5.33 per PAYCE share;
- based on our valuation of PAYCE under the possible outcomes for the overall value attributable to Non Associated Shareholders **who elect to participate in the Buy-back:**
  - assuming 50% of available shares participate in the Buy-back the overall value attributable to each would be \$9.40. This figure comprises the following:
    - cash consideration (of \$0.80 paid on cancellation, \$0.80 paid 12 months after cancellation and \$0.70 paid 18 months after cancellation) valued at \$2.17 per PAYCE share and;
    - fair value of Preference Share of \$7.23;
  - assuming 100% of available shares participate in the Buy-back the overall value attributable to each PAYCE share would be \$8.16. This figure comprises the following:
    - cash consideration (of \$0.80 paid on cancellation, \$0.80 paid 12 months after cancellation and \$0.70 paid 18 months after cancellation) valued at \$2.17 per PAYCE share and fair value of Preference Share of \$7.23 multiplied by 70% which is the acceptance level based on scaling;
    - value of a PAYCE share at this acceptance level of \$5.33 multiplied by 30%, which is the remaining shares not bought back as a percentage of the original shareholder prior to the buy-back.

Subsequent to the implementation of any of the Buy-back, shareholders may be left with minority equity investments in PAYCE and therefore may not be able to realise a full control value for their PAYCE shares, unless a takeover offer materialises for PAYCE. Minority parcels of shares attract a discount to their full underlying value and our fair value calculations post Buy-back have been determined utilising a 20 percent discount.

### **Valuation of PAYCE shares on a control basis**

HCCF has assessed the fair market value of a PAYCE share, on a control basis, to be \$7.57. For the purpose of our opinion, fair market value is defined as the amount at which the PAYCE shares would change hands between a knowledgeable willing buyer and a knowledgeable willing seller, neither being under a compulsion to buy or sell. We have not considered special value in this assessment.



Our valuation assumes a hypothetical change of control transaction and is undertaken prior to the implementation of the Off-market Equal Access Buy-back. That is, our valuation reflects neither the cash payments nor the potential dilution/accretion on the share value potentially resulting from the implementation of the Buy-back.

For the purpose of our analysis, we have valued PAYCE as at 20 February 2015 (the Valuation Date). We have estimated the fair market value of PAYCE by aggregating the estimated fair market value of the assets and liabilities of PAYCE on a sum of the parts basis as summarised in the table below.

**Table 2: Valuation of PAYCE**

| <b>Asset Class</b>         | <b>Reference</b> | <b>\$'000</b>  |
|----------------------------|------------------|----------------|
| Property Developments      | Appendix J       | 209,503        |
| Investment Properties      | Appendix J       | 102,256        |
| Other Assets / Liabilities | 5.4.3            | (86,493)       |
| <b>Total</b>               |                  | <b>225,266</b> |

In determining the value of shares in PAYCE, we also considered whether there should be a premium or discount of those shares compared to PAYCE's net asset value (NAV) or net tangible assets (NTA). NAV's and NTA's are two common valuation metrics of Australian Real Estate Investment Trusts (A-REITs). NTA is based on the underlying book value of assets whereas NAV is based on the expected cash flows from the property assets, together with other income generating assets.

The major property assets of PAYCE are stated at contract price, recent valuation (e.g. Kirrawee), based on the underlying cash flows of the investment asset as assessed in a recent valuation (e.g. East Village) or is in the process of development (e.g. Riverwood). PAYCE's property assets have been determined on the basis of NAV. Whilst it may be argued that there is valuation upside in assets under development those assets represent a small proportion of the overall property assets (7.4%) and in our opinion does not warrant adjusting the overall property portfolio to reflect any premium or discount.



## 9 ADVANTAGES & DISADVANTAGES OF THE BUY-BACK

### 9.1 Advantages and disadvantages

The likely advantages and disadvantages to Non Associated Shareholders if the Buy-back is approved are set out below. Where relevant, we have specifically outlined whether the advantage or disadvantage is from the perspective of a participating shareholder (i.e. a shareholder willing to sell their shares under the Buy-back) or a non-participating shareholder (i.e. a shareholder willing to approve the Buy-back but not participate in the Buy-back).

**Table 3: Summary of main advantages and disadvantages for Non Associated Shareholders who participate in the Buy-back and for Non Associated Shareholders who do not participate in the Buy-back**

|                   | <b>Participation Scenario (from Participating Non Associated Shareholders' perspective)</b>   | <b>Non-Participation Scenario (from non-Participating Non Associated Shareholders' Perspective)</b>   |
|-------------------|---|---|
| <b>Advantages</b> | <ul style="list-style-type: none"> <li>▪ The Buy-back is not compulsory. Non Associated Shareholders will be able to choose whether to participate in the Buy-back having regard to their individual circumstances.</li> <li>▪ At low levels of participation in the Buy-back, Non-Associated Shareholders may be able to exit their entire investment in Ordinary Shares in PAYCE at a 24.2% premium to fair market value of PAYCE (on a control basis) and at a 69.7% premium to recent trading prices</li> <li>▪ Non Associated Shareholders will have the ability to wholly or partially reduce their holding in PAYCE, should they desire to.</li> <li>▪ Buy-back consideration is assessed as fair</li> <li>▪ Participating Shareholders may receive scheduled quarterly Dividends on Preference Shares at the discretion of PAYCE. These dividends rank in priority to Ordinary Shares.</li> <li>▪ Preference Shares receive priority</li> </ul> | <ul style="list-style-type: none"> <li>▪ Potential value accretion for PAYCE shares which continue to be held</li> <li>▪ Potential for future growth in PAYCE with the Managing Director Mr Brian Boyd having a controlling shareholding</li> </ul> |



|                      | Participation Scenario (from Participating Non Associated Shareholders' perspective)   | Non-Participation Scenario (from non-Participating Non Associated Shareholders' Perspective)  |
|----------------------|--|---|
|                      | in a winding up.   |   |
| <b>Disadvantages</b> | <ul style="list-style-type: none"> <li>▪ Adverse impact on share ownership control and voting power</li> <li>▪ At high levels of participation in the Buy-back, Shareholders who wish to exit their entire investment in Ordinary Shares would retain residual shares of up to 30% of their current shares in PAYCE</li> <li>▪ The value received for the Buy-back is part cash and part Preference Shares in PAYCE, which have risks associated with them</li> <li>▪ No liquid market for Preference Shares</li> <li>▪ Dividends on Preference Shares are uncertain</li> <li>▪ PAYCE could re-purchase Preference Shares prior to any appreciation of market price</li> <li>▪ Preference Shares have reduced voting rights</li> <li>▪ Potential income tax liability</li> </ul> | <ul style="list-style-type: none"> <li>▪ Adverse impact on share ownership control and voting power</li> <li>▪ Reduced liquidity of Ordinary Shares due to reduced number of Ordinary Shares on issue.</li> <li>▪ Potential risk of de-listing</li> </ul> |

These advantages and disadvantages are set out in more detail below:

## 9.2 Advantages

### 9.2.1 The Buy-back offers optionality to Non Associated Shareholders (Participating and Non-Participating Shareholders' perspective)

If the Buy-back is approved, Non Associated Shareholders will be able to choose whether to participate in the Buy-back having regard to their individual circumstances. The Buy-back therefore provides Non Associated Shareholders with greater flexibility than would a pro-rata return of capital or a special dividend.

Furthermore, approval of the Buy-back could be considered favourably whatever a Non Associated Shareholder's view is on the value of a PAYCE share:

- (a) if a Non Associated Shareholder considers the value of a PAYCE share is greater than the consideration payable under the Buy-back, the Non Associated Shareholder could approve the Buy-back since it would offer them the possibility of increasing their interest in PAYCE if other shareholders accept the Buy-back.





- (b) if the Non Associated Shareholder's view on the value of a PAYCE share is less than the consideration payable under the Buy-back, the Non Associated Shareholder could approve the Buy-back so that they would have the opportunity of selling their shares at a premium.

In addition, the Buy-back offers the flexibility to participate only for a portion of a Non Associated Shareholder's holding in the Company. This could allow Non Associated Shareholders to immediately realise some shares while retaining upside potential through the unsold Ordinary Shares.

### ***9.2.2 Possibility of achieving greater value in the future (non-Participating Shareholders' perspective)***

To evaluate whether to participate in the Buy-back, shareholders should consider whether there is a reasonable prospect of being able to achieve greater value by holding their PAYCE Ordinary Shares rather than participating in the Buy-back. The table below sets out the fair market value of PAYCE Ordinary Shares on a minority basis (post Buy-back) assuming various levels of participation.

#### **Sensitivity on value impact from Buy-back on non-Participating Shareholders**

| <b>% of available shares participation in the Buy-back</b> | <b>PAYCE share</b> |
|--|--------------------|
|  | <b>\$</b>          |
| 0.001%   | 6.06               |
| 10%  | 6.01               |
| 20%  | 5.95               |
| 30%  | 5.90               |
| 40%  | 5.83               |
| 50%  | 5.77               |
| 60%  | 5.69               |
| 70%  | 5.61               |
| 80%  | 5.53               |
| 90%  | 5.43               |
| 100%   | 5.33               |

1. Based on our fair market value assessment of a PAYCE share of \$7.57 on a control basis, adjusted for a 20% minority discount and the impact of the Buy-back at various participation levels.
2. The total number of shares offered to be bought back is 9,915,075. The maximum number that can participate is 14,268,606 after the intentions of Mr Brian Boyd and Mr Garry Boyd are taken into account.

Moreover, Shareholders that choose to retain their investment in PAYCE may be able to participate in the potential upside.



### 9.2.3 Participating Shareholders will receive an overall value per share at a premium to PAYCE's recent trading price (Participating Shareholders' perspective)

At levels of 70% or less participation in the Buy-back, participating shareholders will be able to maximise their value per share in PAYCE. Participating shareholders are able to realise a total value per share of \$9.40 and exit their entire Ordinary Shareholding in PAYCE at participation levels of 70% or less. This consideration represents an 24.2% premium as at the Valuation Date and a premium of 69.7% to PAYCE's 45-day VWAP as at the Valuation Date. Accordingly, participating shareholders have the opportunity to achieve a higher value than what may be achieved from a current market transaction. Participating shareholders would be able to successfully accept for a minimum 70% of their shares into the Buy-back, assuming full participation by all other eligible shareholders, and an even greater proportion of their shares if not all eligible shareholders participate.

The table below sets out the proceeds receivable by participating shareholders and the overall value per share for participating shareholders at different levels of participation in the Buy-back.

**Table 4: Total value per share at different levels of participation in the Buy-back**

| Acceptance Level | No. of Shares Participating | Pre Buy-back                         | Post Buy-back                   |                                   |              |                                       |               |                                   |                                       |
|------------------|-----------------------------|--------------------------------------|---------------------------------|-----------------------------------|--------------|---------------------------------------|---------------|-----------------------------------|---------------------------------------|
|                  |                             | Ordinary Share Value (Control Basis) | Preference Share (at Valuation) | Cash Consideration (at Valuation) | Allocation % | Ordinary Share Value (Minority Basis) | Unallocated % | Value: Participating Shareholding | Value: Non-Participating Shareholding |
|                  |                             |                                      | Discount Factor at: 10.25%      | Discount Factor at: 7.50%         |              |                                       |               |                                   |                                       |
| 10%              | 991,507                     | \$7.57                               | \$7.23                          | \$2.17                            | 100.00%      | \$6.01                                | 0.00%         | \$9.40                            | \$6.01                                |
| 20%              | 1,983,015                   | \$7.57                               | \$7.23                          | \$2.17                            | 100.00%      | \$5.95                                | 0.00%         | \$9.40                            | \$ 5.95                               |
| 30%              | 2,974,522                   | \$7.57                               | \$7.23                          | \$2.17                            | 100.00%      | \$5.90                                | 0.00%         | \$9.40                            | \$5.90                                |
| 40%              | 3,966,030                   | \$7.57                               | \$7.23                          | \$2.17                            | 100.00%      | \$5.83                                | 0.00%         | \$9.40                            | \$5.83                                |
| 50%              | 4,957,537                   | \$7.57                               | \$7.23                          | \$2.17                            | 100.00%      | \$5.77                                | 0.00%         | \$9.40                            | \$5.77                                |
| 60%              | 5,949,045                   | \$7.57                               | \$7.23                          | \$2.17                            | 100.00%      | \$5.69                                | 0.00%         | \$9.40                            | \$5.69                                |
| 70%              | 6,940,552                   | \$7.57                               | \$7.23                          | \$2.17                            | 100.00%      | \$5.61                                | 0.00%         | \$9.40                            | \$5.61                                |
| 80%              | 7,932,060                   | \$7.57                               | \$7.23                          | \$2.17                            | 100.00%      | \$5.53                                | 0.00%         | \$9.40                            | \$5.53                                |
| 90%              | 8,923,567                   | \$7.57                               | \$7.23                          | \$2.17                            | 100.00%      | \$5.43                                | 0.00%         | \$9.40                            | \$5.43                                |
| 100%             | 9,915,075                   | \$7.57                               | \$7.23                          | \$2.17                            | 100.00%      | \$5.33                                | 0.00%         | \$9.40                            | \$5.33                                |
| 100%             | 10,906,582                  | \$7.57                               | \$7.23                          | \$2.17                            | 90.91%       | \$5.33                                | 9.09%         | \$9.03                            | \$5.33                                |
| 100%             | 11,898,090                  | \$7.57                               | \$7.23                          | \$2.17                            | 83.33%       | \$5.33                                | 16.67%        | \$8.72                            | \$5.33                                |
| 100%             | 12,889,597                  | \$7.57                               | \$7.23                          | \$2.17                            | 76.92%       | \$5.33                                | 23.08%        | \$8.46                            | \$5.33                                |
| 100%             | 13,881,105                  | \$7.57                               | \$7.23                          | \$2.17                            | 71.43%       | \$5.33                                | 28.57%        | \$8.24                            | \$5.33                                |
| 100%             | 14,268,606                  | \$7.57                               | \$7.23                          | \$2.17                            | 69.49%       | \$5.33                                | 30.51%        | \$8.16                            | \$5.33                                |

As set out in the table above, the higher the participation rate in the Buy-back the higher the proportion of shares that will not be bought back and will remain invested in PAYCE.

### 9.2.4 Mr Brian Boyd is a desired investor in PAYCE (non-Participating Shareholders' perspective)



Mr Brian Boyd and his associated entities currently have a 38.74% equity interest in PAYCE, making him PAYCE's largest shareholder. Mr Brian Boyd and his associated entities will hold 49.75% of the equity interest in PAYCE assuming full participation in the Buy-back.

In practical terms, if the voting power of entities associated with Mr Boyd increases, his associated entities will have a potentially greater capacity to influence the voting results of resolutions which may be considered by PAYCE Shareholders in the future (by voting for or against such resolutions). Such resolutions could include, for example, resolutions to appoint or remove directors, to amend the constitution of PAYCE, or to increase or decrease the number of shares on issue. Under the Corporations Act entities associated with Mr Boyd would be excluded from voting on resolutions where Mr Boyd or those associated entities may benefit from it or are affected by it.

Any resolutions which could be considered by PAYCE Shareholders in the future would require the approval of a minimum of 50% of total votes cast by Shareholders entitled to vote on the resolution. As noted above, Mr Brian Boyd and his associated entities will hold 49.75% of the equity interest in PAYCE assuming full participation in the Buy-back.

Mr Brian Boyd has been the Managing Director of PAYCE for over 25 years, and has over 32 years' experience in the property development industry. The independent Directors consider him to be a proactive and experienced property developer and businessman, and therefore a significant and desired investor in PAYCE.

The independent Directors also believe that the implications of Mr Boyd's associated entities increasing their percentage shareholding in PAYCE will not have a material impact on the direction of PAYCE because Mr Boyd, through associated entities, has historically held a significant interest in PAYCE. Mr Boyd has advised the independent Directors that he does not intend to use any increased voting power that may be obtained through his associated entities following the Buy-Back to significantly change PAYCE's principal business of undertaking property development projects.

***9.2.5 In any event, the effect of the Buy-back on the relative concentration of shareholdings and potential control of the Company will not be known until the transaction is completed, as it is unknown to what extent individual Shareholders will participate in the Buy-back. Buy-back Consideration is Fair (Participating Shareholders' perspective)***

We have formed the view that the Buy-back is fair in the context that the value of the consideration being offered, which we assess as in the range of between \$8.16 and \$9.40 per Ordinary Share, is greater than the value of PAYCE shares on a controlling basis as it is greater than our assessment of the fair value of PAYCE Ordinary Shares prior to the Buy-back of \$7.57 per Ordinary Share. If 70% or less of eligible Ordinary Shares accept into the Buy-back all accepting shares will receive an assessed value of \$9.40 per Ordinary Share. If 100% of eligible Ordinary Shares accept into the Buy-back each accepting share will receive \$8.16 per share in our assessed value. Depending on the level of acceptance the total value for Shareholders accepting the Buy-back will be equivalent to assessed value of between \$8.16 per share and \$9.40 per share.



#### **9.2.6 Premium to Market Price**

The value of the Buy-back price consideration is a premium compared to recent share trading prices and significantly greater than our assessment of the fair value of PAYCE's shares.

#### **9.2.7 Opportunity to Exit in an Efficient Manner (Participating Shareholders' perspective)**

Historically, PAYCE's Ordinary Shares have been thinly traded on the ASX. The Buy-back provides Shareholders with an opportunity to sell their Ordinary Shares in an efficient and cost effective manner, in consideration for a combination of a cash payment and Preference Shares which carry a discretionary Dividend.

The Buy-back also allows Shareholders to sell a relatively large volume of Ordinary Shares without depressing the market price of Ordinary Shares, and in circumstances where the market for the Ordinary Shares may not otherwise be sufficiently liquid to accommodate such volume.

#### **9.2.8 Preference Shares Dividends (Participating Shareholders' perspective)**

Historically, PAYCE's Shareholders had only received dividends twice over the past 10 years. By participating in the Buy-back, Shareholders may, at the discretion of PAYCE, receive scheduled quarterly Dividends on their Preference Shares.

#### **9.2.9 Priority of Dividends (Participating Shareholders' perspective)**

Preference Shares receive priority to Ordinary Shares in the receipt of dividends.

#### **9.2.10 Priority in a Winding Up (Participating Shareholders' perspective)**

Preference Shares receive priority to Ordinary Shares in the event of a winding up.

### **9.3 Disadvantages**

#### **9.3.1 Concentration of shareholding (non-Participating Shareholders' perspective)**

The effect of the Buy-back on the relative concentration of shareholdings and potential control of the Company will not be known until the transaction is completed, as it is unknown to what extent individual Shareholders will participate in the Buy-back.

Individual non-participating shareholders other than Mr Brian Boyd will bear the consequences of a blocking stake in PAYCE as a result of the significant influence exercised by Mr Brian Boyd and may therefore forfeit the opportunity to realise a control value in the future. Furthermore, Mr Brian Boyd and his associates may further consolidate their position by purchasing other shares on-market through the 'creep' provisions of the Corporations Act.

#### **9.3.2 Reduction in the free float and liquidity of shares (non-Participating Shareholders' perspective)**

If the Buy-back is approved, the shares tendered under the Buy-back will be transferred to the Company and cancelled in accordance with the Corporations Act. Upon completion of the Buy-back and subsequent cancellation of the shares, the total issued capital of PAYCE may be substantially reduced by up to 33%.

The reduction in the free float and potential effect upon trading liquidity may limit PAYCE shares' attractiveness to institutional investors as it may affect their ability to readily realise large parcels of



shares without impacting the share price. This may have the potential to cause a downward re-rating of the PAYCE shares by these investors.

### **9.3.3 Impact on Voting (Participating and non-Participating Shareholders' perspective)**

Depending on the level of participation by Shareholders in the Buy-Back, the voting power of entities associated with Mr Boyd may increase, giving his associated entities a potentially greater capacity to influence the voting results of resolutions which may be considered by PAYCE Shareholders in the future (by voting for or against such resolutions). Examples of such resolutions could include to appoint or remove directors, to amend the constitution of PAYCE, or to increase or decrease the number of shares on issue. Under the Corporations Act entities associated with Mr Boyd would be excluded from voting on resolutions where Mr Boyd or those associated entities may benefit from it or are affected by it.

Any resolutions which could be considered by PAYCE Shareholders in the future would require the approval of a minimum of 50% of total votes cast by Shareholders entitled to vote on the resolution. As Mr Boyd will ensure that, following the Buy-Back, his associated entities will hold less than 50% of the total Ordinary Shares on issue irrespective of the level of participation in the Buy-Back, these entities will not be able to control the results of any resolution, but could have a substantial influence on the outcome of any resolution.

### **9.3.4 Preference Share Risks (Participating Shareholders' perspective)**

The Preference Shares are a significant part of the value to be received for those accepting the Buy-back. The features and risks associated with the Preference Shares are set out in detail in Section 1.3 and the disadvantages of the Preference Share features in this section under the heading Disadvantages. Shareholders should clearly understand the features and risks of these shares before making a decision. We have taken the features and risks of the Preference Shares into account when determining our discount factor of 10.25% to arrive at a fair market value of \$7.23 for the Preference Shares.

### **9.3.5 Liquidity of Preference Shares (Participating Shareholders' perspective)**

It is assumed the Preference Shares will not be listed on any formal secondary market in which they could be sold.

### **9.3.6 Market Price of Preference Shares (Participating Shareholders' perspective)**

The price at which Preference Shareholders will be able to sell the Preference Shares is uncertain and there will only be a market in the event that the requirements of an authorised exchange are able to be met after the issue of the Preference Shares.

### **9.3.7 Dividends are uncertain (Participating Shareholders' perspective)**

Scheduled Dividends of the Preference Shares are uncertain and subject to Directors' discretion at the time as to whether a dividend is declared and the timing of payments. Additionally, Dividends can be paid via the issue of further Preference Shares at the discretion of Directors.



### **9.3.8 PAYCE's Option to Repurchase (Participating Shareholders' perspective)**

PAYCE has the option to buy-back Preference Shares at their issued price. Therefore, Preference Shareholders could be unable to realise any appreciation of market price of their Preference Shares if in the case of increased market value of those shares.

### **9.3.9 Ordinary Shares Liquidity (Participating and non-Participating Shareholders' perspective)**

The reduction in the number of Ordinary Shares on issue may cause further illiquidity to the already thinly traded Ordinary Shares.

### **9.3.10 Potential Risk of Delisting (non-Participating Shareholders' perspective)**

Potential consequences of the reduction of Ordinary Shares issued include further thin trading and more concentration in holdings of the largest substantial Shareholders. The lack of liquidity and spread increases the risk of PAYCE's Ordinary Shares being delisted by the ASX.

### **9.3.11 No Voting Rights on Company Matters (Participating Shareholders' perspective)**

Ordinary Shareholders accepting the Buy-back will be exchanging Ordinary Shares with voting rights for cash and Preference Shares with no voting rights, except in relation to issues that directly affect the Preference Shares.

### **9.3.12 Taxation (Participating Shareholders' perspective)**

The Buy-back price of \$9.80 includes a component of deemed unfranked dividends for taxation purposes, being \$8.26 per Ordinary Share. No franking credits are to be utilised in relation to the Buy-back. It is possible that Shareholders, who participate in the Buy-back, may have an income tax liability that exceeds the cash component of the Buy-back price. It is recommended that Shareholders seek independent taxation advice.



## APPENDIX A - GLOSSARY

| Term                                     | Definition  |
|--|---|
| AFSL                                     | Australian Financial Services Licence   |
| A-REIT                                   | Australian Real Estate Investment Trust   |
| ASIC                                     | Australian Securities and Investments Commission  |
| Associated Shareholders                  | Mr Brian Boyd and entities associated with him (as defined by the Corporations Act (including Lanox Pty Ltd and Ruz Pty Ltd).     |
| ASX                                      | ASX Limited A.C.N 008 824 691 or the financial market operated by it as the context requires                                      |
| Buy-back                                 | The equal access Buy-back of up to 9,915,075 Ordinary Shares held by Eligible Shareholders  |
| CAANZ                                    | Chartered Accountants Australia and New Zealand   |
| Corporations Act or Act                  | The Corporations Act 2001 (Cth)   |
| DASCO                                    | DASCO Australia Pty Ltd   |
| DCF                                      | Discounted cash flow methodology  |
| Directors                                | The Directors of PAYCE as at the date of this Report, who comprise Brian Boyd, and the Independent Directors                      |
| Eligible Shareholder                     | A Shareholder who is a registered holder of Ordinary Shares on the Buy-back record date   |
| Extraordinary General Meeting            | The meeting of Shareholder scheduled for 2 April 2015 as convened by the Notice of Extraordinary General Meeting                  |
| GICS                                     | Global Industry Classification Study  |
| Hanrick Curran Corporate Finance or HCCF | Hanrick Curran Corporate Finance Pty Ltd A.C.N 165 488 620 holder of AFSL No. 467461  |
| IER or Report                            | Independent Expert's Report   |
| Listing Rules                            | The listing rules of the ASX  |
| Independent Directors                    | Mr Roger Short and Mr Christopher Gabriel, who are non-executive Directors of PAYCE   |
| NAV                                      | Net Asset Value   |
| Notice                                   | The notice of extraordinary general meeting dated 2 March 2015 giving notice to Shareholders of the Extraordinary General Meeting |
| NRA                                      | Net realisable value of assets methodology  |
| NTA                                      | Net Tangible Assets   |
| Offer                                    | The offer to Eligible Shareholders to participate in the Buy-back   |



|                         |  |
|-------------------------|--|
| Ordinary Shares         | An ordinary share in the capital of PAYCE  |
| PAYCE or the Company    | PAYCE Consolidated Limited ABN 19 001 566 310  |
| Preference Shares       | The securities which are to be issued to Eligible Shareholders in partial consideration for the Buy-back |
| Preference Share Holder | A Registered holder of Preference Shares in PAYCE.   |
| Register                | The register of members of PAYCE maintained in accordance with the Corporations Act.                     |
| Resolutions             | The resolutions set out in the Notice of Extraordinary General Meeting                                   |
| RG 110                  | ASIC Regulatory Guide 110 Share buy-backs  |
| RG 111                  | ASIC Regulatory Guide 111 Content of expert reports  |
| RG 112                  | ASIC Regulatory Guide 112 Independence of experts  |
| Sekisui House           | Sekisui House Australia Holdings Limited   |
| Shareholder             | A registered holder of an Ordinary Share in PAYCE  |
| Valuation Date          | 20 February 2015   |
| Wingate                 | Wingate Properties Pty Ltd   |





## **APPENDIX B – SOURCE OF INFORMATION**

### **SOURCE OF INFORMATION**

#### **Documents**

1. PAYCE's audited Financial Statements **(FS)** for June 2012, 2013 and 2014.
2. PAYCE's half yearly reviewed FS for December 2011, 2012 and 2013.
3. Working paper files and management FS for December 2014.
4. PAYCE's constitution, Shareholder agreements, rights of shares and terms of issue for Preference Shares.
5. Agreements pertaining to other parties, eg joint venture agreements.
6. Dividend history over the last 10 years.
7. Share trading volumes and price history for the last 5 years.
8. The 'valuation model' prepared for and utilised by PAYCE, to be able to test its construction and reliability and assess its resilience to different assumptions to December 2021.
9. Valuations prepared for any property held by PAYCE.
10. Business plans, budgets, cashflow forecasts, development forecasts as available to stress test the reliability of prior forecasts and by implication current activity.
11. Documentation regarding the Notes issued, including covenants.
12. Banking documentation, covenants, etc especially as they may impact on the ability to pay Preference and Ordinary Share dividends.
13. Share register details including an analysis of Shareholder numbers by ranges of shareholding



## **APPENDIX C – STATEMENT OF QUALIFICATION AND DECLARATIONS**

### **STATEMENT OF QUALIFICATION AND DECLARATIONS**

Hanrick Curran Corporate Finance Pty Ltd (HCCF), a wholly owned subsidiary of Hanrick Curran (HC), holds an Australian Financial Services Licence under the Act and its representatives are qualified to provide this Report. The director of HCCF responsible for this Report has not provided financial advice to PAYCE.

Prior to accepting this engagement, HCCF considered its independence with respect to PAYCE with reference to Regulatory Guide 112: Independence of experts

This Report has been prepared specifically for the Shareholders of PAYCE in relation to the Buy-back. Neither HCCF, HC nor any employee therefore undertakes responsibility to any person, other than PAYCE Shareholders, in respect of this Report, including any errors or omissions howsoever caused.

The statements and opinions given in this Report are given in good faith and the belief that such statements and opinions are not false or misleading. In the preparation of this Report HCCF has relied upon information believed after due inquiry to be reliable and accurate. HCCF has no reason to believe that any information supplied to it was false or that any material information has been withheld from it. HCCF has evaluated the information provided to it by PAYCE, its advisors, as well as other parties, through inquiry, analysis and review, and nothing has come to its attention to indicate that information provided was materially mis-stated or would not afford reasonable grounds upon which to base its report. HCCF does not imply and it should not be construed that it has audited or in any way verified any of the information provided to it, or that its inquiries could have verified any matter which a more extensive examination might disclose.

The information relied upon in the preparation of this Report is set out in Appendix B to this Report.

PAYCE has provided an indemnity to HCCF for any claims arising out of any mis-statement or omission in any material or information provided to it in the preparation of this Report.

HCCF provided a draft copy of this Report to PAYCE for comments as to factual accuracy, as opposed to opinions, which are the responsibility of HCCF alone. Changes made to this Report as a result of this review by the Directors and Management have not changed the methodology or conclusions reached by HCCF.

HCCF will receive a professional fee based on time spent in the preparation of this Report estimated at approximately \$45,000 (exclusive of GST). HCCF will not be entitled to any other pecuniary or other benefit whether direct or indirect, in connection with the making of this Report.



## **APPENDIX C – Cont’d**

### **STATEMENT OF QUALIFICATION AND DECLARATIONS**

Mr Alex Fraser, a director and representative of HCCF assumed overall responsibility for this Report. He has the necessary experience and professional qualifications appropriate to the advice being offered. Other HCCF staff have been consulted in the preparation of this Report where appropriate.



## **APPENDIX D – VALUATION APPROACHES**

### **VALUATION APPROACHES**

There are a number of methodologies available with which to value an asset, a business, business unit or the securities in an entity. The principal methodologies used are:

- market based assessments
- capitalisation of earnings
- discounted cash flow
- net realisable value of assets

Each of these methodologies is appropriate in certain circumstances. The decision as to which methodology to utilise generally depends on the methodology most commonly adopted in valuing the asset in question and the availability of appropriate information.

Market based assessments relate to the valuation of entities, the units/shares which are often traded on a recognised exchange. In respect of shares traded on the ASX, the share price would, prima facie, constitute the market value of the shares, such market prices usually reflect the prices paid for small parcels of shares and as such do not include a control premium relevant to a significant parcel of shares.

The capitalisation of earnings methodology involves capitalising the earnings of a project, a business or entity at an appropriate multiple, which reflects the risks underlying the earnings together with growth prospects. This methodology is theoretically most appropriate where an entity or business is expected to generate a relatively stable level of earnings but in practice, is also frequently used in a range of other circumstances.

Discounted cash flow methodology involves calculating the net present value of cash flows that are expected to be derived from future activities. The forecast cash flows are discounted by a discount rate that reflects the time value of money and the risk inherent in the cash flows. This methodology is particularly appropriate in valuing projects, businesses and companies that are in a start-up phase and other entities which are expecting considerable volatility and/or growth in earnings during the growth phase, as well as businesses with a finite life (such as mining projects). The utilisation of this methodology generally requires that the asset be sufficiently advanced to enable management to provide long term cash flows with some degree of reliability.

The net realisable value of assets methodology involves the determination of the net realisable value of the assets of a business or entity, assuming an orderly realisation of those assets. This value includes a discount to allow for the time value of money and for reasonable costs of undertaking the realisation. This methodology assumes a reasonable time frame for sale and does not presume the sale is a forced sale.



## **APPENDIX E – BUSINESS OPERATIONS OVERVIEW**

### **BUSINESS OVERVIEW AND KEY DRIVERS**

#### **1. Business Operations & Strategy**

PAYCE is a significant Australian property group whose business model focuses on long-term medium density apartment and mixed use (retail/commercial) product and urban renewal projects. PAYCE focuses on property developments within Sydney and Queensland including large urban renewal and community projects.

Since 2002 PAYCE has delivered “in excess of 2,500 high quality residential and mixed use apartments across Sydney and aims to deliver 7,500 residential mixed use apartments over the next 5 years at Riverwood (Washington Park), Ermington, Wentworth Point, Kirrawee, Auburn and Melrose Park in Sydney and West End in Brisbane”.

#### **2. Property Development**

The key objective of property development is to acquire land and/or buildings and effect change to the acquired asset such that value is created. The process from acquisition through to ultimate settlement:

- Involves risk at the varying stages;
- Requires substantial finance for the acquisition and development of suitable sites;
- Results in cash flows which are generally large and irregular; and
- Involves projects which can sometimes take many years from start to settlement.

#### **3. Key Drivers**

There are a number of factors which are critical to the success of property development which include (but are not limited to):

- Relationships with key industry players including authorities, financiers, builders and consultants; and
- Skills in effecting change through the approvals process;

In addition:

- Housing finance;
- Population growth unemployment rates and economic metrics within the catchment area and generally;
- Housing affordability;
- Supply; and
- Clearance rates

are all important matters.



## **Appendix E – Cont'd**

### **4. PAYCE's Geographic Focus**

The focus to date has and continues to be Sydney, however there are developments in Queensland including West End in Brisbane and also Townsville and Ipswich.

#### **4.1 Sydney**

In its document titled Sydney's Housing Choices the New South Wales Department of Planning and Environment states that "over the last 5 years new housing production has grown from around 13,000 dwellings per annum to around 22,800 per annum....the highest level since 2002. Even with this growth there is a significant gap between current housing production and future housing needs". The document then refers to various strategies to meet the expected future needs including:

- Removing the barriers to increased housing production through Government working with Councils and the development sector to put into place flexible planning controls; and
- Undertaking urban renewal in transport corridors which then identified several nodes and corridors as priorities.

Industry reports indicate that Sydney's population is expected to expand to approximately 6 million people by 2036 and approximately 8 million – 9 million by 2061, which will drive long term and consistent housing demand. This population growth will be largely driven by net overseas migration. Sydney's growth over the next 25 years indicates the requirement for over half a million new apartments.

As such, Sydney requires the construction of circa 32,000 new dwellings (apartments / houses) each year to accommodate the projected 1.5 million extra people into Sydney over the next 20 years; however only circa 15,000 dwellings have been built per annum in recent years, with the exception of 2013 when 21,000 new dwellings were completed.

The most recent census of population and housing indicates that the Sydney market has the most severe imbalance between supply and demand of all capital cities in Australia. The challenges of redressing the situation in Sydney include limited land supply, geographical constraints, land ownership fragmentation and zoning restrictions, together with all planning constraints and delays. As a result of these barriers to entry, many developers are deterred and the supply of new dwellings diminishes.

#### **Medium unit prices and affordability**

According to Australia Property Monitors, in the year to June 2014, the median unit price in Sydney increased by 13.3% to \$573,255. This can be compared to the median house price in Sydney of \$811,837 (increased by 17% from June 2013).

The past 24 months has shown strong and consistent levels of buyer activity in the affordable entry level price category, whilst there has been softer demand for more expensive product.



## **Appendix E – Cont'd**

### **Locational factors**

In Sydney, the location of the development is paramount in driving the decision of prospective purchasers, particularly first time buyers and owner occupiers. There has been, and will continue to be, strong demand for dwellings within the inner and middle rings (within 10-20 kilometers of the CBD), with buyers now willing to forgo internal space to ensure immediate access to amenity including infrastructure, transport, education, employment, cafes, restaurants, bars and beaches.

PAYCE operates largely within the medium density residential apartment market to deliver high quality, affordable apartments located in close proximity to infrastructure and other amenities within the inner and middle rings of Sydney.

### **4.2 Brisbane**

A paper published in 2011 by the Queensland Government under the title Queensland Government Population Projections to 2031 indicates that:

- By 2056 Queensland's population is projected to double to approximately 9.1 million (under the medium series projections); and
- Ipswich is to have the fastest growth estimated at 5% per annum (111,000 people).

The median age of the population is expected to increase from the current 36 years to 38 years by 2021 reaching 43 years by 2056. This will impact on the housing profile with an emphasis on unit dwellings. By 2021 the Brisbane Local Government area is expected to grow by approximately 125,000 people or 1.1% growth per annum.

The structural change towards apartment living is being driven by a number of demographic, social and economic factors, and is slowly taking place in other capital city markets, but well underway in South East Queensland. In the last 20 years around 29% of Queensland dwelling approvals were multi units, in 2012/13 this had risen to 39%.

State Government forecasts suggest that between 2006-2031 Queensland will experience the fastest and largest household growth in Australia, around 68%. Of this growth 89% are lone person households – one of the key drivers of multi-unit dwelling occupancy.

### **5. Key customers and suppliers**

PAYCE works with a variety of service providers, suppliers, contractors and consultants to develop and build its medium density residential apartment and mixed use (retail/commercial) product and urban renewal projects. PAYCE is not reliant on a single service provider or supplier, instead working with several different parties depending on the project being undertaken.

In terms of customers, PAYCE is similarly not dependent on a key customer or customer base. It markets and sells its completed apartment and mixed use (retail/commercial) products to interested third parties in the market place according to demand.



## **Appendix E – Cont'd**

### **6. Key competitors and barriers to entry**

PAYCE's key competitors include other significant listed and unlisted property developers within the Sydney and Queensland markets.

Given PAYCE's significant business history, PAYCE's Directors believe that there are several barriers to entry for new competitors entering the sector. These include:

- the identification and purchase of appropriate development sites at a reasonable price;
- the complexity of the development approval process;
- the sourcing of appropriate funding to both purchase and develop the identified site.

### **7. External threats**

PAYCE faces various risks in implementing its business strategy including:

- Dependence on the Australian economy;
- Competitive environment;
- Reputation;
- Funding risks;
- Operational risks;
- Accounting policies;
- Litigation and regulatory proceedings;
- Environmental risks; and
- Other risks.





## Appendix E – Cont'd

### 8. PAYCE Project Experience

The below table provides a summary of the development projects undertaken by PAYCE since 2000:

| Project description   | Completed |
|---|-----------|
| Mariner's Cove, 248 unit residential development located at Wentworth Point, Sydney                       | 2000      |
| Corfu, 54 residential development located at Marina Parade, Wentworth Point, Sydney                       | 2002      |
| Santorini and Portofino, 58 unit residential and commercial development, Wentworth Point, Sydney          | 2003      |
| Mykonos, 79 unit residential development on Amalfi Drive, Wentworth Point, Sydney                         | 2004      |
| Bellagio, 141 unit residential development located on Bennelong Road, Wentworth Point, Sydney             | 2005      |
| Sorrento, 120 unit residential and commercial development on Hill Road, Wentworth Point, Sydney           | 2006      |
| Paros, 131 unit residential development on Hill Drive, Wentworth Point, Sydney                            | 2006      |
| Palermo, 245 unit residential and commercial development on Hill Road, Wentworth Point, Sydney            | 2007      |
| Valencia, 173 unit residential development on Marine Parade, Wentworth Point, Sydney                      | 2007      |
| The Artisan, 129 unit residential development on Blackwall Point Road, Chiswick, Sydney                   | 2011      |
| APEX, 153 unit residential/commercial development on Defries Avenue, Victoria Park, Sydney                | 2012      |
| Meridian, 123 unit social housing development, Kentucky Road, Washington Park, Riverwood, Sydney          | 2013      |
| East Village, 206 unit residential and mixed use retail / commercial development in Victoria Park, Sydney | 2014      |
| Platinum, 322 unit residential development in Victoria Park, Sydney                                       | 2014      |

### 9. Important contracts

In carrying out its business operations, PAYCE enters into important contracts with:

- Joint Venture / Joint Operation participants  
These agreements outline the roles and responsibilities of the participants in the development of sites.
- Builders appointed to construct the relevant developments  
These agreements outline the contractual obligations of the parties for the construction of residential and mixed use / commercial developments on the site.



## **Appendix E – Cont'd**

These contracts are based on industry practice, and do not contain unusual provisions or clauses which impose onerous obligations on PAYCE.

### **10. Financing arrangements**

PAYCE has funding arrangements at both the corporate and project / development level.

At the corporate level, PAYCE has issued a \$50 million senior secured corporate note expiring in December 2018.

At a development level, PAYCE (or where relevant the joint operation participants) arrange funding for either or both the purchase and development of specific sites. The project funding is generally limited recourse in nature and therefore creates limited or no exposure to the other parts of PAYCE.

### **11. Capital Management Policy**

As part of its PAYCE corporate governance requirements the Directors consider PAYCE's capital management policy and strategy on an on-going basis.

### **12. Recent development activities**

Up until the date of this Report, PAYCE maintained its development activities, progressing the development of multiple sites and acquiring additional development sites

*(Source PAYCE Management and other studies as indicated)*



## APPENDIX F – DIVIDEND DISCOUNT MODEL

### Dividend Discount Model – DDM

The Dividend Discount Model (DDM) is a method of valuing stock price based on the theory that a stock is worth the sum of all of its future dividend payments, discounted back to their present value. In other words, it is used to value stocks based on the net present value of the future dividends. Financial theory says that the value of a stock is worth all of the future cash flows expected to be received by the holder, discounted by an appropriate risk-adjusted rate. According to the DDM, dividends are the cash flows that are returned to the shareholder.

The application of DDM involves calculations using the general discounted cash flow formula:

$$DCF = \frac{CF_1}{(1+r)^1} + \frac{CF_2}{(1+r)^2} + \dots + \frac{CF_n}{(1+r)^n}$$

Where:

- DCF = Value at time 0
- CF = Cash Flow in relevant time period
- r = Appropriate risk-adjusted discount rate

For a stock which pays a fixed dividend with no growth into perpetuity, the price can be calculated using the formula below:

$$P_0 = \frac{D}{(1+r)^1} + \frac{D}{(1+r)^2} + \dots + \frac{D}{(1+r)^n} = \frac{D}{r}$$

Where:

- $P_0$  = Value at time 0
- D = Dividend
- r = Appropriate risk-adjusted discount rate



## APPENDIX G – BINOMIAL OPTIONS PRICING MODEL

### **Binomial Options Pricing Model**

The binomial options pricing model (BOPM) provides a numerical method for the valuation of options. It uses an iterative procedure, allowing for the specification of nodes, or points in time, during the time span assessed. The binomial model takes a risk-neutral approach to valuation. It assumes that underlying security prices can only either increase or decrease with time until the option expires worthless.

The binomial model enables a multi-period view of the underlying asset price. Users can visualize the change in asset price from period to period and evaluate options based on making decisions at different points in time. By looking at the binomial tree of values, one can determine in advance when a decision on exercise may occur. If the option has a positive value, there is the possibility of exercise, whereas if it has a value less than zero, it should be held for longer periods.

Application of the BOPM involves the following steps:

#### **1. Constructing a Binomial Tree**

At each step, it is assumed that the underlying instrument will move up or down by a specific factor (u or d) per step of the tree. The up and down factors are calculated using the underlying volatility,  $\sigma$ , and the time duration of a step, t. u and d are then computed using the formula below:

$$u = e^{\sigma\sqrt{t}}$$
$$d = \frac{1}{u}$$

Where:

- e = the exponential term (base of the natural logarithm)
- $\sigma$  = volatility
- t = time duration of a step

#### **2. Compute Values at the Final Nodes**

Values or prices for the underlying asset at the final nodes of the Binomial Tree constructed above are computed using other appropriate conventional pricing methods (e.g. Discounted Cash Flow, Dividend Discount Model, Perpetuities, etc.)



## Appendix G – Cont'd

### 3. Compute Risk-Neutral Probability

A risk-neutral probability,  $p$ , which represents the probability for  $u$  to occur for each step, is then calculated using the formula below:

$$P(u) = \frac{e^{rt} - d}{u - d}$$

The probability for  $d$ ,  $P(d)$  is then calculated as:

$$P(d) = 1 - P(u)$$

### 4. Backward Induction

The expected value (often referred to as the risk neutral value) is then computed by working backward from two nodes to the node at the prior step. Below is the formula:

$$X_{t-1} = X_{ut} P(u) + X_{dt} P(d)$$

The above process is often combined with appropriate adjustments such as dividends, discounting or exercising of options. They are then repeated until a result is reached at the current period,  $X_0$ .



## APPENDIX H - COST OF EQUITY AND DISCOUNT RATE

### 1. Cost of Equity – Property Development

#### 1.1 Overview

The cost of equity of a Company is the rate of return required by equity investors. There are a number of theoretical risk and return models available to calculate the cost of equity. Of these the Capital Asset Pricing Model (**"CAPM"**) is the most widely used methodology for determining the cost of equity. The CAPM is based on the assumption that a rational investor will value an asset such that the expected rate of return is equal to the risk free rate of return plus a premium for the riskiness of the asset.

$$K_e = R_f + \beta(MRP) + \alpha$$

Where:

- $K_e$  = Cost of Equity
- $R_f$  = Risk Free Rate
- $MRP$  = Market Risk Premium
- $\beta$  = Beta (the systematic risk of a stock relative to the market portfolio)
- $\alpha$  = Alpha (size and other premia)

#### 1.2 Risk Free Rate

The risk free rate compensates the investor for the time value of money including the expected inflation rate over the investment period. In practice, for going concern Australian companies, the ten-year Commonwealth Government Bond rate is a widely used and accepted proxy for the risk free rate. This rate is a nominal rate and therefore includes inflation.

The current risk free rate (spot rate) is at or near an historical low and in view of the long term nature of the assets being valued is unrepresentative of the risk free rate. Accordingly, we have adopted the historical 5 year average ten-year Australian Government Bond rate as a proxy for the risk free rate in determining the cost of equity for PAYCE. According to data released by the Reserve Bank of Australia, the 5 year average rate is 4.17%.

#### 1.3 Market Risk Premium

The expected return on a market portfolio represents the return required by investors on equity securities. Therefore, the market risk premium ("MRP") is the difference between the expected rate of return on the market portfolio and the risk free rate. It represents the additional return that investors require to invest in equity securities, as compared to a risk free investment.

The MRP of the CAPM is the "expected" premium and is therefore unobservable. For practical reasons, the historical premium is generally used as a proxy for the MRP on the basis that a long term average return of what has been earned from equity investments would be a fair indication of what investors would expect to earn going forward with a medium to long term investment horizon.



## Appendix H – Cont'd

Whilst surveys and forecasts provide estimates of the MRP, the use of an appropriate historical time period is usually the best estimate of future performance.

The consensus is that the appropriate historical time period over which to measure the MRP is from the longest period over which quality financial data exists as equity returns in short time periods (generally less than 30 years) tend to be highly volatile. The risk premium required by the market is not constant and changes over time and therefore choosing the most recent data may over emphasise unusual events. At various stages of the market cycle, investors will perceive equities as being more risky than at other times and, as a consequence, they will adjust their required expected premium.

We have adopted MRP of 6% which is consistent with recent studies in calculating PAYCE's cost of equity.

### 1.4 Overall Beta

The beta coefficient is a measure of the expected volatility and therefore risk of a company's stock relative to the market portfolio.

The expected beta cannot be observed. Therefore, historical beta is usually used as a proxy for the expected beta.

The listed companies that may be considered approximately comparable to PAYCE are listed below:

| <b>Ticker</b>                     | <b>Name</b>                 | <b>Market Capital</b> | <b>Levered Beta</b> | <b>Debt/Equity</b> | <b>Asset Beta</b> |
|-----------------------------------|-----------------------------|-----------------------|---------------------|--------------------|-------------------|
| TWD                               | Tamawood Limited            | 91.50                 | 0.41                | 0.00%              | 0.415             |
| DVN                               | Devine Limited              | 150.00                | 0.73                | 59.45%             | 0.519             |
| LLC                               | Lend Lease Group            | 9263.64               | 0.64                | 26.40%             | 0.543             |
| SGP                               | Stockland Corp. Ltd.        | 11096.78              | 0.17                | 29.15%             | 0.145             |
| AVJ                               | AVJennings Limited          | 257.12                | 0.24                | 43.83%             | 0.182             |
| AOG                               | Aveo Group                  | 1153.81               | 0.88                | 140.68%            | 0.444             |
| AXI                               | Axiom Properties Ltd.       | 23.85                 | 0.56                | 80.30%             | 0.310             |
| CWP                               | Cedar Woods Properties Ltd. | 448.87                | 0.29                | 9.37%              | 0.266             |
| CNB                               | CIC Australia Limited       | 105.40                | 0.44                | 31.97%             | 0.335             |
| FRI                               | Finbar Group Limited        | 306.49                | 0.80                | 25.57%             | 0.641             |
| LIC                               | Lifestyle Communities Ltd   | 200.42                | 0.20                | 17.78%             | 0.170             |
| PBD                               | PBD Developments Limited    | 103.93                | 0.73                | 31.62%             | 0.556             |
| PPC                               | Peet Limited                | 535.76                | 0.53                | 60.34%             | 0.363             |
| SDG                               | Sunland Group Limited       | 306.41                | 0.09                | 27.53%             | 0.072             |
| VLW                               | Villa World Limited         | 224.04                | 0.66                | 31.73%             | 0.529             |
| <b>Industry Average</b>           |                             | <b>1617.87</b>        | <b>0.493</b>        | <b>41.05%</b>      | <b>0.366</b>      |
| <b>Selected Companies Average</b> |                             | <b>150.64</b>         | <b>0.530</b>        | <b>33.73%</b>      | <b>0.418</b>      |

Source: Capital IQ



## Appendix H – Cont'd

The above listed companies are involved in property development. No company is directly relevant to PAYCE in respect of its product and target market. However, in considering an appropriate asset beta, we have calculated the average beta for the most relevant companies (TWD, DVN, AVJ and PBD) to determine PAYCE's cost of equity.

We have selected these companies based on one or more of the below listed business activities which are relevant and comparable to PAYCE:

- Residential property development activities.
- Property development projects located in capital cities. (particularly Sydney and Brisbane)
- Townhouse or unit developments.
- Primarily operates in Australia.

The business activities of the most comparable companies are summarised as follows:

|                                 |         |  |
|---------------------------------|---------|--|
| <b>Tamawood Limited</b>         | ASX:TWD | Tamawood Limited (TWD) is an Australia-based company with four business activities: project home building; franchising and licensing; ready-to-occupy construction and sales, as well as a Renewable Energy Certificates origination and trading desks.  |
| <b>Devine Limited</b>           | ASX:DVN | Devine Limited (DVN) is an Australian residential developer offering housing products in QLD, VIC and SA. DVN is segmented by four specialised business units working together. These business segments are: Devine Communities, Devine Home Building, Devine Apartments & Mixed Use Developments and Devine Constructions.  |
| <b>AVJennings Limited</b>       | ASX:AVJ | AV Jennings Limited (AVJ) is an Australian based company, engaging in the land development, integrated housing and apartment development and home improvements. AVJ products and services include land, homes, townhomes, apartments, house and land packages, and investment properties. AVJ has projects in Australia and New Zealand.<br><br>There were 9,952 lots in AVJ's project pipeline as at 30 June 2014 (715 lots under development). The portfolio of lots by state consisted of VIC (31%), SA (28%), QLD (17%), NSW (19%) and New Zealand (5%). |
| <b>PBD Developments Limited</b> | ASX:PBD | PBD Developments Limited (PBD, formerly Port Bouvard Limited) is an Australian property developer focused on the development and sale of residential land and built-form products. The primary focus of the Company is on its development in the Mandurah/Peel Region of WA. PBD's current major projects include Bridgeview and Burwood Square in NSW; The Milton in QLD; Yang Land in VIC; Point Grey and Oceanique in WA.   |

Source: Morningstar





## Appendix H – Cont'd

Accordingly, we have adopted the asset beta of 0.418, the average asset beta of the most comparable companies.

PAYCE has a current debt covenant in relation to its issued corporate notes. At any time during the term of the Notes, PAYCE's leverage is not to exceed 62% under the terms of the Notes. We are advised that the management of the Company intends to maintain the leverage at approximately 50%. This translates to a debt to equity ratio of 100%. We have therefore re-levered the above asset beta applying a 100% target debt to equity ratio to obtain PAYCE's equity beta. Under the assumption of a 30% tax rate, the levered beta for PAYCE is calculated to be 0.71.

### 1.5 Alpha

It is a common practice to adjust for additional risk such as market volatility, country risk, liquidity risk and small company size risk. These are generally included as an alpha adjustment.

In this circumstance, we have considered the size and after risk factors particular to PAYCE, in terms of market capitalisation, is small compared to the overall market. We have applied a 1.75% to 2.25% alpha in calculating PAYCE's cost of equity.

### 1.6 Calculation

Applying the above:

Cost of Equity (Property Development) =  $4.17\% + 0.71(6\%) + 1.75\% = 10.18\%$

Cost of Equity (Property Development) =  $4.17\% + 0.71(6\%) + 2.25\% = 10.68\%$

## 2. Discount Rate

### 2.1 Overview

The discount rate used to equate the future cash flows to the present value reflects the risk adjusted rate of return demanded by a hypothetical investor for the asset or business being valued. Further, the discount rate represents an estimate of the weighted average cost of capital (WACC) appropriate for these assets. HCCF has calculated a WACC for each major business activity undertaken by PAYCE. That is, property development and property rental. The WACC for each is based on the weighted average cost of equity and the cost of debt. In determining the cost of equity for the respective cash flow from property development and property rental, we have referenced each area of the business to entities significantly involved in the respective activity. Accordingly, we have determined a WACC for property development and a WACC for property rental.

There are 3 main elements for the determination of an appropriate WACC. These are:

- Cost of Equity;
- Cost of Debt; and
- Debt/Equity Ratio



## Appendix H – Cont'd

The formula to determine WACC is as follows:

$$WACC = (R_e \times \frac{E}{V}) + (R_d \times (1 - t) \times \frac{D}{V})$$

Where:

- $E$  = value of equity
- $D$  = value of debt
- $V$  = total value of equity + debt
- $R_e$  = cost of equity
- $R_d$  = cost of debt
- $t$  = corporate tax rate

### 2.2 Cost of Equity

#### a) Property Development

The cost of equity for cash flow applicable to property development was determined on the same basis as Section 1 above.

#### b) Property Rental

We analysed listed entities which were substantially involved in property rental within the A-REIT sector. These companies are:

| Ticker                            | Name  | Levered Beta | Mkt. Val. Equity | Debt/Equity   | Asset Beta   |
|-----------------------------------|---|--------------|------------------|---------------|--------------|
| SCG                               | Scentre Group                               | -            | 20,609.0         | 65.44%        | -            |
| GMG                               | Goodman Group                               | 0.584        | 11,345.5         | 22.77%        | 0.496        |
| SGP                               | Stockland Corp. Ltd.                        | 0.175        | 11,096.8         | 29.15%        | 0.142        |
| GPT                               | GPT Group                                   | 0.118        | 8,511.9          | 33.63%        | 0.093        |
| NVN                               | Novion Property Group                       | 0.105        | 7,687.6          | 38.46%        | 0.081        |
| MGR                               | Mirvac Group                                | 0.337        | 7,793.9          | 32.70%        | 0.268        |
| DXS                               | Dexus Property Group                        | 0.305        | 7,236.0          | 46.04%        | 0.224        |
| FDC                               | Federation Centres                          | 0.322        | 4,354.3          | 33.05%        | 0.256        |
| IOF                               | Investa Office Fund                         | 0.267        | 2,566.7          | 37.37%        | 0.206        |
| CMW                               | Cromwell Property Group                     | 0.273        | 2,012.9          | 50.42%        | 0.196        |
| BWP                               | BWP Trust                                   | 0.225        | 1,944.8          | 23.86%        | 0.190        |
| CHC                               | Charter Hall Group                          | 0.675        | 1,740.3          | 0.02%         | 0.675        |
| ABP                               | Abacus Property Group                       | 0.278        | 1,697.7          | 40.79%        | 0.210        |
| CQR                               | Charter Hall Retail REIT                    | 0.175        | 1,633.3          | 43.24%        | 0.130        |
| SCP                               | Shopping Centres Australasia Property Group | 0.465        | 1,353.7          | 50.62%        | 0.332        |
| <b>Industry Average</b>           |   | <b>0.287</b> | <b>6,105.6</b>   | <b>36.50%</b> | <b>0.233</b> |
| <b>Selected Companies Average</b> |   | <b>0.235</b> | <b>4,579.9</b>   | <b>37.43%</b> | <b>0.182</b> |

Source: Capital IQ



## Appendix H – Cont'd

The above listed companies are involved in property rental. Each of the above entities has market capitalisation which is significantly larger than PAYCE. We have assessed the above highlighted entities to be most relevant to PAYCE in respect of its product and target market (Sydney). In considering an appropriate beta, we have calculated the average beta for these companies (GPT, NVN, FDC and ABP) to determine PAYCE's cost of equity for its property rental activities.

We have selected these companies based on one or more of the below listed business activities which are relevant and comparable to PAYCE:

- Commercial or retail rental activities.
- Commercial or retail rental activities for properties located in capital cities.
- Involvement or focus in the NSW market.
- Involvement in the QLD market
- Primarily operates in Australia.

The business activities of the most comparable companies are summarised as follows:

|                              |         |  |
|------------------------------|---------|--|
| <b>Novion Property Group</b> | ASX:NVN | Novion Property Group is an equity real estate investment trust is an equity real estate investment trust launched and managed by Novion RE Limited. The fund invests in the real estate markets of Australia. It makes investments in retail assets primarily in shopping centres and retail outlet centres. The fund benchmarks its performance against UBS Retail 200 Property Accumulation Index. It was formerly known as CFS Retail Property Trust Group. Novion Property Group was formed in 1994 and is domiciled in Australia.  |
| <b>Federation Centres</b>    | ASX:FDC | Centro Retail Australia is an independent equity real estate investment trust. The firm manages unlisted retail property funds and syndicates. It also provides property management, development; leasing and funds management services to the group's managed funds. The firm invests in the real estate markets of Australia. It primarily invests in Australian retail property with a focus on shopping centres. Centro Retail Australia was formed in 2011 and is domiciled in Melbourne, Australia.  |
| <b>Abacus Property Group</b> | ASX:ABP | Abacus Property Group engages in the management and investment of property based assets in Australia. It involves in property investment, funds management, property finance, and projects and investments activities. The company holds a diversified investment portfolio of retail, commercial industrial properties. In addition, Abacus Property Group develops originates, and manages off balance sheet funds; engages in mortgage lending and related property financing solutions; and invests in joint venture activities and in securities of other listed and unlisted property trusts. The company is based in Sydney, Australia. |

Source: Capital IQ



## Appendix H – Cont'd

Accordingly, we have adopted the asset beta of 0.182, the average beta of the most comparable companies.

As detailed above, we have re-levered the asset beta with the target debt structure (100% debt to equity ratio). The levered beta for PAYCE's property rental operation is calculated to be 0.31.

### 2.3 Calculation – Cost of Equity

Applying the CAPM formula:

$$\text{Cost of Equity (Property Rental)} = 4.17\% + 0.31(6\%) + 1.75\% = 7.78\%$$

$$\text{Cost of Equity (Property Rental)} = 4.17\% + 0.31(6\%) + 2.25\% = 8.28\%$$

### 2.4 Cost of Debt

Based on discussions with management, we have used the yield on the Notes (6.85%) as applicable and specific to the property rental operations.

In respect of the property development activities, project and other corporate debt are more widely sourced. After discussions with management and review of the Company's cost of debt generally, the cost of debt of 7.25% has been adopted having regard to the existing debt facilities and the margins reflected therein. HCCF believes that this would be a reasonable estimate including a margin that would match the duration of the cash flows assuming the operations were funded with a mixture of corporate and project debt.

### 2.5 Calculations – WACC (Mid-Point)

Applying the WACC formula and information set out above:

a) WACC - Property Development

$$\begin{aligned}\text{WACC} &= (10.43\% \times 50\%) + (7.25\% \times (1-30\%) \times 50\%) \\ &= 7.75\%\end{aligned}$$

b) Property Rental

$$\begin{aligned}\text{WACC} &= (8.03\% \times 50\%) + (6.85\% \times (1-30\%) \times 50\%) \\ &= 6.41\%\end{aligned}$$

### 2.6 Value Range Considerations

The above discount rates have been applied to the cash flows provided by PAYCE. It is usual to determine a narrow range of discounts that are relevant. However, for the purpose of this report and as a secondary methodology, we have adopted the median mid-point values as appropriate.



## APPENDIX I – DISCOUNTED DIVIDENDS OF PREFERENCE SHARES

At 10.25% Discount Rate:

| Quarter       | Coupon Rate | Coupon           | Discount Factor | Discounted Cashflow | Duration       |
|---------------|-------------|------------------|-----------------|---------------------|----------------|
| 1             | 6%          | \$ 0.1125        | 0.9750          | \$ 0.1097           | 0.0086         |
| 2             | 6%          | \$ 0.1125        | 0.9507          | \$ 0.1069           | 0.0167         |
| 3             | 6%          | \$ 0.1125        | 0.9269          | \$ 0.1043           | 0.0245         |
| 4             | 6%          | \$ 0.1125        | 0.9037          | \$ 0.1017           | 0.0318         |
| 5             | 7%          | \$ 0.1313        | 0.8812          | \$ 0.1157           | 0.0453         |
| 6             | 7%          | \$ 0.1313        | 0.8591          | \$ 0.1128           | 0.0530         |
| 7             | 7%          | \$ 0.1313        | 0.8377          | \$ 0.1099           | 0.0602         |
| 8             | 7%          | \$ 0.1313        | 0.8168          | \$ 0.1072           | 0.0671         |
| 9             | 8%          | \$ 0.1500        | 0.7963          | \$ 0.1195           | 0.0842         |
| 10            | 8%          | \$ 0.1500        | 0.7765          | \$ 0.1165           | 0.0912         |
| 11            | 8%          | \$ 0.1500        | 0.7571          | \$ 0.1136           | 0.0978         |
| 12            | 8%          | \$ 0.1500        | 0.7381          | \$ 0.1107           | 0.1040         |
| 13            | 9%          | \$ 0.1688        | 0.7197          | \$ 0.1214           | 0.1236         |
| 14            | 9%          | \$ 0.1688        | 0.7017          | \$ 0.1184           | 0.1298         |
| 15            | 9%          | \$ 0.1688        | 0.6842          | \$ 0.1155           | 0.1356         |
| 16            | 9%          | \$ 0.1688        | 0.6671          | \$ 0.1126           | 0.1410         |
| 17            | 10%         | \$ 0.1875        | 0.6504          | \$ 0.1220           | 0.1623         |
| 18            | 10%         | \$ 0.1875        | 0.6342          | \$ 0.1189           | 0.1675         |
| 19            | 10%         | \$ 0.1875        | 0.6183          | \$ 0.1159           | 0.1724         |
| 20            | 10%         | \$ 0.1875        | 0.6029          | \$ 0.1130           | 0.1770         |
| 21            | 11%         | \$ 0.2063        | 0.5878          | \$ 0.1212           | 0.1993         |
| 22            | 11%         | \$ 0.2063        | 0.5731          | \$ 0.1182           | 0.2036         |
| 23            | 11%         | \$ 0.2063        | 0.5588          | \$ 0.1153           | 0.2075         |
| 24            | 11%         | \$ 0.2063        | 0.5448          | \$ 0.1124           | 0.2111         |
| 25            | 12%         | \$ 0.2250        | 0.5312          | \$ 0.1195           | 0.2339         |
| 26            | 12%         | \$ 0.2250        | 0.5180          | \$ 0.1165           | 0.2372         |
| 27            | 12%         | \$ 0.2250        | 0.5050          | \$ 0.1136           | 0.2402         |
| 28            | 12%         | \$ 0.2250        | 0.4924          | \$ 0.1108           | 0.2428         |
| <b>*After</b> | <b>12%</b>  | <b>\$ 8.7805</b> | <b>0.4801</b>   | <b>\$ 4.2155</b>    | <b>9.3333</b>  |
|               |             |                  |                 | <u>\$ 7.4091</u>    | <u>13.0025</u> |

\* Perpetuity formula applied



## APPENDIX J – PROPERTY ASSETS VALUATION SUMMARY

| Property  | State | PAYCE Interest | JV Partner    | Basis of Valuation   | Carrying Value as at 31 Dec 2014 | Adjustment to Fair Market Value | Fair Market Value |
|---|-------|----------------|---------------|--|----------------------------------|---------------------------------|-------------------|
|   |       |                |               |  | \$'000                           | \$'000                          | \$'000            |
| <b>Property Development Assets</b>                        |       |                |               |  |                                  |                                 |                   |
| Marshall St, Bankstown                                    | NSW   | 100%           | N/A           | Put & Call Option Value *                                    | 3,004                            | (254)                           | 2,750             |
| Rasmussen, Townsville                                     | QLD   | 100%           | N/A           | Contract Price *   | 4,686                            | (1,537)                         | 3,149             |
| Riverwood, Pennsylvania Ave                               | NSW   | 100%           | N/A           | Contract Price *   | 4,880                            | (280)                           | 4,600             |
| Riverwood - Como  | NSW   | 100%           | N/A           | Independent Valuation + subsequent development Cost - Note 1 | 46,466                           | 3,218                           | 49,684            |
| Riverwood - Fairmont                                      | NSW   | 100%           | N/A           | Independent Valuation + subsequent development cost - Note 1 | 44,177                           | 3,914                           | 48,091            |
| Kirrawee - South Village, Sutherland                      | NSW   | 100%           | N/A           | Independent Valuation - Note 2                               | 72,498                           | 27,502                          | 100,000           |
| Other   | NSW   | 100%           | N/A           | Contract Price *   | 3,217                            | (3,217)                         | 0                 |
| Melrose Park  | NSW   | 50%            | Sekisui House | Contract Price *   | 62,944                           | (3,694)                         | 59,250            |
| Sydney Olympic Park Ferry Wharf                           | NSW   | 50%            | Sekisui House | Contract Price *   | 11,544                           | (1,354)                         | 10,190            |
| Platinum, Victoria Park                                   | NSW   | 50%            | DASCO         | Contract Price *   | 3,468                            | 0                               | 3,468             |
| Baulkham Hills  | NSW   | 60%            | DASCO         | Contract Price *   | 838                              | (370)                           | 468               |
| Auburn  | NSW   | 60%            | DASCO         | Contract Price *   | 4,737                            | (1,737)                         | 3,000             |
| Castle Hill   | NSW   | 60%            | DASCO         | Contract Price *   | 3,963                            | (243)                           | 3,720             |
| Paywin  | QLD   | 100%           | Wingate       | Contract Price *   | 9,256                            | (5,402)                         | 3,853             |
| Ermington   | NSW   | 50%            | Sekisui House | Independent Valuation - Note 3                               | 17,772                           | 32,228                          | 50,000            |
| West End  | QLD   | 50%            | Sekisui House | Independent Valuation - Note 4                               | 28,167                           | (5,667)                         | 22,500            |
| Lot3, Wentworth Point                                     | NSW   | 50%            | Sekisui House | Independent Valuation - Note 5                               | 18,907                           | 22,343                          | 41,250            |
| <b>Total Property Development Asset Fair Market Value</b> |       |                |               |  | <b>340,524</b>                   | <b>65,450</b>                   | <b>405,973</b>    |
| <b>Total Property Development Liabilities</b>             |       |                |               |  |                                  |                                 | <b>(196,471)</b>  |
| <b>NETT Property Development Asset Fair Market Value</b>  |       |                |               |  |                                  |                                 | <b>209,503</b>    |



| Property  | State | PAYCE Interest | JV Partner | Basis of Valuation             | Carrying Value as at 31 Dec 2014 | Adjustment to Fair Market Value | Fair Market Value |
|---|-------|----------------|------------|--------------------------------|----------------------------------|---------------------------------|-------------------|
| <b>Investment Assets</b>                        |       |                |            |                                |                                  |                                 |                   |
| East Village, Victoria Park                     | NSW   | 95%            | N/A        | Independent Valuation - Note 6 | 235,000                          | (19,212)                        | 215,788           |
| Apex Retail, Victoria Park                      | NSW   | 100%           | N/A        | Independent Valuation - Note 7 | 2,161                            | (161)                           | 2,000             |
| <b>Total Investment Asset Fair Market Value</b> |       |                |            |                                | <b>237,161</b>                   | <b>(19,373)</b>                 | <b>217,788</b>    |
| <b>Total Investment Liabilities</b>             |       |                |            |                                |                                  |                                 | <b>(115,532)</b>  |
| <b>NETT Investment Assets Fair Market Value</b> |       |                |            |                                |                                  |                                 | <b>102,256</b>    |
| <b>Total NETT Fair Market Value</b>             |       |                |            |                                |                                  |                                 | <b>311,759</b>    |

**Contract Price \*** The carrying value of these assets has been adjusted by deducting currently non-recoverable acquisition costs, holding costs and other associated development application costs & fees to arrive at Fair Market Value

**Note 1** Development land associated with the Como and Fairmont projects were independently valued by Colliers International (January 2014) for first mortgage purposes on an "as is" basis at \$6.5m and \$11.8m respectively

**Note 2** Development land associated with the Kirrawee project was independently valued by M3 Property Strategists (February 2015) on an "as is" basis for \$100m

**Note 3** Development land associated with the Ermington project was independently valued by Landmark White (January 2014) for first mortgage purposes on an "as is" basis for \$100m

**Note 4** Development land associated with the Westend project was independently valued by Colliers (March 2014) for first mortgage purposes on an "as is" basis for \$45m

**Note 5** Development land associated with the Lot 3, Wentworth Point project was independently valued by Landmark White (September 2014) for first mortgage purposes on an "as is" basis for \$82.5m

**Note 6** The East Village retail/commercial investment asset was independently valued by Colliers International (October 2014) for first mortgage purposes on a capitalisation and discounted cashflow basis for \$235m

**Note 7** The APEX retail investment asset was independently valued by Colliers International (December 2012) for stamp duty purposes on a direct comparison basis for \$2m



## APPENDIX K – CONTROL PREMIUMS

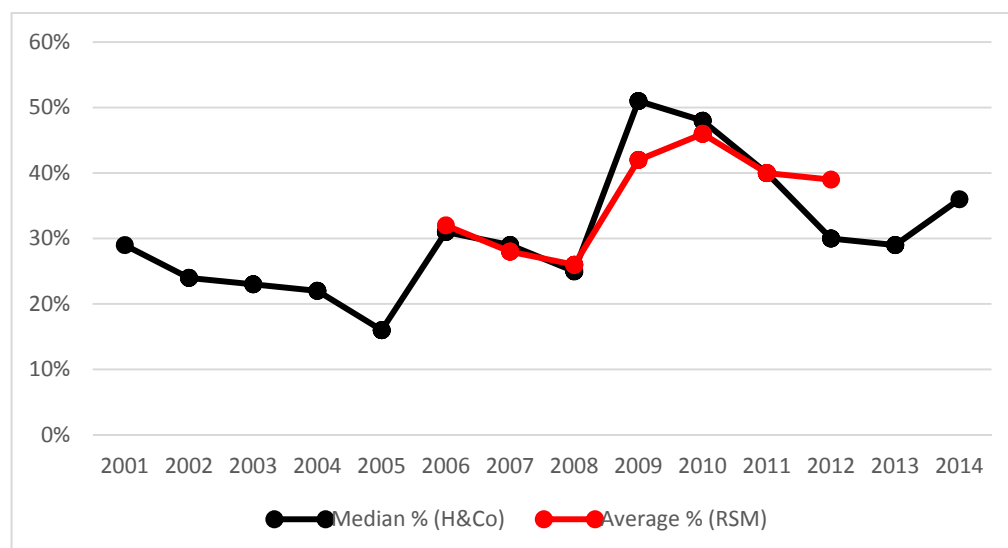
### CONTROL PREMIUMS

The generally accepted way of quantifying control premiums has been to compare the pre-bid or pre-offer price of the company being acquired with the offer or transaction price. The difference, calculated as a percentage of the publically traded share price (the minority interest price) is the control premium. The control premium reflects:

- (a) the value of benefits that can be derived through obtaining control of the business; and may also reflect
- (b) special benefits attributable to synergies based on the 20 day pre-bid price.

Recent studies of the 20 day pre-bid price by RSM Bird Cameron (RSM) and Halligan & Co (H&Co) (extracted from data sourced from Connect4) show the following:

| STUDY   | PERIOD OF STUDY | NO OF TRANSACTIONS | MEDIAN TAKEOVER PREMIUM |
|---|-----------------|--------------------|-------------------------|
| (1)Bird Cameron   | 2006 – 2012     | 345                | 35.3%                   |
| (2)Halligan & Co  | 2000 – 2014     | 605                | 30%                     |
| (1)Control Premium Study 2013<br>(2)Control Premium Research 2014 |                 |                    |                         |



| Year            | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 |
|-----------------|------|------|------|------|------|------|------|------|------|------|------|------|------|------|
| Median % (H&Co) | 29%  | 24%  | 23%  | 22%  | 16%  | 31%  | 29%  | 25%  | 51%  | 48%  | 40%  | 30%  | 29%  | 36%  |
| Average % (RSM) |      |      |      |      |      | 32%  | 28%  | 26%  | 42%  | 46%  | 40%  | 39%  |      |      |





## **Appendix K – Cont'd**

Typical control premiums are in the order of 25% - 40%. Within this range premiums vary year on year and for different industries but the long term median has generally been around 30%. In addition the RSM study noted the average of 22 transactions in the real estate industry for the period 2006-2012 was 20.7%.

### **Minority Interest Discount Formula:**

$$1 - \left[ \frac{1}{1 + \text{Control Premium}} \right]$$



## APPENDIX L - BINOMIAL TREES – DISCOUNT RATE

R=10.25%

| Quarter |  | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 | 11 | 12 | 13 | 14 | 15 | 16 | 17 | 18 | 19 | 20 | 21 | 22 | 23 | 24 | 25 | 26 | 27     | 28     |
|---------|--|---|---|---|---|---|---|---|---|---|----|----|----|----|----|----|----|----|----|----|----|----|----|----|----|----|----|--------|--------|
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |        | 91.55% |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 84.42% | 77.84% |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 71.78% | 66.19% |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 66.19% | 61.03% |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 61.03% | 56.28% |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 56.28% | 51.89% |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 51.89% | 47.85% |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 47.85% | 44.12% |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 44.12% | 40.69% |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 40.69% | 37.52% |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 37.52% | 34.60% |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 34.60% | 31.90% |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 31.90% | 29.42% |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 29.42% | 27.12% |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 27.12% | 25.01% |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 25.01% | 23.06% |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 23.06% | 21.27% |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 21.27% | 19.61% |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 19.61% | 18.08% |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 18.08% | 16.67% |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 16.67% | 15.38% |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 15.38% | 14.18% |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 14.18% | 13.07% |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 13.07% | 12.05% |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 12.05% | 11.12% |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 11.12% | 10.25% |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 10.25% | 9.45%  |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 9.45%  | 8.72%  |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 8.72%  | 8.04%  |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 8.04%  | 7.41%  |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 7.41%  | 6.83%  |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 6.83%  | 6.30%  |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 6.30%  | 5.81%  |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 5.81%  | 5.36%  |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 5.36%  | 4.94%  |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 4.94%  | 4.56%  |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 4.56%  | 4.20%  |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 4.20%  | 3.87%  |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 3.87%  | 3.57%  |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 3.57%  | 3.29%  |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 3.29%  | 3.04%  |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 3.04%  | 2.80%  |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 2.80%  | 2.58%  |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 2.58%  | 2.38%  |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 2.38%  | 2.20%  |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 2.20%  | 2.02%  |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 2.02%  | 1.87%  |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 1.87%  | 1.72%  |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 1.72%  | 1.59%  |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 1.59%  | 1.46%  |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 1.46%  | 1.35%  |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 1.35%  | 1.24%  |
|         |  |   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    |    | 1.24%  | 1.15%  |



## APPENDIX L - BINOMIAL TREES – HYPOTHETICAL BOND (OPTION-FREE)

| Quarter |         | 1       | 2       | 3       | 4       | 5       | 6        | 7        | 8        | 9        | 10       | 11       | 12       | 13       | 14       | 15       | 16       | 17       | 18       | 19       | 20       | 21       | 22       | 23       | 24       | 25       | 26       | 27       | 28       |          |          |
|---------|---------|---------|---------|---------|---------|---------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|
|         |         |         |         |         |         |         |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          | \$ 1.27  | \$ 1.21  |          |          |
|         |         |         |         |         |         |         |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          | \$ 1.35  | \$ 1.38  |          |          |
|         |         |         |         |         |         |         |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          | \$ 1.43  | \$ 1.46  | \$ 1.58  |          |          |          |          |
|         |         |         |         |         |         |         |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          | \$ 1.57  | \$ 1.72  | \$ 1.64  | \$ 1.67  | \$ 1.82  |          |          |          |          |
|         |         |         |         |         |         |         |          |          |          |          |          |          |          |          |          |          |          |          |          |          | \$ 1.76  | \$ 1.91  | \$ 1.81  | \$ 1.88  | \$ 1.77  | \$ 1.93  | \$ 2.11  |          |          |          |          |
|         |         |         |         |         |         |         |          |          |          |          |          |          |          |          |          |          |          |          | \$ 1.94  | \$ 2.03  | \$ 2.09  | \$ 2.09  | \$ 1.98  | \$ 2.17  | \$ 2.04  | \$ 2.23  | \$ 2.44  |          |          |          |          |
|         |         |         |         |         |         |         |          |          |          |          |          |          |          |          |          | \$ 2.28  | \$ 2.17  | \$ 2.37  | \$ 2.24  | \$ 2.46  | \$ 2.56  | \$ 2.42  | \$ 2.65  | \$ 2.51  | \$ 2.74  | \$ 2.58  | \$ 2.83  |          |          |          |          |
|         |         |         |         |         |         |         |          |          |          |          |          |          |          | \$ 2.54  | \$ 2.40  | \$ 2.64  | \$ 2.51  | \$ 2.75  | \$ 2.60  | \$ 2.71  | \$ 2.97  | \$ 2.80  | \$ 2.91  | \$ 3.18  | \$ 3.00  | \$ 3.28  |          |          |          |          |          |
|         |         |         |         |         |         |         |          |          |          |          |          | \$ 2.82  | \$ 3.12  | \$ 2.95  | \$ 3.25  | \$ 3.07  | \$ 3.39  | \$ 3.20  | \$ 3.51  | \$ 3.32  | \$ 3.66  | \$ 3.45  | \$ 3.78  | \$ 3.57  | \$ 3.93  | \$ 3.70  | \$ 4.06  | \$ 3.82  |          |          |          |
|         |         |         |         |         |         |         |          |          |          | \$ 3.15  | \$ 3.48  | \$ 3.29  | \$ 3.64  | \$ 3.44  | \$ 3.78  | \$ 3.58  | \$ 3.95  | \$ 3.72  | \$ 4.09  | \$ 3.87  | \$ 4.01  | \$ 4.41  | \$ 4.16  | \$ 4.31  | \$ 4.73  | \$ 4.46  |          |          |          |          |          |
|         |         |         |         |         |         |         |          | \$ 3.51  | \$ 3.33  | \$ 3.68  | \$ 3.48  | \$ 3.84  | \$ 4.01  | \$ 4.17  | \$ 4.34  | \$ 4.51  | \$ 4.60  | \$ 4.77  | \$ 4.96  | \$ 4.68  | \$ 5.14  | \$ 4.85  | \$ 5.34  | \$ 5.02  | \$ 5.52  | \$ 5.20  |          |          |          |          |          |
|         |         |         |         |         |         | \$ 3.93 | \$ 3.71  | \$ 4.11  | \$ 3.90  | \$ 4.30  | \$ 4.06  | \$ 4.49  | \$ 4.25  | \$ 4.68  | \$ 4.87  | \$ 5.06  | \$ 5.37  | \$ 5.06  | \$ 5.57  | \$ 5.26  | \$ 5.46  | \$ 5.14  | \$ 5.66  | \$ 5.34  | \$ 5.87  | \$ 5.52  | \$ 6.08  |          |          |          |          |
|         |         |         |         | \$ 4.39 | \$ 4.16 | \$ 4.60 | \$ 4.35  | \$ 4.81  | \$ 4.55  | \$ 5.03  | \$ 4.75  | \$ 5.24  | \$ 4.96  | \$ 5.46  | \$ 5.15  | \$ 5.68  | \$ 5.37  | \$ 5.91  | \$ 5.57  | \$ 6.14  | \$ 5.79  | \$ 6.00  | \$ 6.61  | \$ 6.24  | \$ 6.86  | \$ 6.45  | \$ 7.11  |          |          |          |          |
|         |         |         | \$ 4.91 | \$ 4.64 | \$ 4.87 | \$ 5.39 | \$ 5.09  | \$ 5.64  | \$ 5.33  | \$ 5.88  | \$ 5.55  | \$ 6.13  | \$ 5.80  | \$ 6.39  | \$ 6.02  | \$ 6.65  | \$ 6.27  | \$ 6.91  | \$ 6.51  | \$ 6.77  | \$ 7.18  | \$ 6.77  | \$ 7.45  | \$ 7.02  | \$ 7.29  | \$ 7.55  | \$ 8.32  |          |          |          |          |
|         | \$ 5.20 | \$ 4.91 | \$ 5.45 | \$ 5.15 | \$ 5.72 | \$ 5.39 | \$ 5.97  | \$ 5.64  | \$ 6.24  | \$ 5.88  | \$ 6.50  | \$ 6.13  | \$ 6.78  | \$ 6.39  | \$ 7.05  | \$ 6.65  | \$ 7.34  | \$ 6.91  | \$ 7.61  | \$ 7.18  | \$ 7.92  | \$ 7.45  | \$ 8.21  | \$ 7.73  | \$ 8.53  | \$ 8.02  | \$ 8.84  | \$ 8.32  |          |          |          |
|         |         | \$ 5.77 | \$ 6.40 | \$ 6.04 | \$ 6.70 | \$ 6.32 | \$ 7.00  | \$ 6.60  | \$ 7.31  | \$ 6.89  | \$ 7.61  | \$ 7.18  | \$ 7.93  | \$ 7.47  | \$ 8.25  | \$ 7.78  | \$ 8.59  | \$ 8.08  | \$ 8.91  | \$ 8.40  | \$ 9.27  | \$ 8.72  | \$ 9.61  | \$ 9.05  | \$ 9.99  | \$ 9.39  | \$ 10.36 | \$ 9.75  |          |          |          |
|         |         |         |         | \$ 7.10 | \$ 7.42 | \$ 7.74 | \$ 8.20  | \$ 7.74  | \$ 8.57  | \$ 8.07  | \$ 8.92  | \$ 8.41  | \$ 9.29  | \$ 8.75  | \$ 9.66  | \$ 9.10  | \$ 10.05 | \$ 9.46  | \$ 10.44 | \$ 9.83  | \$ 10.85 | \$ 10.21 | \$ 11.26 | \$ 10.60 | \$ 11.70 | \$ 11.01 | \$ 12.14 | \$ 11.42 |          |          |          |
|         |         |         |         |         | \$ 8.70 | \$ 9.08 | \$ 9.46  | \$ 10.04 | \$ 9.46  | \$ 10.45 | \$ 9.85  | \$ 10.89 | \$ 10.25 | \$ 11.32 | \$ 10.66 | \$ 11.78 | \$ 11.09 | \$ 12.23 | \$ 11.52 | \$ 12.72 | \$ 11.97 | \$ 13.20 | \$ 12.43 | \$ 13.72 | \$ 12.90 | \$ 14.24 | \$ 13.40 |          |          |          |          |
|         |         |         |         |         |         |         | \$ 10.65 | \$ 11.09 | \$ 10.45 | \$ 11.55 | \$ 10.89 | \$ 12.02 | \$ 11.32 | \$ 12.50 | \$ 11.78 | \$ 13.01 | \$ 12.26 | \$ 13.50 | \$ 12.72 | \$ 14.03 | \$ 13.20 | \$ 14.57 | \$ 13.72 | \$ 15.13 | \$ 14.24 | \$ 15.72 |          |          |          |          |          |
|         |         |         |         |         |         |         |          | \$ 11.78 | \$ 11.09 | \$ 12.26 | \$ 11.55 | \$ 12.77 | \$ 12.02 | \$ 13.27 | \$ 12.50 | \$ 13.81 | \$ 13.01 | \$ 14.38 | \$ 13.55 | \$ 14.97 | \$ 14.15 | \$ 15.62 | \$ 14.79 | \$ 16.26 | \$ 15.43 | \$ 16.90 | \$ 16.07 | \$ 17.65 |          |          |          |
|         |         |         |         |         |         |         |          |          | \$ 13.01 | \$ 12.26 | \$ 13.55 | \$ 12.77 | \$ 14.09 | \$ 13.27 | \$ 14.66 | \$ 13.81 | \$ 15.19 | \$ 14.38 | \$ 15.86 | \$ 15.03 | \$ 16.51 | \$ 15.68 | \$ 17.26 | \$ 16.43 | \$ 18.01 | \$ 17.18 | \$ 18.85 | \$ 17.92 |          |          |          |
|         |         |         |         |         |         |         |          |          |          | \$ 15.89 | \$ 14.97 | \$ 16.54 | \$ 15.57 | \$ 17.20 | \$ 15.78 | \$ 17.57 | \$ 16.54 | \$ 18.26 | \$ 17.20 | \$ 19.00 | \$ 17.88 | \$ 19.74 | \$ 18.58 | \$ 20.53 | \$ 19.31 | \$ 21.26 | \$ 20.06 | \$ 22.01 | \$ 20.75 |          |          |
|         |         |         |         |         |         |         |          |          |          |          | \$ 17.57 | \$ 16.54 | \$ 18.26 | \$ 17.20 | \$ 19.00 | \$ 17.88 | \$ 19.74 | \$ 18.58 | \$ 20.53 | \$ 19.31 | \$ 21.26 | \$ 20.06 | \$ 22.01 | \$ 20.75 | \$ 22.66 | \$ 21.43 | \$ 23.38 | \$ 22.15 | \$ 24.00 | \$ 22.65 |          |
|         |         |         |         |         |         |         |          |          |          |          |          | \$ 19.41 | \$ 18.26 | \$ 20.18 | \$ 19.00 | \$ 21.00 | \$ 19.74 | \$ 21.88 | \$ 20.53 | \$ 22.66 | \$ 21.43 | \$ 23.55 | \$ 22.32 | \$ 24.57 | \$ 23.34 | \$ 25.59 | \$ 24.36 | \$ 26.61 | \$ 25.38 | \$ 27.63 |          |
|         |         |         |         |         |         |         |          |          |          |          |          |          | \$ 21.44 | \$ 20.18 | \$ 22.30 | \$ 21.00 | \$ 23.00 | \$ 21.74 | \$ 23.97 | \$ 22.66 | \$ 24.99 | \$ 23.76 | \$ 26.11 | \$ 24.88 | \$ 27.25 | \$ 26.02 | \$ 28.27 | \$ 27.04 | \$ 29.30 | \$ 28.07 |          |
|         |         |         |         |         |         |         |          |          |          |          |          |          |          | \$ 23.69 | \$ 22.30 | \$ 24.63 | \$ 23.17 | \$ 25.60 | \$ 24.15 | \$ 26.61 | \$ 25.16 | \$ 27.66 | \$ 26.21 | \$ 28.71 | \$ 27.26 | \$ 29.81 | \$ 28.36 | \$ 30.91 | \$ 29.46 |          |          |
|         |         |         |         |         |         |         |          |          |          |          |          |          |          |          | \$ 26.18 | \$ 24.63 | \$ 27.21 | \$ 25.60 | \$ 28.19 | \$ 26.61 | \$ 29.20 | \$ 27.66 | \$ 30.25 | \$ 28.71 | \$ 31.30 | \$ 29.76 | \$ 32.35 | \$ 30.81 | \$ 33.40 |          |          |
|         |         |         |         |         |         |         |          |          |          |          |          |          |          |          |          | \$ 28.92 | \$ 27.21 | \$ 30.06 | \$ 28.29 | \$ 31.25 | \$ 29.39 | \$ 32.48 | \$ 30.56 | \$ 33.65 | \$ 31.73 | \$ 34.82 | \$ 32.90 | \$ 36.07 | \$ 34.15 |          |          |
|         |         |         |         |         |         |         |          |          |          |          |          |          |          |          |          |          |          | \$ 31.95 | \$ 30.06 | \$ 33.23 | \$ 31.25 | \$ 34.53 | \$ 32.48 | \$ 35.77 | \$ 33.73 | \$ 37.99 | \$ 35.95 | \$ 39.20 | \$ 37.16 |          |          |
|         |         |         |         |         |         |         |          |          |          |          |          |          |          |          |          |          |          |          | \$ 35.31 | \$ 33.23 | \$ 36.71 | \$ 34.53 | \$ 38.15 | \$ 35.95 | \$ 39.66 | \$ 37.43 | \$ 41.19 | \$ 38.96 | \$ 42.70 | \$ 40.47 |          |
|         |         |         |         |         |         |         |          |          |          |          |          |          |          |          |          |          |          |          |          | \$ 39.03 | \$ 36.71 | \$ 40.56 | \$ 38.15 | \$ 41.19 | \$ 38.96 | \$ 42.70 | \$ 40.47 | \$ 44.21 | \$ 41.98 | \$ 45.72 |          |
|         |         |         |         |         |         |         |          |          |          |          |          |          |          |          |          |          |          |          |          |          | \$ 43.13 | \$ 40.56 | \$ 44.83 | \$ 42.17 | \$ 46.60 | \$ 44.21 | \$ 48.32 | \$ 45.93 | \$ 50.64 | \$ 48.25 |          |
|         |         |         |         |         |         |         |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          | \$ 47.66 | \$ 44.83 | \$ 49.55 | \$ 46.60 | \$ 51.50 | \$ 48.32 | \$ 53.21 | \$ 50.03 | \$ 55.74 |          |
|         |         |         |         |         |         |         |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          | \$ 52.68 | \$ 49.55 | \$ 54.76 | \$ 51.50 | \$ 56.92 | \$ 53.66 | \$ 60.53 | \$ 57.27 |          |
|         |         |         |         |         |         |         |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          | \$ 58.23 | \$ 54.76 | \$ 60.53 | \$ 57.27 | \$ 64.36 | \$ 61.09 | \$ 67.82 | \$ 64.55 |
|         |         |         |         |         |         |         |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          | \$ 64.36 | \$ 60.53 | \$ 67.82 | \$ 64.55 | \$ 71.14 | \$ 67.82 |
|         |         |         |         |         |         |         |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          |          | \$ 78.65 |          |          |



## APPENDIX L - BINOMIAL TREES – HYPOTHETIC BOND (OPTION-BEARING)

[illegible]



# Financial Services Guide

## 1. Hanrick Curran Corporate Finance Pty Ltd

Hanrick Curran Corporate Finance Pty Ltd ("HCCF") carries on a business, and has a registered office, at Level 11, 307 Queen Street, Brisbane QLD 4001. HCCF holds Australian Financial Services License No 467461 authorising it to provide financial product advice in relation to securities to wholesale and retail clients.

HCCF has been engaged by PAYCE Consolidated Limited ("PAYCE" or "the Company") to provide general financial product advice in the form of an independent expert's report to the Proposed Buy-back. This Report is to be included in the Company's Notice of Meeting and Explanatory Memorandum.

## 2. Financial Services Guide

This Financial Services Guide ("FSG") has been prepared in accordance with Corporations Act, 2001 and provides important information to help retail clients make decision as to their use of the general financial product advice in a report, the services we offer, information about us, our dispute resolution process and how we are remunerated.

## 3. General financial product advice.

In our Report we provide general financial product advice. The advice in a report does not take into account your personal objectives, financial situation or needs.

HCCF does not accept instruction from retail clients. HCCF provides no financial services directly to retail clients and receives no remuneration from retail clients for financial services. HCCF does not provide any personal retail financial product advice directly to retail investors nor does it provide market-related advice directly to retail investors.

## 4. Remuneration

When providing the Report, HCCF's client is the Company. HCCF receives its remuneration from the Company. In respect of the Report, HCCF will receive from PAYCE a fixed fee of \$45,000 plus GST, which is based on a commercial rate plus reimbursement of out-of-pocket expenses for the preparation of the Report. Our directors and employees providing financial services receive an annual salary, a performance based bonus or profit share depending on their level of seniority.

Except for the fees referred to above, no related body corporate of HCCF or any directors, employees or any associated entities receives any other remuneration or other benefit directly or indirectly for or in connection with the provision of this Report.

## 5. Independence

HCCF is required to be independent of PAYCE in order to provide this Report. The guidelines for independence in the preparation of independence expert's report are set out in Regulatory Guide 112 *Independence of experts* issued by the Australian Securities and Investments Commission ("ASIC"). The following information in relation to the independence of HCCF is stated below.

*"HCCF and its related entities do not have at the date of this Report, and have not had within the previous two years, any shareholding in or other relationship with PAYCE (and associated entities)*



*that could reasonably be regarded as capable of affecting its ability to provide an unbiased opinion in relation the transaction.*

*HCCF has no involvement with, or interest in the outcome of the transaction, other than the preparation of this Report.*

*HCCF will receive a fee based on commercial rates for the preparation of this report. This fee is not contingent on the outcome of this transaction. HCCF's out of pocket expenses in relation to the preparation of the Report will be reimbursed. HCCF will receive no other benefit for the preparation of this Report.*

*HCCF considers itself to be independent in terms of Regulatory Guide 112 Independence of experts issued by the ASIC.*

## **6. Complaints process**

HCCF has an internal complaint handling mechanism and is a member of the Financial Ombudsman Service (membership no. 34891). All complaints must be in writing and addressed to the Managing Director at HCCF. We will endeavor to resolve all complaints within 30 days of receiving the complaint. If the complaint has not been satisfactorily dealt with, the complaint can be referred to the financial Ombudsman Service who can be contacted at:

PO Box 579 – Collins Street West  
Melbourne, VIC 8007  
Telephone: 1800 335 405

HCCF is only responsible for this Report and FSG. Complaints or questions about the General Meeting should not be directed to HCCF. HCCF will not be responsible in any way that might involve any provision of financial product advice to any retail investor.

## **7. Compensation**

HCCF has professional indemnity insurance cover under its professional indemnity insurance policy. This policy meets the compensation arrangement requirements of section 912B of the Corporations Act, 2001.

# CORPORATE DIRECTORY

## SHARE REGISTRY

For general queries, please contact:

| POSTAL ADDRESS   | FAX             | PHONE        |
|--|-----------------|--------------|
| Boardroom Pty Limited<br>GPO Box 3993<br>Sydney NSW 2001 | +61 2 9290 9655 | 1300 737 760 |



PAYCE Consolidated Limited  
ABN 19 001 566 310



#### All Correspondence to:

✉ **By Mail** Boardroom Pty Limited  
GPO Box 3993  
Sydney NSW 2001 Australia  
  
Level 7, 207 Kent Street,  
Sydney NSW 2000 Australia  
  
📠 **By Fax:** +61 2 9290 9655  
  
💻 **Online:** [www.boardroomlimited.com.au](http://www.boardroomlimited.com.au)  
  
☎ **By Phone:** (within Australia) 1300 737 760  
(outside Australia) +61 2 9290 9600

## YOUR VOTE IS IMPORTANT

For your vote to be effective it must be recorded **before 2.30pm AEST on Saturday 2 May 2015.**

### 💻 TO VOTE ONLINE

### 📱 BY SMARTPHONE

**STEP 1:** VISIT [www.votingonline.com.au/payceegm2015](http://www.votingonline.com.au/payceegm2015)

**STEP 2:** Enter your holding/investment type:

**STEP 3:** Enter your Reference Number:

**STEP 4:** Enter your Voting Access Code:



Scan QR Code using smartphone  
QR Reader App

**PLEASE NOTE:** For security reasons it is important you keep the above information confidential.

### TO VOTE BY COMPLETING THE PROXY FORM

#### STEP 1 APPOINTMENT OF PROXY

Indicate who you want to appoint as your Proxy.

If you wish to appoint the Chairman of the Meeting as your proxy, mark the box. If you wish to appoint someone other than the Chairman of the Meeting as your proxy please write the full name of that individual or body corporate. If you leave this section blank, or your named proxy does not attend the meeting, the Chairman of the Meeting will be your proxy. A proxy need not be a security holder of the company. Do not write the name of the issuer company or the registered securityholder in the space.

##### Appointment of a Second Proxy

You are entitled to appoint up to two proxies to attend the meeting and vote. If you wish to appoint a second proxy, an additional Proxy Form may be obtained by contacting the company's securities registry or you may copy this form.

To appoint a second proxy you must:

- (a) complete two Proxy Forms. On each Proxy Form state the percentage of your voting rights or the number of securities applicable to that form. If the appointments do not specify the percentage or number of votes that each proxy may exercise, each proxy may exercise half your votes. Fractions of votes will be disregarded; and
- (b) return both forms together in the same envelope.

#### STEP 2 VOTING DIRECTIONS TO YOUR PROXY

To direct your proxy how to vote, mark one of the boxes opposite each item of business. All your securities will be voted in accordance with such a direction unless you indicate only a portion of securities are to be voted on any item by inserting the percentage or number that you wish to vote in the appropriate box or boxes. If you do not mark any of the boxes on a given item, your proxy may vote as he or she chooses. If you mark more than one box on an item for all your securities your vote on that item will be invalid.

##### Proxy which is a Body Corporate

Where a body corporate is appointed as your proxy, the representative of that body corporate attending the meeting must have provided an "Appointment of Corporate Representative" prior to admission. An Appointment of Corporate Representative form can be obtained from the company's securities registry.

#### STEP 3 SIGN THE FORM

The form **must** be signed as follows:

**Individual:** This form is to be signed by the securityholder.

**Joint Holding:** where the holding is in more than one name, all the securityholders should sign.

**Power of Attorney:** to sign under a Power of Attorney, you must have already lodged it with the registry. Alternatively, attach a certified photocopy of the Power of Attorney to this form when you return it.

**Companies:** this form must be signed by a Director jointly with either another Director or a Company Secretary. Where the company has a Sole Director who is also the Sole Company Secretary, this form should be signed by that person. **Please indicate the office held by signing in the appropriate place.**

#### STEP 4 LODGEMENT

Proxy forms (and any Power of Attorney under which it is signed) must be received no later than 48 hours before the commencement of the meeting, therefore by **2.30pm AEST on Saturday 2 May 2015**. Any Proxy Form received after that time will not be valid for the scheduled meeting.

Proxy forms may be lodged using the enclosed Reply Paid Envelope or:

💻 **Online** [www.votingonline.com.au/payceegm2015](http://www.votingonline.com.au/payceegm2015)

📠 **By Fax** + 61 2 9290 9655

✉ **By Mail** Boardroom Pty Limited  
GPO Box 3993,  
Sydney NSW 2001 Australia

👤 **In Person** Level 7, 207 Kent Street,  
Sydney NSW 2000 Australia

#### Attending the Meeting

If you wish to attend the meeting please bring this form with you to assist registration.



☐**Your Address**

This is your address as it appears on the company's share register. If this is incorrect, please mark the box with an "X" and make the correction in the space to the left. Securityholders sponsored by a broker should advise their broker of any changes. **Please note, you cannot change ownership of your securities using this form.**

**PROXY FORM****STEP 1 APPOINT A PROXY**

I/We being a member/s of **PAYCE Consolidated Limited** and entitled to attend and vote hereby appoint

☐

**Chairman of the Meeting (mark box)**

**OR** if you are **NOT** appointing the Chairman of the Meeting as your proxy, please write the name of the person or body corporate (excluding the registered shareholder) you are appointing as your proxy below

or failing the individual or body corporate named, or if no individual or body corporate is named, the Chairman of the Meeting as my/our proxy at the Extraordinary General Meeting of **PAYCE Consolidated Limited** to be held at **Pulse, 9 The Crescent, Wentworth Point NSW 2127 at 2.30pm AEST on Monday 4 May 2015** and at any adjournment of that meeting, to act on my/our behalf and to vote in accordance with the following directions or if no directions have been given, as the proxy sees fit.

The Chairman of the Meeting will vote all undirected proxies in favour of all Items of business. If you wish to appoint the Chairman of the Meeting as your proxy with a direction to vote against, or to abstain from voting on an item, you must provide a direction by marking the 'Against' or 'Abstain' box opposite that resolution.

**STEP 2 VOTING DIRECTIONS**

\* If you mark the Abstain box for a particular item, you are directing your proxy not to vote on your behalf on a show of hands or on a poll and your vote will not be counted in calculating the required majority if a poll is called.

|        |   | For                      | Against                  | Abstain*                 |
|--------|---|--------------------------|--------------------------|--------------------------|
| Item 1 | Approval of Share Buy-Back                  | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> |
| Item 2 | Approval for the issue of Preference Shares | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> |

**STEP 3 SIGNATURE OF SHAREHOLDER(S)**

This form must be signed to enable your directions to be implemented.

Individual or Securityholder 1

Sole Director and Sole Company Secretary

Securityholder 2

Director

Securityholder 3

Director / Company Secretary

Contact Name.....

Contact Daytime Telephone.....

Date / / 2015