ASIC REGULATORY GUIDE 46 DISCLOSURE

UNLISTED PROPERTY SCHEMES | IMPROVING DISCLOSURE FOR RETAIL INVESTORS

SECTION 1: DISCLOSURE PRINCIPLES

APN | Property Group

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ASIC REGULATORY GUIDE 46

The Australian Securities and Investments Commission (ASIC) issued a revised Regulatory Guide 46 (RG 46) in March 2012 which outlines eight enhanced disclosure principles and six benchmarks for unlisted property schemes. These benchmarks and disclosure principles are designed to extract key risk and return information for retail investments in unlisted property schemes.

In addition to the regular disclosures made by APN Funds Management Limited (APN FM), clear and prominent disclosure of this information will help retail investors compare the relative risk and return of investments in unlisted property schemes and decide whether these investments are suitable for them.

This document provides an overview of ASIC's eight enhanced disclosure principles and six benchmarks (refer Section 1). The responses of APN FM as Responsible Entity to each of the key risk features identified together with the practical application of the principles and benchmarks to each of the applicable funds is found in Section 2.

Funds investing in Australian property	
APN Property Plus Portfolio	ARSN 101 227 614
APN Coburg North Retail Fund	ARSN 601 833 363

Funds investing in European property	
APN Euro Property Fund	ARSN 123 172 930
APN Champion Retail Fund	ARSN 127 948 127

The Regulatory Guide 46 Disclosure information should be read in conjunction with the relevant fund's latest Product Disclosure Statement and the fund's most recent financial statements which are available on APN FM's website www.apngroup.com.au.

APN FM will update the Disclosure information when material changes occur. Please refer to the website www.apngroup.com.au for these updates. A printed copy of this document will be provided upon request and without charge.

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An overview of ASIC's eight enhanced disclosure principles and six benchmarks and where they are referenced in Section 1 of this document is as follows:

Principal	Description	Page
Gearing	**Disclosure principal 1** indicates the extent to which a fund's assets are funded by external borrowings. **Benchmark 1** addresses each fund's policy on gearing at an individual credit facility level.	4
Interest cover	**Disclosure principal 2** indicates a fund's ability to meet interest payments from earnings. **Benchmark 2** addresses each fund's policy on the level of interest cover at an individual credit facility level.	5
Interest capitalisation	**Benchmark 3** addresses whether the interest expense of a fund is capitalised.	6
Borrowing	**Disclosure principal 3** provides information on each fund's credit facilities and associated risks including the circumstances in which credit facility covenants will be breached.	7
Portfolio diversification	**Disclosure principal 4** provides information on a fund's investment practices and direct property investment portfolio risk.	8
Valuations	**Benchmark 4** addresses the way in which valuations are carried out by APN FM in relation to the fund's assets.	9
Related party transactions	**Disclosure principal 5** outlines APN FM's governance procedures that regulate transactions with related parties. **Benchmark 5** addresses APN FM's policy on related party transactions.	10
Distribution practices	**Disclosure principal 6** outlines a fund's distribution practices including where the distributions are sourced and sustainability of distributions. **Benchmark 6** addresses where distributions are sourced from and whether forecast distributions are sustainable.	11
Withdrawal arrangements	**Disclosure principal 7** outlines the withdrawal rights for unitholders for those funds that offer a withdrawal mechanism and the risk factors that may affect the unit price on withdrawal.	12
Net tangible assets	**Disclosure principal 8** addresses disclosure of the net tangible asset (NTA) backing per unit of the fund.	13

Please note a glossary of terms and definitions can be found on pages 15-16 of this document.

Gearing

Disclosure principle 1: Gearing ratio

The gearing ratio indicates the extent to which a fund's assets are financed by external borrowings. It is calculated using the following formula:

$$\frac{\text{Total fund interest bearing liabilities}}{\text{Total fund assets}}$$

The look-through gearing ratio indicates the extent to which a fund and each of its underlying investments have been financed by external borrowings. It is calculated using the following formula:

$$\frac{\text{Total interest bearing liabilities + proportionate share of interest bearing liabilities of the fund's underlying investments}}{\text{Total fund assets (excluding investments) + proportionate share of assets of the fund's underlying investments}}$$

Gearing levels provide an indication of the potential risks a fund faces in terms of its level of borrowings due to, for example, an increase in interest rates or a decrease in asset values. It is a useful indicator of risk that can be weighed up against a fund's rate of return.

Gearing is used to increase potential returns to investors. Direct property investment traditionally supports higher levels of gearing compared to other investment classes based on the matching of long term rental payments with interest costs.

The liabilities and assets used to calculate the gearing ratio will be based on the Fund's latest financial statements. The latest financial statements would usually be the latest audited or reviewed financial statements, except where APN FM is aware of material changes since those statements which will clearly be disclosed as such.

Benchmark 1: Gearing policy

Benchmark: The responsible entity maintains and complies with a written policy that governs the level of gearing at an individual credit facility level.

The Responsible Entity has a written Treasury Policy that sets out the parameters and targets for the management of gearing for each of its Funds.

In accordance with this policy, gearing targets are established on inception and periodically thereafter, aimed at ensuring that each Fund is compliant with the Loan Value Ratio covenant(s) required by its lender(s) at all times and, where possible, headroom is available to withstand a downward movement in valuations without triggering the right for the lender to accelerate its loan facilities due to a breach. However, there may be good commercial reasons or factors beyond the control of APN FM that may cause a Fund to fall outside the gearing target(s).

A copy of the Treasury Policy is available upon request.

Interest cover

Disclosure principle 2: Interest cover ratio

Interest cover measures the ability of a fund to meet its interest payments on borrowings from its earnings. The level of interest cover is a critical indication of a fund's financial health. It is a key measure of the risks associated with a fund's level of borrowings and the sustainability of borrowings. The lower the interest cover, the higher the risk that a fund will not be able to meet its interest payments. A fund with a low interest cover only needs a small reduction in earnings (or a small increase in interest rates or other expenses) to be unable to meet its interest payments out of current year earnings. Interest cover is also useful for investors when comparing a fund's relative risks and returns to investments in similar products.

A fund's ability to meet interest payments depends on a variety of factors. Changes to market interest rates may or may not impact the fund's interest cover, as interest rate hedging or other activities designed to manage risk can reduce the impact of market changes on the fund's profitability.

Interest cover is calculated using the following formula:

$$\frac{\text{EBITDA - unrealised gains + unrealised losses}}{\text{Interest expense}}$$

Benchmark 2: Interest cover policy

Benchmark: The responsible entity maintains and complies with a written policy that governs the level of interest cover at an individual credit facility level.

The Responsible Entity has a written Treasury Policy that sets out the parameters and targets for the management of interest cover for each of its Funds.

In accordance with this policy, interest cover targets are established on inception and periodically thereafter, aimed at ensuring that each Fund is compliant with the Interest Cover Ratio covenant(s) required by its lender(s) at all times and, where possible, headroom is available to withstand a reduction in income and/or increase in interest rates without triggering the right for the lender to accelerate its loan facilities due to a breach. However, there may be good commercial reasons or factors beyond the control of APN FM that may cause a Fund to fall outside the interest cover target(s).

A copy of the Treasury Policy is available upon request.

Interest capitalisation

Benchmark 3: Interest capitalisation

Benchmark: The interest expense of the fund is not capitalised.

Interest capitalisation occurs when accrued or accumulated interest is added to the loan principal instead of being paid on a regular basis. It generally occurs where a fund's assets are under construction as such assets generally do not derive rental income to meet interest payment obligations that are required under loan facilities until construction has been completed and the property is occupied by the tenant.

Borrowing

Disclosure principle 3: Fund borrowing

A fund has the potential to enhance returns to investors through the use of borrowings. However, this is not without risk. For example, increases in interest rates or falls in property income can reduce the income returns available for investors, while falls in property values can erode investor's initial capital investment. Other risks associated with borrowings are set out below.

Refinancing risk

Refinancing risk arises where long term assets (e.g. property) are financed by short term borrowings that will require regular refinancing. During periods where credit is restricted or difficult to obtain, refinancing may occur on less favourable terms or not at all. This can affect a fund's ability to continue and may result in a fund being required to sell assets on a forced sale basis potentially leading to capital losses.

APN FM endeavours to ensure that the facilities are obtained on terms that are aligned with the terms of the funds. Borrowing maturity profiles and undrawn credit facilities can provide important information to investors to highlight potential refinancing risk.

Generally, the debt facilities are secured by a first mortgage over a fund's investment properties. This means that debt providers typically rank ahead of all unsecured creditors and investors upon disposal of the property or winding up of a fund.

Interest rate risk

Interest rate risk arises when a fund has financed an asset with variable interest rate borrowings but receives income which does not change with movements in the interest rate.

Adverse interest rate movements may affect any portion of the fund's debt which is unhedged and this could affect the level of distributions to unitholders or the net asset value of the units.

Interest rate risk is managed through the use of interest rate swap contracts (that 'swap' variable interest rate liabilities for fixed interest rate liabilities) or fixed rate borrowing agreements.

Currency risk

Currency risk arises where a fund has obtained finance in a different currency to that in which the asset is valued and/or generates its revenue. All of the APN FM funds have mitigated currency risk by borrowing in the currency that applies to the assets they finance.

Breaches of loan covenants

Most borrowing facilities contain borrowing covenants that relate to:

- gearing levels; and/or
- interest cover.

A breach of a borrowing covenant may result in the lender requiring immediate repayment of the facility, payment of interest rate/margin penalties and/or a freeze on any further borrowings under the facility.

APN FM regularly monitors each fund's compliance with its banking covenants and maintains regular communication with the lenders. Where the prospect of a breach of a covenant arises, immediate action is instigated to mitigate a potential breach. Typically this would require debt repayment to a level that restores compliance with the covenant. Financing a debt reduction may require the sale of assets, the reduction of distributions or a combination of both.

Portfolio diversification

Disclosure principal 4: Portfolio diversification

APN FM as the Responsible Entity for each of the funds has an Investment Committee to manage and supervise the investment process and to approve investment and divestment decisions for each fund in accordance with each fund's relevant investment strategy. Any acquisition of additional properties must meet the investment objectives of each fund and must complement the fund's existing exposure. It is APN FM's aim to invest in such a way that any risks the funds are exposed to are minimised, while at the same time endeavouring to achieve the investment objectives of each of the funds. APN FM ensures that each fund's investments conform to the fund's investment strategy.

The quality of the properties held by each fund, including the quality of leases entered into over those properties is a key element in the financial position and performance of the funds. Generally, the more diversified the portfolio, the lower the risk that an adverse event affecting one property or lease will put the overall portfolio at risk.

Valuations

Benchmark 4: Valuation policy

Benchmark: The responsible entity maintains and complies with a written valuation policy that requires the following:

a. a valuer to:

   i. be registered or licensed in the relevant state, territory or overseas jurisdiction in which the property is located (where a registration or licensing regime exists), or otherwise be a member of an appropriate professional body in that jurisdiction; and
   ii. be independent;

b. procedures to be followed for dealing with any conflict of interest;

c. rotation and diversity of valuers;

d. valuations to be obtained in accordance with a set timetable; and

e. for each property, an independent valuation to be obtained:

   i. before the property is purchased, for a development property on an 'as is' and 'as if complete' basis, and for all other property, on an 'as is' basis; and
   ii. within two months after the directors form a view that there is a likelihood that there has been a material change in the value of the property.

The Responsible Entity has a written Valuation Policy governing the frequency and process for valuing real property assets that are owned directly by a fund.

Subject to an overriding obligation to ensure property assets are stated at fair value at each reporting period, this policy requires that an external, independent valuation expert value each property under the following circumstances:

- as a pre-condition of the purchase of that property. The valuation methodology to be used is dependent on the type of property being acquired:
  - For a development property – on an 'as is' and 'as if complete' basis; or
  - For all other property – on an 'as is' basis;
- upon completion of a Investment Property under construction;
- at least once every three years;
- within two months of the Board of APN FM forming the view that there is a likelihood that there has been a material change (±5%) in the value of the property; and
- when required by a lender in order to comply with any facility agreement term.

Valuers will be appointed having regard to their expertise and experience in locality, appropriate qualifications, cost and any actual or potential conflicts of interest. Where required, approval by the secured lender(s) must also be obtained. In particular, the following guidelines will be applied when appointing a valuer:

- The valuer will be registered, licensed or a member of the appropriate professional body applicable to the relevant state, territory or jurisdiction in which the property is located (as appropriate);
- The valuer will be independent from parties that may have a financial interest in or associated with the Property (i.e. APN and its associates) and will be free from conflicts of interests (circumstances which may create a risk that professional judgment or actions regarding a primary interest (i.e. determining the fair value of a property) will be unduly influenced by a secondary interest (other motives, whether financial or non-financial in nature)). Where an actual or perceived conflict of interest is identified the appointment of the valuer will be terminated; and
- The same valuer will not be appointed for more than two consecutive Independent Valuations for a Property (excluding its acquisition valuation).

A copy of the Valuation Policy is available upon request.

Related party transactions

Disclosure principle 5: Related party transactions

Related party transactions can carry a risk that they could be assessed and monitored less rigorously than arm's length third party transactions. It is important for investors to be able to assess whether responsible entities take an appropriate approach to related party transactions. A significant number and value of such transactions may mean that investors should consider the financial position of the related group as a whole and the risk of potential conflicts of interest.

Benchmark 5: Related party transactions

Benchmark: The responsible entity maintains and complies with a written policy on related party transactions, including the assessment and approval processes for such transactions and arrangements to manage conflict of interest.

The Responsible Entity's written Related Party Transactions and Conflict of Interests Policy governs the assessment and approval process for such transactions and the arrangements in place to manage conflicts of interest.

The purpose of this policy is:

- to provide the Responsible Entity and its staff with an overview of the regulation of conflicts of interest and related party transactions so that APN FM and its staff can identify transactions that would be subject to this policy;
- to specify the principles to be adopted in relation to circumstances giving rise to conflicts of interest and the conduct of a related party transaction;
- to establish the practices and procedures relating to circumstances giving rise to conflicts of interest and the conduct of related party transactions; and
- to specify the basis of proper disclosure of such matters giving rise to conflicts of interest and related party transactions.

Ultimately, this policy:

- prescribes the circumstances in which a member of the Responsible Entity may enter into a related party transaction; and
- where a member proposes to enter into a transaction which may not be a related party transaction, but nevertheless gives rise to a potential conflict of interest, to prescribe the manner in which the Responsible Entity may deal with the potential conflict.

Management of compliance with related party transactions

The Responsible Entity has appropriate control systems in its related party transaction policy management system including:

- monitoring and assessment of transactions by staff regarding related party transactions;
- ensuring (where necessary) through an independent third party that any relevant related party transaction is on reasonable "arms length" terms;
- monitoring and review of transactions by the Compliance Officer for compliance with this policy; and
- reporting on transactions to the Audit, Compliance & Risk Management Committee of the relevant fund for compliance with this policy.

A copy of this policy is available upon request.

Distribution practices

Disclosure principle 6: Distribution practices

APN FM determines the distribution to be paid by each fund based upon a number of factors, including, where applicable:

- The constitution of the fund;
- Accounting net income, including unrealised earnings;
- Retained earnings;
- Capital expenditure requirements;
- Debt management requirements;
- Future earnings expectations; and
- Smoothing of distributions.

In some instances, this may require that the distribution be supplemented by distributions out of capital. This is permitted under the constitution of each in the following circumstances:

- cash generated from operations exceeds the fund's net accounting income;
- taxable income exceeds the fund's net accounting income for the year;
- management determine it appropriate to distribute a portion of the fund's unrealised gains; or
- management determine to normalise distribution income for short term fluctuations in the fund's net accounting income.

The amount of distributions made from capital is assessed on a periodic basis, in the context of current and forecast fund performance. Due care is exercised when considering whether the distribution component comprising capital (if any) can be considered a sustainable practice over the ensuing 12 months. Where a distribution is made from capital, this is adopted to manage a short term position, not on a sustained basis.

Given the current economic climate, APN FM has considered it prudent to suspend distributions from some funds and apply the retained cash to reduce fund debt and to help mitigate further compression of debt and/or hedging covenants. This action has been necessary to strengthen the funds' balance sheets and improve flexibility in dealing with any potential issues in the future. The ability of the funds to pay future distributions has not yet been assessed and will be dependent on compliance with financial covenants, discussions with financiers and the requirement to strengthen the funds' balance sheet to provide future flexibility to respond to economic events.

This approach will be regularly reviewed and all potential financing options assessed to further strengthen balance sheets in order to reinstate distribution payments to investors.

Benchmark 6: Distribution practices

Benchmark: The fund will only pay distributions from its cash from operations (excluding borrowings) available for distribution.

The Responsible Entity has an objective of paying distributions from the cash from operations of a Fund. However, as identified above, there are certain circumstances where distributions paid may be supplemented by capital payments funded from drawdown of additional borrowings. APN FM carefully evaluates the sustainability of distributions where payments of capital occur when finalising the distribution to be paid.

Withdrawal arrangements

Disclosure principle 7: Withdrawal arrangements

The following funds do not offer withdrawal arrangements to investors:

- APN Coburg North Retail Fund
- APN Champion Retail Fund

These funds are fixed term funds for which there is no current redemption or withdrawal facility available to unitholders. Due to the nature of the funds and their underlying assets, the funds are considered "illiquid" based on the definition in the Corporations Act. Accordingly, APN FM does not propose to offer a redemption facility to investors, although it has the power to make withdrawal offers under the funds' constitutions and the Corporations Act. The above funds should be considered as medium to long term investments, with the ability to withdraw only upon the termination of the fund.

The following funds offer or have previously offered withdrawal arrangements to investors:

- APN Property Plus Portfolio
- APN Euro Property Fund

Temporary suspension of withdrawals

The withdrawal arrangements for the following funds have been temporarily suspended:

- APN Euro Property Fund

The unprecedented wave of economic events over recent times has led to major declines in the value of the listed Australian and international Real Estate Investment Trust (REIT) markets. This, combined with the surge in withdrawals in the wake of the introduction of the federal government's bank deposit guarantee, has resulted in the proportion of illiquid assets in the fund reaching unacceptable levels for the optimum operation of the fund. In response to these circumstances, APN FM suspended all withdrawals to protect the interests of unitholders as a whole until such time that APN FM deems the market has stabilised and liquidity can be provided without unfairly treating those investors who wish to remain invested.

Risk factors and limitations that may affect the ability of investors to withdraw from the fund include the allocation of liquid and illiquid assets within the fund. This in turn is affected by the state of the Australian and international REIT market, valuations of assets in the direct property market and the funds' ability to dispose of assets.

APN FM continues to monitor the market environment and will notify unitholders of any updates on the matter.

Net tangible assets

Disclosure principle 8: Net tangible assets

The net tangible asset (NTA) backing of a fund gives investors information about the value of the tangible assets of the fund. The NTA calculation helps investors understand the value of the assets upon which the value of their unit is determined.

The NTA is calculated using the following formula:

$$\frac{\text{Net assets} - \text{intangible assets} +/- \text{any other adjustments}}{\text{Number of units on issue in the fund}}$$

Examples of intangible assets or other adjustments are prepaid borrowing costs which are typically paid upfront and recorded as an asset and then amortised to the Income Statement over the total term of the facility.

APN FM bases the NTA calculation on the fund's latest financial statements. The latest financial statements are usually the latest audited or reviewed financial statements, except where APN FM is aware of material changes since those statements were issued. In such circumstances the date of the information used to calculate the NTA and the events that lead to the material change would be disclosed.

The movement in the NTA provides investors information on the performance of the fund and therefore the performance of their investment. It is a measure that can be used to analyse how the value of the fund's assets are performing over time and provides an indication of what value will be returned to them at the end of the life of the fund.

SECTION 2: DISCLOSURE PRINCIPLES AS THEY APPLY TO THE FUNDS

Click on the individual fund below to be directed to the disclosure principles and benchmarks as they apply to the funds.

Funds investing in Australian property	
APN Property Plus Portfolio	ARSN 101 227 614
APN Coburg North Retail Fund	ARSN 601 833 363

Funds investing in European property	
APN Euro Property Fund	ARSN 123 172 930
APN Champion Retail Fund	ARSN 127 948 127

GLOSSARY

AREITs	Australian real estate investment trusts (previously known as LPTs, Listed Property Trusts). They describe a managed portfolio of real estate that is listed on the ASX. They are a highly liquid form of property.
Arm's length transaction	A transaction between two parties who act independently as if they were unrelated, so that there is no question of a conflict of interest.
ASIC	Australian Securities Investment Commission. ASIC is the regulatory body that enforces company and financial services laws to protect consumers, investors and creditors.
Borrowing maturity	Refers to the period when borrowings must be repaid.
Business Day	Has the meaning set out in the constitution for each fund.
Capitalisation rate (Cap rate)	A market derived rate or yield applied to a property's net income to determine its value at a specific date.
Credit facility	Refers to the maximum value available to be borrowed under a loan facility.
Distributions	Payment of part of a fund's assets (usually from profits, but may include part of the capital of the fund) to investors which is expressed as a number of cents per unit, often referred to as DPU (distribution per unit).
Diversification	A key aspect for managing investment risk is diversification or more commonly referred to as "not putting all your eggs in one basket". Diversification can be achieved through: ▪ Exposure to a wide ranging portfolio of property ▪ Geographic spread of investments located both within Australia and overseas ▪ Sector diversification including retail, office and industrial ▪ Tenant diversification - within each asset there are frequently multiple tenants who will have different businesses, different rent levels, varying lease covenants and rent review timings.
EBITDA	Earnings before interest, tax, depreciation and amortisation. EBITDA is widely regarded as a useful metric to evaluate profitability.
Fixed term funds	Often referred to as 'syndicates', fixed term funds have a definitive start and end date. Investors are generally unable to redeem their investment until the fund end date.
Gearing	A fundamental analysis of a fund's level of debt compared to its total asset investments. Gearing is expressed in percentage form. Funds with high gearing levels are generally considered to be more risky. Gearing is also referred to as "financial leverage".
Hedging	Hedging is a method of reducing the risk of adverse price movements. Hedging strategies can be applied to currency and interest expense.
Illiquid	An investment which cannot easily be sold or converted into cash. Examples include: fixed term funds, real estate, collectibles and private company interests.

GLOSSARY

Loan covenants	A loan covenant is a condition in a commercial loan that requires the borrower to fulfil certain conditions or which forbids the borrower from undertaking certain actions. Typically, breaching a covenant may result in a default on the loan conditions which can result in penalties being applied or a demand for immediate repayment of the loan. Covenants may also be waived, either temporarily or permanently, usually at the sole discretion of the lender.
Look-through	Where a fund invests in other external funds (listed and/or unlisted), the underlying investments of these external funds are shown on a look-through basis for the purposes of asset allocation by sector or geographic location. The look-through amounts are calculated as a proportion of the fund's total investments. A "look-through" approach can also be used for lending calculations such as gearing ratios, in circumstances where the underlying funds in which the head fund invests also have direct borrowings. In this case, the borrowings are weighted on a proportional basis to the amount that each fund represents of the head fund's total investments.
Look-through interest bearing liabilities	The proportionate share of interest bearing liabilities of non-consolidated investments held by the fund.
Look-through total assets	The proportionate share of the total assets of non-consolidated investments held by the fund, less the asset value recorded by the fund of this investment.
Net lettable area	The floor area of a building for which rent can be charged.
Off-balance sheet financing	This is a method of financing which is not reflected on a fund's balance sheet. Examples include: sale-and-leaseback, operating leases, joint ventures and research and development partnerships.
WALE (Weighted Average Lease Expiry)	Weighted average lease expiry is the average lease term remaining to expiry across the portfolio weighted by gross rental income or by net lettable area. Longer WALES are generally more highly regarded as they provide greater security for longer term income streams.

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