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CORPORATE ADVISORY

Ayers Rock Resort Review- Final Report

Indigenous Land Corporation (ILC)

18 December 2013

This Report has been prepared by McGrathNicol Advisory in accordance with the terms of the engagement letter dated 17 September 2013.

In accordance with our engagement letter, this Report has been prepared for the Indigenous Land Corporation ("ILC") only. This report should not be modified, including by removing this disclaimer, without our consent in writing.

The information contained in the report has been prepared on the basis of:

+ information provided to McGrathNicol by ILC;
+ discussions held with ILC management;
+ discussions held with the ILC Oversight Committee;
+ discussions with current and previous ILC Directors;
+ discussions held with other ILC consultants and stakeholders; and
+ publicly available information regarding the ILC and its past and current Board of Directors.

We have not carried out an audit, nor have we verified any of the information given to us by ILC. We have relied upon assurances from management as to the accuracy of the information provided. As the achievement of any prediction as to the results of subsequent trading is dependent upon future events, the outcome of which cannot be assured, the actual results achieved may vary materially from the projections included in this report. In all circumstances, whilst we believe that the statements made by us in this report are accurate, no warranty of accuracy or reliability is given.

In accordance with our policy, we advise that neither McGrathNicol Advisory nor any member or employee or related or associated entity of the firm undertakes responsibility in any way whatsoever, including by way of any errors or omissions arising through negligence or otherwise however caused to any persons other than ILC.

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Defined Term	Definition
Accor	Accor Asia Pacific Ltd
ANAO	Australian National Audit Office
ANZ	Australia and New Zealand Banking Group Ltd
ARMC	ILC Board's Audit and Risk Management Committee
ARR	Ayers Rock Resort
ATSI Act	Aboriginal and Torres Strait Islander Act 2005
CAC Act	Commonwealth Authorities and Companies Act 1997
Capex	Capital Expenditure
CBA	Commonwealth Bank of Australia
CBRE	CB Richard Ellis Hotels
CBRE Valuation	Full speaking valuation of the ARR prepared by CBRE for NAB dated May 2009
Colliers International	Colliers International Consultancy & Valuation Pty Limited
Corrs	Corrs Chambers Westgarth
CPGs	The then Commonwealth Procurement Guidelines
CPI	Consumer Price Index
DCF	Discounted Cash Flow
Director Baffsky	Former ILC Director David Baffsky
Director Driscoll	Former ILC Director Kevin Driscoll
Director Goolagong-Cawley	Former ILC Director Evonne Goolagong-Cawley
Director Gorringe	Former ILC Director Max Gorringe
Director Jeffries	Former ILC Director Sam Jeffries
Director McPherson	Former ILC Chairperson Ms Shirley McPherson
Director Trust	ILC Director Ian Trust
DoFD	Department of Finance and Deregulation
EBITDA	Earnings Before Interest, Tax, Depreciation, Amortisation
FaHCSIA	Department of Families, Housing, Community Services and Indigenous Affairs
FF&E	Furniture, Fittings and Equipment

Defined Term	Definition
GFC	Global Financial Crisis
GPT	GPT Ltd
GS	Grant Samuel
GS financial model	Financial model prepared by GS to provide the ILC with analysis of the ARR's projected cash flows and the NPV of those cash flows
Horwath	Horwath HTL
ILC	Indigenous Land Corporation
ILC COO	ILC Chief Operating Officer
Kd	Cost of Debt: the interest rate payable on debt finance
Ke	Cost of Equity: the rate of return expected on invested equity
Minister for FaHCSIA	The Minister for FaHCSIA at the time of the transaction, Jenny Macklin, MP
Minister for DoFD	The Minister for DoFD at the time of the transaction, Senator Penny Wong
NAB	National Australia Bank Ltd
NILS	National Indigenous Land Strategy
NPV	Net Present Value
PPM	Planned Property Management
Rf	Risk-free Interest Rate
Rm	Market Risk Premium: expected market rate of return in addition to the Risk-free interest rate.
SLA Proposal	Strategic Land Acquisition Proposal dated 1 October 2010
SPA	Sale Purchase Agreement
SWOT	Strengths, Weaknesses, Opportunities and Threat Analysis
The Land Account	The Aboriginal and Torres Strait Islander Land Account
Voyages	Voyages Indigenous Tourism Australia Pty Limited
WACC	Weighted Average Cost of Capital
Westpac	Westpac Banking Corporation
WU	Wana Ungkunytja
β	Beta: the rate of correlation to the Rm (Market Risk Premium)

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Area	Key findings
Engagement	The ILC engaged McGrathNicol to conduct a review of the financial performance and acquisition of the Ayers Rock Resort ("ARR"). Component 1 of the review is a forward looking assessment of the long term strategies for the ILC as owner of the ARR. Component 2 of the review focuses on the acquisition of the ARR and the establishment of the ILC's wholly owned subsidiary, Voyages Indigenous Tourism Australia Pty Limited ("Voyages"). This report addresses Component 2 only and considers matters pertaining to the adequacy of the due diligence undertaken directly or on behalf of the then ILC Board in relation to the acquisition of the ARR and the establishment of Voyages. Our detailed scope for Component 2 is set out at Appendix 1.
Introduction	The ARR is located adjacent to the Uluru-Kata Tjuta National Park in the Northern Territory. In July 2008, GPT Ltd ("GPT") offered for sale a package of Central Australian assets including the ARR. Following an approach from Wana Ungkunytja ("WU"), an Aboriginal corporation representing communities around Uluru, and holders of a first right of refusal in respect of the purchase of the ARR, the ILC commenced due diligence into the potential acquisition of the ARR. Following negotiations spanning from December 2008 to October 2010, the ILC entered into an agreement with GPT to acquire the ARR on 15 October 2010. The acquisition completed on 23 May 2011. The structure of the transaction under the Sale and Purchase Agreement ("SPA"), including the net purchase price of $292 million, is set out in the table below:

SPA purchase price structure

Instalments	$'000 Value
Deposit	13,500
Completion Date Payment	67,500
12 month Installment	81,000
60 month Installment	138,000
Total Purchase Price	**300,000**
Minumum Uplift Payment to GPT	17,000
Total ILC transaction outlays	**317,000**
Total GPT Capital contribution (over 5 years)	(25,000)
Net Purchase Price	**292,000**

Source: Sale Purchase Agreement

Area	Key findings
Value for money	**McGrathNicol examined whether the purchase price represented value for money for the ILC. This included consideration of:**

- The advice and valuations provided by consultants, including considering the following questions in accordance with the engagement scope:
  - Was the advice and valuations provided by consultants realistic?
  - Were the projections regarding profitability and return on investment appropriate and realistic?
  - Were the projections of capital expenditure and maintenance requirements realistic and appropriate?
- Whether negotiations of the purchase price were conducted in the best interests of the ILC.

The ILC Board minutes and Board papers generally reflect an intention that, regardless of how beneficial the potential Indigenous employment outcomes could be, the ARR acquisition had to be economically viable and stand up from a financial perspective. Accordingly we have assessed value for money from a purely financial perspective

Valuations received by the ILC

In this report we have considered three valuations used by the ILC throughout their due diligence:

Valuations received by the ILC

Features	Colliers	CBRE	Grant Samuel
Date	1 December 2008	26 May 2009	1 October 2010
Presentation	Formal valuation report	Formal valuation report	Presentation to ILC Board meeting
Adopted Value	$290 million	$270 million	$292 million
Methodologies	$274 to $295 million: + Passing Year's Income Capitalised + Third Year's Income Capitalised + 10 Year Discounted Cash Flow	$269.5 to $273.8 million: + Stabilized Income Capitalised + Five Year Discounted Cash Flow + 10 Year Discounted Cash Flow	$292 million: + Calculation of Net Present Value of 10 year forecast ARR Cashflows

We note the following:

- Technical analysis of the models did not identify any material technical weaknesses.
- From early 2009 to October 2010, the ILC appeared to place significant reliance on both the CB Richard Ellis Hotels ("CBRE") valuation and the Grant Samuel ("GS") financial model in assessing the $292 million net purchase price. The Colliers International Consultancy & Valuation Pty Limited ("Colliers International") model did not appear to be critical to the ILC Board's decision making in 2010 to purchase the ARR.
- A key risk treatment strategy for the ILC (addressing the risk of paying a purchase price greater than valuation) was to obtain a full speaking valuation. The CBRE valuation was used in this regard.
- However, due to the timespan between the date of the CBRE valuation (May 2009) and the date the ARR was acquired (October 2010), it is not unreasonable to assume that CBRE could have reached a different conclusion on value if it had updated its report at the time of purchase.

Area	Key findings
Value for money (continued)	***Restatement of valuations***

In considering the CBRE valuation:

- Given the time that passed between the date of the valuation and the purchase date, the ILC had the ability to reconsider the CBRE valuation based on more than 12 months of additional trading results. Importantly, this was in the context of warnings from the ILC's financial due diligence consultant which cautioned that actual trading results had been significantly under forecast, likely leading to an impact on valuation.
- It does not appear that any analysis was undertaken to update the operating forecasts underlying the CBRE valuation between May 2009 and October 2010 notwithstanding Horwath HTL's ("Horwath") findings that there was likely to be a "*substantial shortfall against forecast 2010*". Updating the CBRE valuation operating forecasts in line with the first half 2010 actual results and rebasing future years growth off these results indicates a revised value in the order of $250 million (from the initial value of $270 million).

In considering the GS valuation model:

- The model rightly identified that occupancy was the key driver for the ARR's revenues. However, the model indicated a strong improvement in occupancy in years after the transaction, stabilising at a level of 67%. The historical trend on occupancy at ARR had seen a reduction to a trend level approximating 63% for the four years prior to the Global Financial Crisis ("GFC"). Adjusting the occupancy levels in the GS model to reflect a 63% occupancy level would suggest a net present value of $250 million (from the initial value of $292 million).
- Capital expenditure projections underlying the GS model exceeded the projections prepared by the independent due diligence consultant and were conservative in comparison to the capex projections included in the Colliers and CBRE valuations. However, the projections prepared by the independent consultant had initially been estimated at higher amounts and were revised to lower amounts under instructions to reflect essential expenditure only and not upgrading the quality of hotel rooms. It is arguable that the assumed occupancy growth would have required a level of investment beyond that which was "*essential*" only. Adjustments to the GS model for capital expenditure (to a level that was consistent to the original capital expenditure projections by the independent consultant) resulted in a valuation range of $273 million to $278 million (from the initial value of $292 million).
- It does not appear that GS presented the ILC Board with any sensitivity analysis with respect to their Net Present Value ("NPV") calculation prior to entering into the transaction. In November 2010, GS did provide the ILC with two sensitivity scenarios. However, this did not extend to highlighting the impact on the calculation of the NPV. The NPV calculation would have been reduced to between $237 million and $274 million based on the sensitivity scenarios.

The impact of the above is summarised as follows:

Restatement of valuations

Valuation	Description	Original Value	Adjusted Value
CBRE	Adjustment of EBITDA to reflect adjusted 2010 budget based on first half 2010 actuals.	$270 million	$250 million
GS Model	Adjusting operating projections for stabilised occupancy beyond year 5 at 63%.	$292 million	$250 million
	Assuming higher levels of capital expenditure to support optimistic operating projections.	$292 million	$273 - $278 million
	Determining the impact on the GS valuation model based on GS sensitivity analysis scenarios.	$292 million	$237 - $274 million
Net Price	The net price paid for the ARR under the SPA.	**$292 million**	

Source: CBRE Valuation and GS financial model, McGrathNicol analysis.

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Area	Key findings
Value for money (continued)	***Negotiations*** + GS provided advice to the ILC in respect of the negotiation of the transaction price. Negotiations with GPT for the purchase of the ARR extended from late 2008 to September 2010. Whilst it appears that the ILC may have been the only interested purchaser of the ARR, and that GPT was a motivated seller, GPT was not prepared to sell at any price, anecdotally seeking a headline sale price of $300 million. Despite some Board opposition, the ILC appears to have been a motivated purchaser. Documentation indicates that the ILC considered valuation advice and attempted to negotiate the transaction price with GPT. + The ILC agreed to provide WU with 7% equity in the ARR upon the earlier of the repayment of all loans and ILC monies (including the $100,000 legal costs reimbursed to WU, and the $200,000 paid to WU on settlement of the ARR in consideration of WU's first right of refusal) or ten years, in return for WU not exercising its first right of refusal with GPT to purchase the ARR assets. WU had no capacity to purchase the ARR on its own and there appeared to be no other parties interested in purchasing the ARR. Accordingly, the first right of refusal was of little or no value. The equity provided to WU is significant, and appears to have been granted in order to obtain the support of an organisation with links to the local Indigenous community. This relationship is difficult to value and there is limited documented evidence of the negotiations. ***Overall conclusions on value for money*** + The scope of our review does not include any consideration of non-financial factors that may impact on value for money and which may have been considered by the ILC (e.g. Indigenous employment). + In forming our conclusion we have sought to consider what the ILC and its advisors would have known at the time, rather than the use of hindsight. + Based on our review of the advice and valuations provided to the ILC by consultants, including projections regarding profitability, return on investment and capital expenditure, and the negotiations related to the transaction, McGrathNicol concluded that: • documentation supports that the ILC considered valuation advice provided by consultants and attempted to negotiate the transaction price with GPT; • the transaction price was consistent with the NPV suggested by the GS financial model; however • the transaction price was higher than the value suggested by CBRE; • the CBRE valuation was not updated to reflect changes to trading performance, which may have resulted in reduced valuation conclusions; and • It is arguable that some of the assumptions used in the GS financial model were ambitious. + Ultimately, the assessment of value is subjective and it is possible that the ILC Board considered these matters and had good reason to assess that the price was appropriate; but we believe it would have been appropriate to document the assessment of downside risk.

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Area	Key findings
Establishment of Voyages	**McGrathNicol examined whether the establishment of Voyages, including Directors' appointments and setting of remuneration, was in accordance with normal practice:** + In establishing the Voyages entity for the purposes of the ARR transaction, it appears that the ILC has acted in accordance with the Aboriginal and Torres Strait Islander Act 2005 ("ATSI Act"). + The Board Briefing Paper of April 2011 states that "*the ILC is fortunate to have Directors of the calibre and experience of those recommended for appointment*". McGrathNicol does not disagree with this assertion. While the appointed directors may have been well known to the ILC, and their competency was not in question, the ILC failed to follow internal policies in documenting a transparent process. + McGrathNicol considers it inappropriate that the original Voyages Constitution did not require that the Voyages Board be controlled by a majority of directors common to the ILC. This gave rise to an inability to control the subsidiary and ensure compliance with the Commonwealth Authorities and Companies Act 1997 ("CAC Act"). We are advised that the Voyages Constitution has since been rectified to address a number of these issues. + The Directors' fee pool of circa \$1.5 million for three years was approved based on advice received from Deloitte, referenced to market conditions. We regard this approach to determining remuneration to be reasonable.
Board decision making	**McGrathNicol examined whether a transparent audit trail was established to record ILC Board decisions, and whether the advice provided by consultants was followed by the Board:** + The ILC Board were provided with board papers in advance of the key meeting of 1 October 2010, including the "Strategic Land Acquisition Proposal"("SLA Proposal"). This document set out the costs and benefits of the transaction, and how risks would be managed. This document was accompanied by due diligence reports and advice from consultants, with key consultants present at the 1 October 2010 Board meeting. + The Board minutes provide a summary of the due diligence work undertaken, although they do not clearly set out the findings of this work, and relevance to the decision to pursue the acquisition. Accordingly, McGrathNicol is unable to confirm the extent to which consultants' advice was deliberated on by the Board. + The ILC Board ultimately resolved the transaction was in the ILC's best interests. However, the reasoning for this conclusion was not adequately documented. + The Board minutes only record clear support for the acquisition by three of the seven directors, with two directors abstaining from voting. While we understand that it was not the practice of the ILC Board to record the vote of each member, given the magnitude of the acquisition, it would have been appropriate to fully record the Board deliberations and include Board member views.
Conflicts of interest	**McGrathNicol examined whether appropriate recording of conflicts of interest were made as part of the acquisition process:** + The ILC did not maintain a conflict of interest register for the ARR transaction, instead relying on employees and directors to declare conflicts as they arose. This is considered a shortcoming in the ILC's governance framework. + From searches of publicly available information, we have noted an indirect (but undeclared) link between the ARR vendor and an ILC Director but due to its remoteness it appears unlikely it represents a conflict of interest. + Voyages appointed Accor as the ARR's hotel service provider. ILC Director David Baffsky ("Director Baffsky") was Hotel: Australia's Accor ("Accor") Honorary Chairman. This potential conflict of interest was managed appropriately by the ILC through the exclusion of Director Baffsky from the selection process. + GS's advisory fee was based on a percentage of the purchase price of the ARR. Whilst commonplace in the financial services sector, a fee arrangement of this nature does not incentivise an advisor to seek the lowest possible transaction price or advise against the transaction. We make no finding that GS acted improperly in this respect. However, we consider that it may have been prudent for ILC to consider alternative fee structures.

Area	Key findings
ANZ cash advance facility and the GPT vendor finance facility	**McGrathNicol examined whether the loan arrangements negotiated with the Australia and New Zealand Banking Group Ltd "(ANZ") and GPT were appropriate and undertaken at arm's length:** + The ILC obtained a five year $60 million cash advance facility from ANZ to fund capital expenditure for the ARR, and to assist with making part payment of the purchase price. + The loan arrangements with the ANZ resulted from a competitive process in which other banks were invited to participate. The terms and conditions of the facility are consistent with those that would reasonably be expected by a bank providing a secured credit facility. The interest rate margin of 0.80% p.a. above the Bank Bill Rate is considered to be competitive when compared to the prevailing market conditions at the time of the transaction, and with offers made to the ILC by other banks. + It appears that the GPT vendor financing structure was entered into by the ILC due to difficulties in sourcing bank financing to fund the ARR purchase. The GPT facility applies a coupon rate of a 6.5% p.a. However, there is an effective interest rate of 8.5% p.a. due to a guaranteed valuation uplift payment of at least $17 million due to GPT after five years. + We do not consider that the effective interest rate of 8.5% was excessive given GPT's subordinated security position (behind the ANZ), and the prevailing market interest rates at the time of the transaction. We have identified no evidence to suggest that the ILC accepted an arrangement that was uncompetitive or disadvantageous.
Borrowing limits	**McGrathNicol examined whether the borrowings to facilitate the ARR purchase fell within the monetary limits prescribed by the ATSI Act:** + The ATSI Act sets out that the ILC is subject to a borrowing and guarantee limit. Given the substantial borrowings required to complete the ARR purchase, the ILC sought legal advice in April 2011 on whether its borrowings (including those required to purchase the ARR) were within the limits prescribed by the ATSI Act. In addition, in May 2011, the ILC engaged the Australian National Audit Office ("ANAO") to undertake a review of the borrowing limits. + The advice from the ILC's lawyers and the ANAO indicate that the ILC's total borrowings did not exceed the limits set out in the ATSI Act. + The advice to the ILC was provided in April 2011 and May 2011, more than five months after the ARR purchase agreement and ANZ loan facility were entered into. It would have been prudent to seek this advice prior to entering into the contract to purchase the ARR.
Risk management	**McGrathNicol examined whether the risk strategies adopted to mitigate the risks identified at the time of the ARR purchase were appropriate:** + With the assistance of its consultants, the ILC prepared a comprehensive risk management plan specific to the ARR acquisition. Key transactional and operational risks were identified and assessed in accordance with an appropriate risk management framework. Furthermore, for risks identified as Extreme, High or Moderate, risk treatment strategies were documented. + Prior to the 1 October 2010 Board meeting, the ILC Board was provided with an extract of the risk assessment. This document included risk treatment strategies to mitigate risks identified as Extreme and High risk. This risk assessment extract was deficient in that a number of the Extreme or High acquisition risks presented for Board consideration did not appear to have been adequately considered. For example, the risk treatment strategy to mitigate the risk that the purchase price was too high was identified as the CBRE valuation. As noted above, this valuation was 17 months old at the time of the transaction. + The Board minutes and papers do not evidence discussion of the risk assessment. Accordingly, documentation does not support that the risks set out in the SLA Proposal Risk Assessment were considered and accepted by the Board as part of its decision to acquire the ARR.

Area	Key findings
Engagement of advisors and consultants	**McGrathNicol examined whether the consultancies commissioned by the ILC Board were consistent with the ILC's purchasing guidelines and generally accepted governance procedures:** + At the time of the transaction, the ILC's procurement policies aligned with the key principles of the (then) Commonwealth Procurement Guidelines ("CPGs") and were consistent with generally accepted governance practices for an agency such as the ILC. + Documentation does not support that the procurement of the ILC's key advisor (GS) was undertaken in accordance with the ILC's policies. GS did not appear to have been engaged through a competitive tender process or a process where multiple quotations were sought. We further note that the contract between the ILC and GS (i.e. counter-signed engagement letter initiated by GS) did not meet the ILC's policy requirements (albeit it is consistent with our understanding of market practice for engagement of this nature in the private sector). + In respect of the engagement of other key consultants, documentation does not generally support that competitive tender or quotation processes were used by the ILC (or GS on the ILC's behalf) in making procurement decisions. Accordingly, the documentation does not indicate that the ILC's procurement activities were conducted in accordance with its policies.
Engagement with the Australian Government	**McGrathNicol examined whether the ILC's engagement with key Australian Government stakeholders in respect of the acquisition of the ARR was appropriate:** + The ATSI Act and the CAC Act set out the legislative requirements that the ILC was required to adhere to in its decision to acquire the ARR. + From our review of relevant legislation and correspondence between the ILC and the Australian Government, it appears that the ILC met its requirements under the ATSI Act to keep the Minister for Families, Housing, Community Services and Indigenous Affairs ("FaHCSIA") informed of the transaction. The CAC Act did not require Ministerial approval to enter into the transaction. + Notwithstanding this, a number of issues regarding the transaction and perceived financial and operational risks were raised by Australian Government representatives in the lead up to the ILC entering into the transaction. Documentation indicates that the Department of FaHCSIA, the Department of Finance and Deregulation ("DoFD") and their respective Ministers raised concerns regarding the purchase of the ARR in strongly worded letters to the ILC. + At the time of entering into the transaction to purchase the ARR, some of the concerns raised by the Minister for DoFD had not been responded to on 8 October 2010. The Minister requested further sensitivity analysis be undertaken in the event the transaction proceeded. The ILC Board proceeded with the transaction in the absence of this further analysis, providing a response including some analysis on 5 November 2010 (within 28 days as requested by the Minister, but after entering into the transaction).
Capital expenditure forecasts	**McGrathNicol examined whether projections of the capital refurbishment and maintenance requirements over the immediate, medium and longer term were realistic and appropriate:** + Planned Property Management ("PPM") were engaged to prepare capex projections in late 2008, and provided revised projections based on instructions to focus on essential capex rather than improve standards of accommodation to higher levels. The GS valuation model capex projections in the short to medium term exceed the projections prepared by the physical due diligence consultant. + It appears that the PPM capex projections reflected essential capex only, which arguably may not have been at levels that would support the forecast growth in operating projections outlined in the GS Model. Accordingly, it may be considered that a higher amount of capex would be needed in the short to medium term (first 5 years post-acquisition) in order to assist in achieving the operating projections underlying the GS financial model. + Capex projections over the long term were included in the GS financial model based on 5.5% of revenue projections in years six to 10. In comparison to the capex projections in the Colliers and CBRE valuations, the long term capex projections included in the GS financial model appear conservative.

Area	Key findings
Appropriateness of the transaction	**McGrathNicol examined whether it was appropriate for the ILC to enter into the purchase of the ARR. This included consideration of whether the ILC obtained sufficient advice to confirm that it was legally able to enter into the transaction and whether it was reasonable for the ILC to consider that the acquisition would not have an impact on the ILC's existing operations:** ***Legal capacity of the ILC to enter into the transaction*** + External legal advice obtained by the ILC supports that the acquisition and management of the ARR (with a long term view to transfer ownership) is permitted in accordance with the ATSI Act and the CAC Act. + However, the expectation of the ILC at the time of the acquisition appears to be that the ARR operating business (i.e. the going concern) would be leased back after the transfer of the land, potentially for a 99 year term. This would result in the ILC becoming the long term operators of the ARR. The legal advice obtained by the ILC does not appear to consider whether a long term lease back arrangement is consistent with the ILC's functions and objectives. ***Impact of the ARR transaction on the ILC's existing operations*** + The ARR's net $292 million purchase price was funded by a mixture of debt funding and the ILC's cash reserves. Prior to the transaction being entered into, the Ministers for FaHCSIA and DoFD expressed concerns that the acquisition would have an impact on the ILC's existing operations and future investment opportunities. + The ILC strongly countered these concerns in letters to the Ministers and their respective Departments. In the Strategic Land Acquisition Proposal ("SLA Proposal") presented to the Board on 1 October 2010, it is stated that "*the ILC has been careful to ensure that all due diligence, planning and financial forecasts for the acquisition and operation of ARR provided for the ILC maintaining its current and future planed operations*". + Given the significant scale of the acquisition in the context of the ILC's existing operations and balance sheet, and the inherent challenges and risks involved in acquiring a large and complex tourism business, McGrathNicol considers that it was ambitious to assert to key stakeholders that a purchase of this materiality would not have a significant impact on the ILC's operations and land acquisitions in the future. It is clear that an ongoing and active management of the post-acquisition implementation would be required, regardless of the success of the acquisition. ***Overall conclusions on the appropriateness of the acquisition of the ARR*** + Clear and strong warning signs were being expressed by the Minister for DoFD and the Minister for FaHCSIA, cautioning the ILC about the ARR purchase. + Significant risks were identified by the ILC's consultants in respect of the transaction. Whilst risk treatment activities were identified, these do not appear to have been sufficiently progressed by the ILC to manage the risks to an acceptable level. + The scale of the transaction was extraordinarily large in light of the ILC's ordinary business operations. The transaction absorbed the ILC's existing cash reserves and all but exhausted the ILC's borrowing limits under the ATSI Act. + In the light of these matters we believe the ILC was deficient in documenting the appropriate deliberation and assessment required to demonstrate sound business principles. This does not of itself mean that the acquisition was inappropriate. However, a transaction of this scale, requiring such significant borrowings, opens the ILC up to the charge that it did not adequately protect itself against downside risk.

2.1 Scope and background

McGrathNicol was engaged by the ILC to undertake a forensic audit of the acquisition of ARR and establishment of Voyages Indigenous Tourism Australia Pty Limited. The review requires McGrathNicol to examine all matters pertaining to the adequacy of the due diligence undertaken directly or on behalf of the then ILC Board in relation to the acquisition of the ARR and the establishment of Voyages.

Scope

In September 2013, the ILC engaged McGrathNicol to provide the following consultancy services:

- Component 1 - independent advice on the financial projections and short and long term strategies, including associated risks, regarding the performance of the ARR and strategies the ILC might pursue as owner of ARR to mitigate risks.
- Component 2 - a forensic audit of the acquisition of ARR and establishment of Voyages.

This report addresses Component 2 only.

Background to the Component 2 review

Following a Board initiated independent review of ILC corporate governance completed recently, several matters regarding the ARR acquisition, procurement process, Board governance and the establishment of Voyages were drawn to the ILC Board's attention. These observations were the catalyst for prompting the Component 2 review.

The forensic audit requires McGrathNicol to consider the adequacy of the due diligence undertaken directly or on behalf of the then ILC Board in relation to the acquisition of the ARR and the establishment of Voyages.

The detailed scope for Component 2 is attached at Appendix 1.

Sources of information

The information contained in the report includes:

- Information provided to McGrathNicol by ILC; and
- Discussions held with ILC management, ILC current and previous Directors; and other ILC consultants and stakeholders.

McGrathNicol is aware of a review of the ILC's borrowing powers and guarantee limits commissioned by the Minister for FaHCSIA and undertaken by KPMG, and that this review was completed in early 2011. We have been advised that there is a limitation of the distribution of KPMG's report, and accordingly, it has not been provided to us.

A full listing our sources of information relied on is set out at Appendix 2

About the ILC

The ILC is an independent statutory authority of the Australian Government established in 1995. The ILC's enabling legislation is ATSI Act. The ILC is also subject to the requirements of the CAC Act.

In accordance with the ATSI Act, the ILC has land acquisition and land management functions. The ILC's major policy statement is the National Indigenous Land Strategy ("NILS"). The NILS outlines policies, strategies, and priorities that guide the ILC's land acquisition and land management functions.

The ILC has the following priority outcomes for achieving Indigenous benefits through acquiring and managing land:

- Access to and protection of cultural and environmental values; and
- Socio-economic development.

By committing to these priorities, the ILC is helping to Close the Gap between Indigenous and non-Indigenous Australians and build a secure and sustainable Indigenous land base now and for future generations.

In 2008, GPT invited proposals for the acquisition of its Central Australian assets, including the ARR. WU, holding a first right of refusal provided by GPT allowing them to match any concrete offer, approached the ILC about working together to purchase the ARR. In December 2008, the ILC submitted a non conforming offer to purchase the ARR. This led to GPT providing the ILC a 30 day exclusivity period in early 2009 in which to enter into a transaction. Whilst negotiations between the ILC and GPT continued throughout most of 2009, as a result of the ILC's inability to source sufficient funding, negotiations temporarily ceased in November 2009.

The purchase of the ILC

The ARR is located adjacent to the Uluru-Kata Tjuta National Park in the Northern Territory. On 15 October 2010, the ILC entered into an agreement with GPT to acquire the ARR. The acquisition completed on 23 May 2011. The assets comprising the ARR that were acquired included the following:

+ The 104,000 hectares of freehold land on which the resort is situated;
+ Lease and operation of Ayers Rock (Connellan) airport;
+ The plant and equipment including computer equipment and motor vehicles;
+ The Voyages management and booking office and the Voyages platform assets;
+ The intellectual property of the ARR and Voyages;
+ The township of Yulara including staff accommodation, retail shopping centre, petrol station, visitor information centre, conference centre and recreational facilities; and
+ Other assets such as trading stock, interests in contracts and rights relating to the operation of the ARR businesses.

The ILC's initial interest in the ARR

In 1999, GPT first offered for sale a package of assets that included the ARR. However, it was not until 2008 that the ILC first became interested in the acquisition of the ARR. In July 2008 GPT offered for sale a package of Central Australian property consisting of the ARR, Alice Springs resort, Kings Canyon resort, El Questro resort and Wrotham Park resort. The ILC were approached by WU, an Aboriginal corporation representing communities around Uluru, regarding the opportunity to purchase the ARR. In 1997, WU signed a deed and first right of refusal with GPT to purchase the ARR assets. The first right of refusal allowed WU to match any "concrete offer" from another party for the ARR, if it can raise funds to match the offer by itself or in a joint venture with another entity.

As WU did not have the capacity to undertake the transaction on its own, it engaged advisers Wayne Kirkpatrick, Glendle Schrader and GS to assist it in finding partners to form a consortium to purchase the ARR.

We understand from discussions with ILC that representatives of FaHCSIA suggested to WU that they should approach ILC about being part of the consortium for the potential purchase of the ARR. Following the approach from WU, on 27 August 2008 the ILC Board resolved that it would pursue the acquisition of the ARR.

In late 2008, an agreement was drafted for the ILC and WU to work together in respect of the acquisition of the ARR. Whilst this agreement was not signed by the ILC, from this point on the ILC took control of pursuing the acquisition of the ARR, with WU's role significantly reduced.

The ILC engaged GS as lead due diligence advisor in October 2008. As part of their role, GS identified a number of other consultants to provide due diligence advice in respect of legal, accounting, capital expenditure, environmental, airport licencing and other matters.

In December 2008, the ILC submitted a non conforming offer for the ARR and the El Questro resort. In late January 2009, GPT agreed to provide the ILC with a 30 day exclusive dealing period. From February 2009 to November 2009 the ILC continued in negotiations and discussions with GPT regarding the purchase of the ARR. However, due to the ILC's inability to arrange funding for the resort from the Aboriginal and Torres Strait Island Land Account ("the Land Account"), negotiations temporarily ceased in November 2009.

In early 2010, GPT agreed to provide vendor financing to the ILC, which enabled negotiations for the purchase of the ARR to recommence. In August 2010, the ILC's accounting due diligence advisor identified that first half 2010 results for the ARR were down on forecast. This led the ILC to offer a revised purchase price of $270 million for the ARR. Whilst GPT rejected this revised offer, in August 2010 GPT agreed to provide a $25 million capital expenditure allowance to the ILC over five years. On 1 October 2010, the ILC Board resolved to purchase the ARR for a net purchase price of $292 million and a sale agreement was executed with GPT on 15 October 2010.

Recommencement of negotiations

In late 2009 GPT again offered the ARR to market. At a meeting between ILC Director Baffsky and GPT CEO Michael Cameron in December 2009 it was identified that if GPT was able to assist the ILC with the financing of the acquisition of the ARR, a transaction may be able to be progressed. From early 2010 to mid 2010 a range of transaction structures were discussed, that generally involved the ILC acquiring 54% of the ARR initially (through a combination of equity and vendor financing) and GPT retaining the remaining 46% (with an option to sell this interest to the ILC five years after the transaction is entered into).

The ILC obtained legal advice that the ATSI Act prevented it or a subsidiary from issuing securities. Accordingly, in July 2010 it was agreed by the parties that the ILC would acquire 100% of the ARR, but significant funding would be provided by GPT. Also, a key component of the transaction was that five years following completion of the acquisition, the ultimate amount payable to GPT would be uplifted by a minimum of $17 million based on growth in value of the ARR. A Heads of Agreement was entered into on 13 July 2010 setting out a proposed transaction price of $300 million, plus a minimum capital uplift payable to GPT of $17 million.

In August 2010 Horwath (engaged by the ILC to provide accounting due diligence advice) advised the ILC that ARR first half 2010 actual EBITDA results were lower than forecast, which may impact negatively on valuation. Following this, the ILC wrote to GPT seeking a reduction in the purchase price to $270 million. This request was refused by GPT, though it is noted that in August 2010, incorporated into the proposed transaction structure was payment by GPT to the ILC of $25 million over 5 years to cover capital expenditure on the ARR.

Final Board approval and execution of the agreement for ILC to purchase the ARR

At the 1 October 2010 meeting of the ILC Board, it was resolved that the ILC should enter into a transaction with GPT to acquire the ARR. Two ILC Directors (ILC Director Ian Trust ("Director Trust") and Director Kevin Driscoll ("Director Driscoll")) abstained from voting on the resolution to purchase the ARR. McGrathNicol was advised by Director Max Gorringe ("Director Gorringe") that he had not supported the transaction at this meeting.

The Sale and Purchase Agreement sets out a headline price of $300 million, and the acquisition was for a net purchase price of $292 million as illustrated on page 17. The acquisition timetable is illustrated at Appendix 3.

On 15 October 2010, the ILC entered into an SPA with GPT for the acquisition of the ARR based on a total purchase price of $300 million, payable in three installments. The SPA also included 6.5 % per annum interest on deferred installments, a minimum $17 million valuation uplift payment to GPT at the end of five years and $25 million contributions from GPT over five years. Under the SPA, the net purchase price equated to $292 million.

Net purchase price under the Sale Purchase Agreement

On 15 October 2010, the ILC entered into a contract with GPT for the acquisition of the ARR, including the following terms:

- $300 million, payable in three installments:
  - a Completion Payment of $81 million (including the $13.5 million deposit);
  - $81 million installment, payable on or before 12 months post settlement; and
  - $138 million installment, payable on or before 60 months post settlement;
- interest on the 12 month and 60 month installments:
  - 6.5% p.a. calculated daily paid quarterly in arrears until the installments are paid in full; and
  - 10% p.a. to be paid monthly on any part of the installments not paid within the required timeframe;
- a valuation uplift payable to GPT five years after completion, which is:
  - equal to 46.5% of the increase in the value of the ARR five years after Completion, over a $300 million base value, adjusted for capital expenditure, and will include:
    - a minimum of $17 million; and
    - an Excess Uplift Amount payable in addition to the minimum, which will not be known until five years after completion;
- $25 million capital expenditure contributions payable to the ILC over five years as claimed by the ILC:
  - based on actual capital expenditure incurred, not claimed more than once per month;
  - not exceeding the contribution amount for each year, plus any unclaimed amounts from prior years; and
  - plus 6.5% p.a. interest calculated daily on any portion of contribution amounts not paid by the end of each year.

Under the SPA, the net purchase price equated to $292 million.

Net Purchase Price under the SPA	$'000 Value
Instalments	
Deposit	13,500
Completion Date Payment	67,500
12 month instalment	81,000
60 month instalment	138,000
Total Purchase Price	300,000
Uplift Payment	
Minimum Uplift Amount	17,000
Excess Uplift Amount (amount payable in excess of the minimum uplift amount)	?
Total Uplift Payment	17,000
GPT Capital Contribution	
Capex Yr 1	(4,000)
Capex Yr 2	(8,000)
Capex Yr 3	(8,000)
Capex Yr 4	(3,000)
Capex Yr 5	(2,000)
Total GPT Capital contribution	(25,000)
Net Purchase Price	**292,000**

Source: Sale Purchase Agreement

We note the following matters which do not impact the net purchase price of $292 million under the Sale Purchase Agreement at the time of entering into the transaction:

- ILC paid a $2.03 million settlement adjustment to reflect changes in working capital and other matters between the exchange date and the date of settlement;
- GPT Capital Contributions were settled early in 2012 for a calculated present value of approximately $22 million.

MCN+ MCGRATHNICOL

We consider that ILC had a requirement to demonstrate value for money in respect of the ARR acquisition, and a critical element of this is consideration of the valuation of the asset, and negotiation of the best purchase price possible. In this section of the report we have reviewed the valuation due diligence and negotiations conducted by the ILC to endeavor to obtain value for money. We have also reviewed the presentation of this due diligence information to the ILC Board to facilitate their decision making.

The ILC's strategy to obtain value for money in respect of the ARR acquisition

The ILC set out in its own Procurement policy (*ILC, May 2007, Purchasing – User Guide*) that the ILC conducts its procurement in accordance with the key principles of the CPG's, including the core principle of achieving value for money. We consider that ILC had a requirement to demonstrate value for money in respect of the ARR acquisition, comprising both consideration of the valuation of the asset and negotiation of the best purchase price possible.

In this section of the report we have reviewed the valuation due diligence and negotiations conducted by the ILC to endeavour to obtain value for money for the acquisition. We have also reviewed the presentation of this due diligence information to the ILC Board to enable Board members to make a decision in respect of the proposal to acquire the ARR. Accordingly, in this section we have:

- reviewed the Colliers International valuation commissioned by the ILC in 2008, and the relevance of this valuation to the decision to acquire the ARR;
- reviewed the CBRE valuation commissioned by the National Australia Bank Ltd ("nab") in 2009, and the relevance of this valuation to the decision to acquire the ARR;
- considered the financial modelling undertaken by GS, including the net present value analysis presented to the Board in October 2010, and the relevance of this valuation to the decision to acquire the ARR; and
- assessed the evidence to support whether the ILC and its lead due diligence advisor (GS) undertook sufficiently robust negotiations to ensure that the best possible outcome for the ILC was obtained.

It is noted that other elements of value for money relevant to this acquisition include the requirement for the transaction to be appropriate in accordance with the ILC's functions, and the extent to which the transaction may achieve Indigenous employment outcomes. The ILC Board minutes and Board papers generally reflect an intention of the ILC Board that regardless of how beneficial the potential Indigenous employment outcomes could be, the ARR acquisition had to be economically viable and stand up from a financial perspective. Accordingly, in this section we have assessed value for money solely from a financial perspective.

On 1 October 2010 GS advised the ILC Board that the NPV of all payments to GPT under the transaction arrangements was $273 million. It appears this was calculated using the Weighted Average Cost of Capital ("WACC") determined by Grant Samuel to discount the cashflows. We question the validity of this calculation, as it is not appropriate to discount the purchase price installments and interest payments at a WACC, and it does not appropriately factor in the potential quantum of the uplift payment. However, it is noted that the SLA Proposal set out a net purchase price of $292 million, and this is likely to have been the value the ILC Board considered to be the purchase price.

Net Present Value of purchase price

On 1 October 2010, Grant Samuel gave a presentation to the ILC Board advising that the value of the ARR was $292 million. In the presentation, Grant Samuel also advised that:

- *"The NPV of all payments to GPT (including interest and GPT's share of the valuation uplift) is $273 million at a 9.7 % discount rate."*

Additionally, in email correspondence from GS to the ILC (including Director Baffsky and the ILC General Manager, David Galvin) dated 2 September 2010, GS advised the ILC that the proposed transaction structure provided GPT with a headline sale price of $300 million, while allowing the ILC to effectively pay consideration of $270 million.

We note that based on the 1 October 2010 presentation, it appears the analysis of the NPV of the effective transaction price was calculated using a Weighted Average Cost of Capital ("WACC") determined by GS to discount the cashflows.

However, we question the validity of this calculation, noting:

- it is not appropriate to discount the purchase price installments, and interest payments at the business' WACC (as discussed across); and
- the calculation is undertaken on the basis that the uplift payment will be the minimum contractual amount, $17 million, five years after the transaction. However, under the SPA, there is no limit to the upper value that may be required to be paid. Accordingly, the calculation does not appropriately factor in the potential for the uplift payment to be higher than $17 million.

Further, we note that the SLA Proposal sets out that the negotiated purchase price under the SPA equated to a net purchase price of $292 million, based on:

- a headline price of $300 million;
- plus the $17 million minimum uplift in year five; and
- less $25 million contributions from GPT over five years.

Accordingly, it appears the net purchase price considered by the ILC in assessing the transaction was based on a net value of $292 million.

Discounting purchase price installments

We do not consider that it is appropriate to discount the purchase price installments, and interest payments at the business' WACC.

- The risk associated with the uncertainty of future cashflows should be taken into account when setting a discount rate to determine the present value of forecast cashflows.
- A WACC is a discount rate designed to reflect the specific risks of not achieving forecast cashflows from a business overall, therefore is appropriate to use to discount the forecast cashflows of that business.
- However, in determining the NPV of the effective transaction price, there is significantly less uncertainty regarding the timing or quantum of the transaction payments which are legally binding as set out in the sale and purchase agreement.
  - Under the Sale and Purchase Agreement, the purchase price installments incur a cost of 6.5% p.a. interest.
- Accordingly, it would be more appropriate to discount the installment payments, and the interest payments at the vendor finance costs (i.e. 6.5%).

In late 2008, GS engaged Colliers International to provide a valuation of the ARR to assist in the consideration of initial offers. While the valuation was influential in the ILC determining initial offers and negotiations in late 2008 and early 2009, and was considered by the ILC Board throughout the transaction negotiations, by October 2010 the valuation was outdated and less influential on the ILC Board's decision to enter into the transaction.

Overview of the Colliers International December 2008 valuation of the ARR

In late 2008, GS were assisting the ILC to prepare for the submission of an initial offer in response to an Information Memorandum. GS engaged Colliers International to prepare a fair market valuation of the ARR and the Airport on 17 November 2008.

The valuation provided by Colliers International ("Colliers Valuation") is summarised in the table below:

Summary of Colliers International Valuation Report			
Date	+ 1 December 2008		
Presentation	+ Formal valuation report		
Asset valued:	+ Freehold interest of the Ayers Rock Resort, and the leasehold interest of the Ayers Rock (Connellan) Airport		
Adopted Value	+ $290 million		
Methodologies	**Last Yr Capitalisation**	**3rd Yr Capitalisation**	**Discounted Cash Flow**
Basis:	Income: $25,691,396	Income: $27,902,554	10 Years
	Capitalisation Rate: 9%	Capitalisation Rate: 9%	Discount Rate: 11.75%
			Terminal Yeild: 9.75%
Valuation	285,459,954	293,711,097	305,949,819
Less Capex	11,200,000	11,200,000	11,200,000
Net Valuation	**274,259,954**	**282,511,097**	**294,749,819**

Source: Colliers International, 1 December 2008, Valuation Report Ayers Rock Resort Lasseter Highway Yulara, Nothern Territyry

Valuation outputs

The Colliers Valuation of $290 million was based on their determination of an average net value of $288 million across the three methodologies applied. However, we calculate the average to be approximately $284 million based on the three valuation methodologies.

The Colliers valuation included sensitivity analysis against 1 % movements in the yield and discount rate, which indicated an impact on the Discounted Cash Flow valuation between $282 million and $310 million.

Relevance to the transaction

The following factors should be taken into account with respect to the relevance of the Colliers Valuation to the ultimate transaction and purchase price agreed by the ILC.

- The valuation allowed $11.2 million for immediate capital expenditure on infrastructure works and reserves for furniture fittings and equipment at 4 % of revenue. However, the valuation did not account for works required to improve or maintain resort accommodation (as identified by due diligence consultants in early 2009).
- Colliers International commented on a number of factors that would likely impact any range that purchasers would place on the value of the assets, including:
  - not having an indication of any offers made by other interested parties, which was considered crucial information in determining the valuation;
  - the isolated geographic location;
  - the valuation assumed a 'willing seller' and 'willing buyer' scenario and accordingly, the valuation:
    - assumed a competitive bidding process; and
    - excluded the possibility that GPT may have been a forced seller (which at one stage appeared to be the perception of the ILC Board members).
- Given prevailing market uncertainty at the time, Colliers International recommended that regular valuation updates be sought throughout the transaction negotiations.

Impact on transaction negotiation

The Colliers Valuation appeared to be influential for the ILC in determining initial offers and negotiation in December 2008 and January 2009. Having regard to the Colliers Valuation, and also to GPT's potentially distressed position, GS recommended an initial offer of $288 million. We note the Board's initial offer was for $265 million.

However, by the time of the ARR acquisition in October 2010, the Colliers Valuation was 22 months old and, although considered by the ILC Board throughout 2009, it did not appear to have significant influence on the final decision to enter into the transaction.

In April 2009, the nab sought a valuation of the ARR from CBRE to assist in considering the ILC's financing application with respect to its proposed $270 million purchase of the ARR. CBRE concluded that a contract price of $270 million was within market parameters, and adopted a value exactly equal to the proposed contract price. Whilst it was 17 months old as at the date of the transaction, the CBRE Valuation appears to have been a key factor influencing the ILC Board's ultimate decision to proceed.

Overview of the CBRE May 2009 valuation of the ARR

In April 2009, the ILC sought financing proposals from nab, ANZ and Westpac Banking Corporation Limited ("Westpac") with respect to the proposal to acquire the ARR. In May 2009, nab sought a valuation from CBRE. The valuation ("CBRE Valuation") is summarised in the table below:

Summary of CBRE Valuation Report			
Date	+ 26 May 2009		
Presentation	+ Formal valuation report		
Asset valued:	+ Freehold interest of the Ayers Rock Resort, and the leasehold interest of the Ayers Rock (Connellan) Airport		
Adopted Value	+ $270 million		
Methodologies	**Stabilized income Capitalisation**	**Discounted Cash Flow**	**Discounted Cash Flow**
Basis:	Income: $31,419,846 Capitalisation Rate: 10%	5 Years Discount Rate: 11.75% Terminal Yeild: 9.75%	10 Years Discount Rate: 11.75% Terminal Yeild: 9.75%
Valuation	314,198,463	N/A	N/A
Less Capex (PV)	43,827,949	(Included in Cashflows)	(Included in Cashflows)
Net Valuation	270,370,514	269,611,000	273,829,000
Rounded to:	**270,250,000**	**269,500,000**	**273,750,000**

Source: CBRE, 26 May 2009, A Valuation Report Prepared For The Indigenous Land Corporation and National Australia Bank Of Ayers Rock Resort Yulara Drive Yulara Northern Territory

Valuation outputs

CBRE adopted a valuation of $270 million based on the three methodologies applied, and concluded that a contract price of $270 million was "within market parameters".

We note the purpose of the valuation was to assist nab in considering its financing proposal with respect to a proposed $270 million contract price.

Impact on transaction negotiation

Although the CBRE Valuation had become significantly dated (17 months old) at the time of entering into the transaction, it appears to have been a key factor influencing the ILC Board's consideration of the transaction, and the ultimate decision to proceed with the transaction in October 2010. We note the following:

+ ILC Board meeting minutes and briefing packs indicate the Board considered the potential purchase price against the CBRE valuation throughout the progression of the transaction and negotiations.
+ In correspondence with the Department and Ministers with respect to the transaction, the ILC made reference to the CBRE valuation.
+ The ILC SLA Proposal dates 1 Oct 2010, presented to the Board at meeting No. 136 cited the CBRE Valuation as a factor in the basis of negotiating the purchase price.
+ The Risk Management Plan included in the SLA Proposal, lists the CBRE Valuation as a proposed treatment for the risk that the purchase price is not commensurate with the ARR's value.

Given the CBRE Valuation appears to have had a significant influence on the ultimate decision to enter into the transaction, it is important to consider:

+ the robustness of, and any technical matters with respect to the valuation;
+ how the ILC factored the CBRE Valuation into their consideration of the ultimate purchase price;
+ any sensitivity analysis included in the CBRE Valuation; and
+ the operating forecasts underlying the valuation.

3.4 CBRE valuation of ARR May 2009 – Technical matters

We have read the CBRE valuation of ARR in the context of the October 2010 acquisition. Our findings are that the CBRE valuation report appears to be robust and well supported. However, due to the date the report was completed, it would not have been appropriate to wholly rely upon the conclusions in the report for considering a purchase price for the ARR in October 2010 especially given changes in the operating performance of the ARR which the ILC Board was aware of.

CBRE & the CBRE Valuation Report:

CBRE is one of the leading full service commercial real estate firms in Australia. They are well known for their expertise in the market.

The CBRE report is a robust valuation that includes the following:

- detailed review of the property, accommodation and facilities;
- summary of potential environmental issues;
- overview of historical improvements;
- analysis of historical and forecast capital expenditures;
- overview of the tourism industry and hotel investment market in Australia;
- financial and trading analysis of the ARR;
- Strengths, Weaknesses, Opportunities and Threat (“SWOT”) analysis presenting positive and negative characteristics of the resort;
- application of two valuation approaches:
  - the Capitalisation Analysis; and
  - Discounted Cash Flow Analysis;
- sensitivity analysis varying Average Daily Rate (“ADR”) and Occupancy assumptions; and
- a $270 million valuation conclusion for the ARR on a going concern basis.

Potential technical issues from using the CBRE report in 2010:

The following technical issues limit the reliability of the CBRE report for use in setting a price in the October 2010 acquisition:

- market value, liquidity and pricing can change significantly over a short period of time in the real estate market, particularly following the start of the GFC in 2008. The timespan between May 2009 (the date of the CBRE report) and October 2010, (the date a final price was being negotiated for the ARR) is wide enough to limit the reliability of the conclusions contained in the CBRE report;
- in addition to market conditions changing, the ARR had continued to underperform against expectations subsequent to the finalisation of the CBRE valuation;
- the CBRE valuation conclusion seems to be limited to opining to the reasonableness of a $270 million price for the transaction contemplated at the time; and
- while various sensitivity analyses were presented that suggested a range of values around $270 million, the report does not specifically conclude on the values in those ranges.

Conclusions:

While we have not performed a full review of the CBRE valuation that a real estate valuation expert might perform, the CBRE valuation appears to have been a robust and well supported analysis.

Due to the timespan between the date of the CBRE valuation and the date the ARR was acquired, it is not unreasonable to assume that CBRE could have had significantly different valuation conclusions if it had updated its report on or around October 2010.

Although the CBRE Valuation appears to have heavily influenced transaction negotiations and the ultimate decision to proceed with the transaction, it appears the ILC considered the net purchase price of $292 million as commensurate with the top end of a $250 million to $290 million range identified as the CBRE Valuation. However, the ultimate purchase price exceeded CBRE's adopted $270 million valuation by $22 million.

ILC's consideration of the CBRE Valuation v ultimate purchase price

The CBRE Valuation appears to have been heavily influential on transaction negotiations and the ultimate decision to proceed at the agreed net purchase price of $292 million. However, based on the documentation reviewed, it appears the ILC considered the valuation as a range of values, whereas the CBRE Valuation is clearly stated in the report as an adopted valuation of $270 million. We noted that:

- ILC Board meeting minutes and briefing packs indicate CBRE valued the ARR between a range of $250 million to $290 million; and
- The SLA Proposal dated 1 October 2010, presented to the Board at meeting No. 136, cites the CBRE Valuation as between $250 million to $290 million.

The 1 October 2010 SLA Proposal indicated the CBRE Valuation was a factor in negotiating the purchase price stating:

"The purchase price for ARR has been arrived at through a very intensive period of negotiation and through the use of … independent valuations." (p. 27)

In describing the independent valuations sought, the SLA Proposal only identifies the CBRE Valuation, stating the *"ARR was valued between $250 - $290 million in 2009"* (p. 27) and citing the CBRE Valuation.

The SLA Proposal then sets out the negotiated purchase price, stating the net purchase price would be $292 million.

Accordingly, it appears that the ILC Board considered the net purchase price of $292 million as being commensurate to the top end of the $250 million to $290 million range identified as the CBRE Valuation.

As described on the following page, it appears that the range was attributed to the sensitivity analysis provided in the CBRE Valuation report. However, the ultimate purchase price exceeded the adopted valuation by $22 million.

The CBRE Valuation provided sensitivity analysis indicating the value of the ARR had a higher sensitivity to changes in the terminal yield than to changes in the discount rate applied, and a higher sensitivity to changes in occupancy levels than changes in room rates. It appears the ILC may have adopted a valuation range of $250 to $290 million from the sensitivity tables included in the report. However, this did not reflect the full range of sensitivities and it is not certain that CBRE itself considered this to be a valuation range.

CBRE Adopted Valuation Sensitivity Analysis

Five Year DCF Sensitivity by IRR and Terminal Yield

Terminal Yield \ Internal Rate of Return	12.93%	12.43%	11.93%	11.43%	10.93%
11.00%	240,000	250,000	250,000	260,000	260,000
10.50%	250,000	260,000	260,000	270,000	270,000
10.00%	260,000	260,000	270,000	280,000	280,000
9.50%	270,000	280,000	280,000	290,000	290,000
9.00%	280,000	290,000	290,000	300,000	310,000

Valuation Sensitivity by Trading Variance

Average Daily Rate \ Occupancy	2.50%	1.25%	0.00%	(1.25%)	(2.50%)
2.50%	240,000	250,000	260,000	270,000	280,000
1.25%	246,000	256,000	266,000	276,000	286,000
0.00%	251,000	261,000	270,000	281,000	292,000
(1.25%)	256,000	267,000	277,000	287,000	297,000
(2.50%)	262,000	272,000	283,000	293,000	303,000

CBRE Capitalization Sensitivity Analysis

Capitalization Rate Sensitivity

Capitalization Rate	
10.50%	254,750
10.00%	270,250
9.50%	287,500

Average Daily Rate & Occupancy Sensitivity

Average Daily Rate \ Occupancy	2.50%	0.00%	(2.50%)
2.50%	239,000	259,000	279,000
1.25%	244,500	264,750	285,000
0.00%	250,000	270,250	290,750
(1.25%)	255,250	276,000	296,500
(2.50%)	260,750	281,750	302,500

CBRE Discounted Cash Flow Sensitivity Analysis – Five Year

Five Year DCF Sensitivity by IRR and Terminal Yield

Terminal Yield \ Internal Rate of Return	13.00%	12.50%	12.00%	11.50%	11.00%
11.00%	250,250	250,750	251,250	251,750	252,250
10.50%	259,000	259,500	260,000	260,500	261,000
10.00%	268,500	269,000	269,500	270,250	270,750
9.50%	279,250	279,750	280,250	280,750	281,250
9.00%	291,000	291,500	292,250	292,750	293,250

Valuation Sensitivity by Trading Variance

Average Daily Rate \ Occupancy	2.50%	1.25%	0.00%	(1.25%)	(2.50%)
2.50%	238,750	248,500	258,500	268,250	278,000
1.25%	244,250	254,000	264,000	274,000	283,750
0.00%	249,500	259,500	269,500	279,750	289,500
(1.25%)	255,000	265,000	275,250	285,250	295,250
(2.50%)	260,250	270,500	280,750	291,000	301,000

CBRE Discounted Cash Flow Sensitivity Analysis – 10 Year

Ten Year DCF Sensitivity by IRR and Terminal Yield

Terminal Yield \ Internal Rate of Return	13.00%	12.50%	12.00%	11.50%	11.00%
11.00%	245,500	253,500	262,250	271,000	280,500
10.50%	250,500	259,000	267,750	277,000	286,500
10.00%	256,000	264,750	273,750	283,250	293,250
9.50%	262,250	271,250	280,500	290,250	300,500
9.00%	269,000	278,250	288,000	298,250	308,750

Valuation Sensitivity by Trading Variance

Average Daily Rate \ Occupancy	2.50%	1.25%	0.00%	(1.25%)	(2.50%)
2.50%	242,250	252,250	262,250	272,250	282,250
1.25%	247,750	258,000	268,000	278,250	288,500
0.00%	253,250	263,500	273,750	284,000	294,250
(1.25%)	258,750	269,250	279,500	289,750	300,000
(2.50%)	264,500	274,750	285,250	295,750	306,000

CBRE Sensitivity analysis provided

The CBRE Valuation provided four sets of sensitivity analysis being: adopted valuation sensitivities; capitalisation sensitivities; five year Discounted Cash Flow ("DCF") sensitivities; and 10 year DCF sensitivities. The sensitivity analysis indicates across the valuation methodologies that approximately:

- a +/-1 % variance to discount rate results in a $20 million valuation variance, and a +/-1 % variance to terminal yield results in a $40 million valuation variance; and
- a +/-2.5 % variance to occupancy results in a $40 million valuation variance, and a +/-2.5 % variance to average daily rates results in a $20 million valuation variance.

Source: CBRE, 26 May 2009, A Valuation Report Prepared For The Indigenous Land Corporation and National Australia Bank Of Ayers Rock Resort Yulara Drive Yulara Northern Territory

It appears the ILC's consideration of the CBRE valuation as a range between $250 million and $290 million may have been drawn from the sensitivity tables included in the report, as highlighted in the five year DCF sensitivity tables above.

However, the sensitivity analysis was provided by CBRE as a guide in support of their valuation opinion, and does not necessarily equate to a valuation range.

Further, we note that the rate sensitivity table for the five year DCF methodology table appears to be flawed, indicating values equivalent to a +/-0.1 % variance to the discount rate rather than +/-1 % as stated. However, this inconsistency does not appear to impact the adopted valuation sensitivities or the 10 year DCF sensitivities. Accordingly, we have not sought to adjust the five year DCF sensitivity tables as presented by CBRE.

3.4 CBRE valuation of ARR May 2009 – operating forecasts

Although the CBRE Valuation appears to have been influential on the ILC, it was 17 months old at the time of the transaction. It does not appear that any analysis was undertaken to update the operating forecasts underlying the valuation between May 2009 and October 2010. Updating the CBRE valuation operating forecasts in line with the first half 2010 actual results indicates a DCF valuation in the order of $250 million.

As outlined above, the CBRE valuation was highly influential on the Board's decision to acquire the ARR, but was 17 months old at the date the transaction was entered into. In order to assess whether the CBRE valuation was likely to have materially changed at 1 October 2010, we have reviewed the actual results for 2009 and first half 2010, and compared these to the forecasts in the CBRE Valuation.

CBRE Operating Forecasts

The CBRE Valuation was prepared in May 2009, and included operating forecasts prepared by CBRE based on review of historic trading results for 2006, 2007, 2008, the first four months of 2009 actual results, and 2009 forecasts prepared by ARR Management provided by the vendor. The operating forecasts prepared by CBRE included forecasts for the period 2009 to 2019.

ARR 2009 and 2010 actual operating performance

CBRE forecast approximately $21.6 million EBITDA for 2009, and $28.0 million for 2010. Although 2009 ARR actual EBITDA totalled approximately $28.1 million, exceeding CBRE's projections, due diligence identified underperformance in early 2010.

In their due diligence report provided to the ILC in August 2010, Horwath raised concerns over the ARR's recent trading downturn at the time and questioned whether the forecast 2010 results were achievable, highlighting that the first half of 2010 results fell short of budget by 12 %.

Profit & Loss YTD June 2010 ARR Consolidated

$'000	Actual	Budget	2009	% Vairance
Revenue	45,129	48,197	46,597	*(6%)*
Operating Costs	(23,952)	(24,793)	(23,466)	*(3%)*
Overhead Costs	(13,146)	(14,316)	(12,310)	*(8%)*
EBITDA	**8,031**	**9,088**	**10,821**	***(12%)***

Voyages Corporate Office Due Diligence Report August 2010

Impact of actual operating performance on the CBRE Valuation

Based on the material deterioration in 2010, Horwath expected the results indicated *"the likelihood of actual performance during the second half of 2010 being well below the Forecast level, with the consequence of a substantial shortfall against Forecast 2010".*

The Horwath report identified that ARR management's 2010 budget was $26.7 million. Assuming a similar 12 % underperformance in the second half of 2010, as occurred in the first half, the 2010 budget would be approximately $24.8 million, $3.3 million less than CBRE's projection.

Although the CBRE valuation was 17 months old at the time of entering into the transaction, and actual ARR trading for the first half of 2010 was significantly different from CBRE's projections, no analysis appears to have been undertaken to update the CBRE Valuation between May 2009 and October 2010.

Adjusting the Year 1 operating forecasts in CBRE's five and 10 year DCF valuations for adjusted EBITDA of $24.8 million in 2010, and applying EBITDA growth on adjusted 2010 consistent with the CBRE Valuation from 2010 results in a valuation in the order of $250 million.

Adjusted CBRE Five Year DCF Valuation

Five Year DCF	Total PV $'000	Year 1 $'000	Year 2 $'000	Year 3 $'000	Year 4 $'000	Year 5 $'000	TV $'000
Forecast EBITDA		24,750	30,358	31,466	32,649	33,609	-
Forecast Capex		(13,500)	(20,514)	(21,006)	-	-	-
Net ARR Cashflows		**11,250**	**9,844**	**10,460**	**32,649**	**33,609**	**341,644**
Timing		0.50	1.50	2.50	3.50	4.50	5.00
Discount Factor		0.94491	0.84367	0.75328	0.67257	0.60051	0.56743
DCF	**262,814**	**10,630**	**8,305**	**7,879**	**21,959**	**20,182**	**193,858**
Acquisition Costs	(14,055)						
Net DCF Valuation	**248,759**						

Source: McGrathNicol

Grant Samuel prepared a financial model to assist the ILC in reviewing the cash flows of the ARR. Based on the financial model, GS presented to the ILC Board on 1 October 2010, advising the Net Present Value of ARR cash flows was $292 million, and recommending that the ILC proceed with the acquisition of the ARR based on the $292 million net purchase price.

Influence on the transaction

From 2008 through to the October 2010 transaction execution, GS undertook financial modeling to provide the ILC with analysis of the ARR's projected cash flows, and the likely Net Present Value ("NPV") of those cash flows ("GS financial model"). We note this was not a full speaking valuation.

On 1 October 2010 GS gave a presentation to the ILC Board, and advised under the heading "**Valuation**" that:

- *"The [NPV] of the ARR cash flows in the financial model is $292 million…"*; and
- *"The $292 million* ***valuation*** *compares to previous valuations of Colliers … and CBRE…"* (emphasis added).

Additionally, GS "*recommended that the ILC purchase Ayers Rock Resort and the Voyages platform on the terms proposed*". On 15 October 2010, 14 days after the presentation, the ILC exchanged contracts with GPT for the purchase of the ARR.

Accordingly, it appears that the GS Model and NPV assessment was significantly influential on the Board's ultimate decision to enter into the transaction.

Calculation of NPV

Although it was not the purpose of the GS financial model to provide the ILC with a full speaking valuation, and therefore did not include the preparation of a valuation report, Grant Samuel calculated a NPV of the ARR's cashflows in the model and presented this to the Board.

Our review of the information available to us identified two versions of the GS financial model around the transaction date, a 21 September 2010 version and a 20 October 2010 version.

McGrathNicol was advised by the ILC Chief Operating Officer ("ILC COO") that the 21 September 2010 version was the basis for the ARR cash flow modeling provided to the ILC Board on 1 October 2010. However, it does not include any NPV calculations. Although the 20 October 2010 version includes NPV calculations, it is dated after the transaction date and does not reconcile to the $292 million NPV.

Based on the ARR cash flows included in the 21 September version and the NPV methodology included in the 20 October version, it appears the 21 September version reconciles to the $292 million NPV, as shown in the table below. Accordingly, our analysis is focused on the 21 September 2010 version of the GS financial model.

Reconciliation of GS financial model to $292 million NPV

$'000		Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10
ARR Adjusted EBITDA		**19,169**	**21,251**	**27,852**	**34,362**	**42,711**	**46,095**	**47,036**	**48,261**	**49,512**	**50,789**
Change in Working capital		(2,550)	23	(781)	(783)	(1,002)	(655)	(140)	(177)	(182)	(187)
Tax Paid		(5,751)	(6,375)	(8,356)	(10,309)	(12,813)	(13,828)	(14,111)	(14,478)	(14,854)	(15,237)
ARR Capex		(19,412)	(19,106)	(6,728)	(4,101)	(4,392)	(4,594)	(4,720)	(4,862)	(5,007)	(5,158)
Net ARR Cashflows		**(8,544)**	**(4,207)**	**11,988**	**19,169**	**24,504**	**27,017**	**28,065**	**28,745**	**29,469**	**30,207**
Terminal Value											464,376
Timing		0.50	1.50	2.50	3.50	4.50	5.50	6.50	7.50	8.50	9.50
Discount Factor		0.9548	0.8703	0.7934	0.7232	0.6593	0.6010	0.5478	0.4994	0.4552	0.4150
NPV	**292,342**	**(8,157)**	**(3,661)**	**9,511**	**13,864**	**16,155**	**16,237**	**15,375**	**14,355**	**13,416**	**205,247**

Source: McGrathNicol, based on Grant Samuel ILC Financial Model_(21 Sep 10)_Final.xls (September Version) and ILC Financial Model_(20 Oct 10)_Sensitivities Analysis.xls (October Version)

We have performed a review of the methodology and calculations applied in the GS financial model. Based on our review, the GS financial model is consistent with what is commonly seen in acquisition models used for Mergers and Acquisition purposes in the wider market. The GS financial model is not cross checked against other valuation methods, and contains limited sensitivity analysis. This indicates it was not specifically delivered as a full speaking valuation opinion.

Overall methodology:

The DCF valuation methodology applied in the GS financial model is a common methodology used for acquisition pricing models.

Calculations:

We have reviewed the calculations, and with the following exceptions, we have not found material calculation or methodological errors:

- A 30% tax rate is assumed in the DCF calculations. It is unclear whether the tax benefit of the depreciation resulting from capital expenditure projects is reflected in the model.
- There does not seem to be a clear link between capital expenditures and depreciation. "Project Capex" assumptions in the model are hard-coded and do not seem to impact the calculation of depreciation going forward. This may have an impact on value.
- The valuation date is not stated specifically in the GS financial model, however it effectively is set to the beginning of FY11, i.e. 1 July 2010. Since the acquisition was as at 15 October 2010, there may be an inconsistency in the timing of the cash flows modelled to what was included in the transaction. However, this is not expected to have a material impact on value, unless there were any material cash inflows or outflows expected between 1 July 2010 and 15 October 2010 that need to be reflected/adjusted in the GS financial model.

We note that, as the valuation calculated in the GS financial model was presented to the ILC and used by them in considering the purchase price, we have not attempted to adjust the GS Model for the above minor calculation, or methodological errors.

Assumptions:

Addressed in the remainder for this report, the following are the key assumptions that drive the value estimated in the model:

- number of rooms available;
- occupancy rates;
- capital expenditures;
- income from the airport, food sales, spa, tours and activities; and
- cost growth.

There are hard-coded assumptions (e.g. project capital expenditures, room rates and Beta) which makes it difficult to determine the source of these assumptions.

Cross checking:

In any valuation it is best practice to test the results of a DCF model against other methodologies, if possible, including investigating prices paid in transactions of similar assets as a cross check to the value calculated by the DCF methodology. With respect to other methodologies, an implied Enterprise Value / EBITDA multiple is calculated in the GS financial model. Ideally, industry based cross checks would be included, such as Price / number of rooms, implied capitalisation rates and Internal Rates of Return, etc. compared to market data from prior transactions. These cross checks are not specifically included in the model. It is also noted that this is a unique resort which limits the comparability to prior transactions.

There are few sensitivity tables presented in the model that show alternative valuation conclusions based on changing key assumptions. Ideally the value impact of changing all key assumptions (such as room rates, occupancy, costs, growth rates, profit margins) would be analysed and presented. There are tabs in the model that present additional assumption scenarios, but they do not appear to be linked to calculations that produce valuations for these scenarios. Since this model was not specifically delivered as a full speaking valuation providing robust support for the ultimate purchase price, GS may have performed sensitivity analyses that are not included in this model. However, we have not identified any evidence of sensitivity analysis being conducted prior to the transaction being entered into.

Although presented to the ILC Board as conservative, based on comparison to historic trends, and to the projections underlying the Colliers and CBRE valuations, the operating forecasts underlying the GS financial model appear to be optimistic. However, in order to assess the reasonableness of operating projections, it is important to review the assumptions and key drivers underlying the projections, and sensitivity analysis undertaken with respect to operating assumptions.

Revenue and expense projections

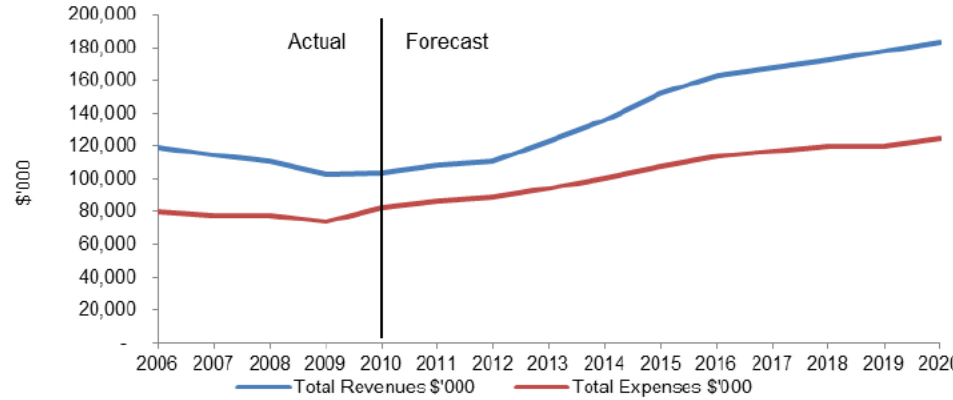
As illustrated (across), revenue in the years prior to the transaction was in decline, reducing from $119 million revenue in 2006 to $103 million in 2009 (actuals). However, revenue projections forecast in the GS financial model assume an immediate turn around, with revenues increasing from the first year of projections ($108 million in 2011 to $176 million in 2020).

Expenses are also projected to grow along with revenues:

- revenue growth is projected at 6 % p.a. on average; and
- expense growth is projected at 4 % p.a. on average.

As a result of revenue growth forecast to exceed expense growth, the diagram across the page illustrates the forecast widening gap between revenue and expenses.

GS Model Revenue and Expense Projections vs Actuals



Operating profit projections

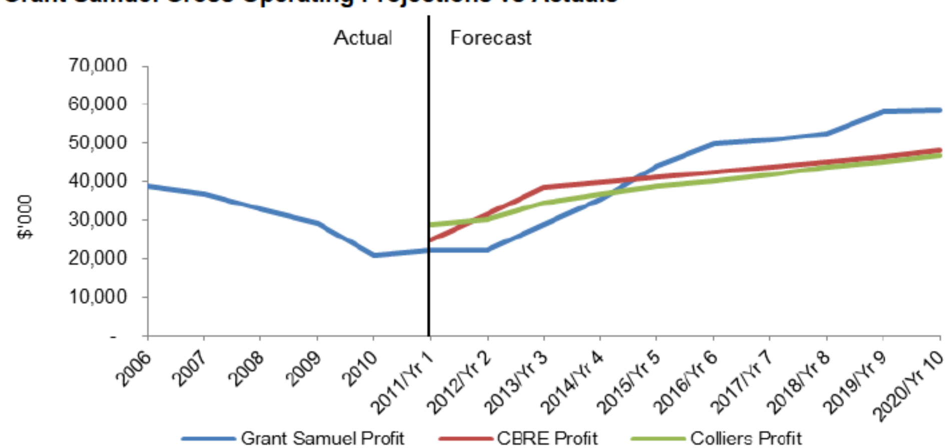
In the GS 1 October 2010 presentation to the ILC Board, the projections underlying the GS financial model were presented as conservative.

With revenue growth exceeding that projected for operating expenses, gross operating profit is projected to grow at 12 % per annum on average, growing by 122% over 10 years, from $24 million in 2010 to $53 million in 2020.

In comparison to the projections underlying the Colliers and CBRE independent valuations, the growth forecast in the Grant Samuel operating projections are more aggressive:

- Colliers projected 4 % p.a. revenue growth, 3 % p.a. expenses growth and 5 % p.a. profit growth; and
- CBRE projected 5 % p.a. revenue growth, 5 % p.a. expenses growth, and 8 % p.a. profit growth.

Grant Samuel Gross Operating Projections vs Actuals



3.5 Grant Samuel financial model assumptions - External factors impacting assumptions

Industry analysis in 2010 indicated that whilst there may be growth in visitor numbers and revenue in the next five years, the growth was forecast to be moderate, and tempered by restrained growth in domestic tourist numbers. Accordingly, it is expected that the GS financial model should have reflected limited growth attributable to expected improving economic conditions.

Review of forecasts – analysis of external and industry specific factors

In considering the appropriateness of forecasts, it is necessary to consider both the external and internal factors that may be impacting on the ARR both now, and over the forecast period.

In order to understand the external industry specific factors that were known (or should have been known) in October 2010 and incorporated into the development of the GS financial forecasts, we have reviewed the following publicly available material assessing the tourism and accommodation industries:

- "Territory Tourism Outlook 2009/10 to 2011/12", prepared by Tourism NT dated April 2010; and
- "Submission on the Northern Territory Budget 2010-2011", prepared by the Tourism and Transport Forum, dated December 2009.

Known factors impacting forecasts	Likely Impact
+ International visitors to the NT are expected to grow by 1.5% in 2010/11 and 2.3% in 2011/12. (Source: Tourism NT)	↑
+ Domestic visitor numbers are expected to increase by 1.4% in 2010/11 and 0.8% in 2011/12 (Source: Tourism NT)	↔
+ Between 2008 and 2018, growth in international visitor nights across Australia is forecast to be 3.8% per annum, though forecasts for the Northern Territory are below the other states. (Source: Tourism and Transport Forum)	↑
+ By 2018, domestic visitor nights in the Northern Territory are forecast to be around the same level as the mid 2000s (Source: Tourism and Transport Forum)	↓

Source: Industry reports (as referenced) and McGrathNicol

Conclusion on external factors

Whilst industry analysis in 2010 indicated that there may be growth in visitor numbers and revenue in the next five years, the growth is forecast to be moderate, and tempered by restrained growth in domestic tourist numbers. The growth assumptions used in the GS financial model are arguably optimistic in this context.

Occupancy is the main variable underlying operating projections in the GS financial model, being a direct driver of 8 of the 10 revenue categories and 8 of the 10 operating expense categories. Room revenues are also directly based on daily room rates, and account for 37% of total revenues. In order to assess the reasonableness of operating projections in the GS financial model, it is important to consider the occupancy and daily average room rate assumptions underlying the financial model.

Key revenue and expense drivers

The Grant Samuel financial model includes 10 categories of operating revenues and operating expenses for the ARR.

A summary of the key drivers with respect to each of the operating revenue and operating expense categories underlying the operating projections included in the financial model are set out in the table to the right.

The summary table indicates that the main drivers / assumptions underlying the Grant Samuel financial model include:

- occupancy;
- prior year results; and
- assumed growth rates.

Of the above three drivers, occupancy is the main variable underlying the operating projections. Occupancy is:

- a direct driver underlying eight of the 10 revenue categories;
- an indirect driver of one revenue category (through growth in room nights sold); and
- a direct driver underlying eight of the 10 expenditure categories.

Additionally, we note that "Rooms revenues" comprise the most significant revenue category, contributing approximately 37% of total revenues over the forecast period. In addition to occupancy, the daily average room rate is a key variable and driver of "Rooms revenues".

Accordingly, to assess the reasonableness of operating projections in the GS financial model, it is important to consider the occupancy and daily average room rate assumptions underlying the financial model.

Key Drivers underlying Grant Samuel financial model

Operating Revenues	% Total	Key Revenue Drivers
Rooms	37.5%	Occupancy, Rates
Food & Beverage	24.3%	Occupancy, assumed growth
Hotel Sundry	1.5%	Occupancy, assumed growth
Campground & Lodge	4.5%	Occupancy, assumed growth
Retail	16.7%	Occupancy, assumed growth
Airport	8.6%	Growth in no. room nights sold (Occupancy), Revenue per passenger (Inflation)
Property	4.8%	Growth on prior years (Inflation)
Touring & Activities	1.3%	Occupancy, sensitivity to occupancy, assumed growth
Spa	0.4%	Occupancy, assumed growth
Other	0.4%	Occupancy, assumed growth
Operating Expenses	**% Total**	**Key Expense Drivers**
Rooms	17.7%	Occupancy, sensitivity to occupancy, assumed growth
Food & Beverage	38.8%	Occupancy, sensitivity to occupancy, assumed growth
Hotel Sundry	0.9%	Occupancy, sensitivity to occupancy, assumed growth
Campground & Lodge	3.7%	Occupancy, sensitivity to occupancy, assumed growth
Retail	26.4%	Occupancy, sensitivity to occupancy, assumed growth
Airport	4.9%	Occupancy, sensitivity to occupancy, assumed growth
Property	4.7%	Growth on prior years (Inflation)
Touring & Activities	2.1%	Occupancy, sensitivity to occupancy, assumed growth
Spa	0.7%	Occupancy, assumed growth
Other	0.2%	Growth on prior years (Inflation)

Source: McGrathNicol based on Grant Samuel ILC Financial Model_(21 Sep 10)_Sent to Banks_Final.xls

Horwath highlighted in their 2010 due diligence report that the ARR's declining occupancy trend indicated decreased demand for the resort. However, occupancy appeared to stabilise at approximately 63% from 2004 to 2007, prior to the GFC. Occupancy projections in the GS financial model appear to stabilise at approximately 67%. Adjusting the GS Model for 63% stabilised occupancy results in a $250 million NPV of ARR Cashflows, compared to $292 million originally calculated in the GS Model.

ARR Occupancy trends

Horwath highlighted in their 2010 due diligence report a long term trend with occupancy declining from a peak of 81% in 2000 to 52% over the ten years to 2010. Horwath states this is indicative of a long term decrease in the demand for the ARR.

However, there appears to be a period where occupancy stabilised, and remained at approximately 63% from 2004 to 2007. Following this period of stability, occupancy began to decline again, falling to 51% in 2009 in the wake of the GFC.

	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
	A	A	A	A	A	A	A	A	A	A	A	A
Occupancy	*73%*	*79%*	*81%*	*77%*	*69%*	*59%*	*63%*	*65%*	*63%*	*63%*	*59%*	*51%*

Source: Horwath: Key Issue 2 - Long Term Revenue Trend Issue

ARR Occupancy Projections

The average occupancy projected in the GS financial model maintains post GFC levels in the first three years, and grows from a base of 53% over the following four years, to 65% in 2015 and stabilises at 67% for the years 2016 to 2020.

	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
	A/F	F	F	F	F	F	F	F	F	F	F
Occupancy	*52%*	*53%*	*53%*	*56%*	*59%*	*65%*	*67%*	*67%*	*67%*	*67%*	*67%*

Source: Grant Samuel Financial Model September 2010

Given the long term decline in occupancy highlighted by Horwath, the occupancy growth projected in the GS financial model appears to be overly optimistic.

Similarly, stabilised occupancy of 67% does not appear conservative if the period of stability at approximately 63% between 2004 to 2007 is considered indicative of stabilised occupancy prior to the impact of the GFC.

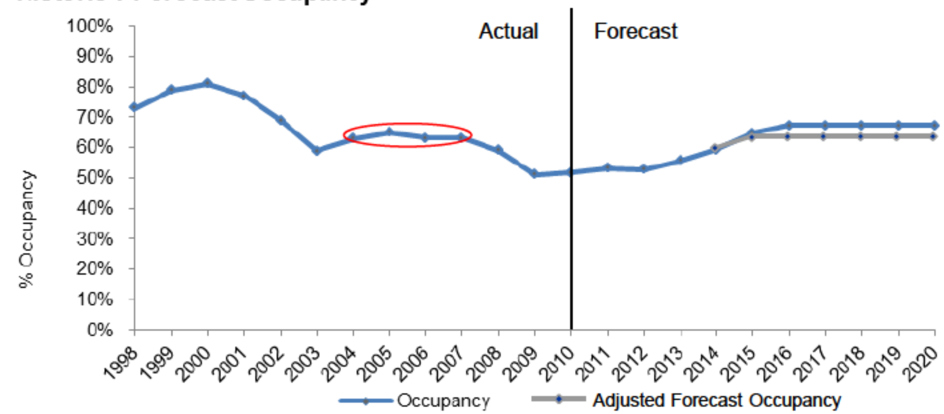
(Note: Our analysis of historical occupancy data did not include assessing the impact that number of rooms available, or room rates may have had on occupancy. Room rates were forecast by GS to increase consistent with historical growth and CPI).

Impact on GS's calculation of NPV of ARR Cashflows

Adjusting the GS financial model to reflect stabilised occupancy at 63% results in decreased net cash flows in years five to 10 of the projections, and significantly reduces the terminal value.

The impact is a reduction in the calculated NPV from $292 million to $250 million.

Historic v Forecast Occupancy



Adjusted Cashflow $ million		Yr 1	Yr 2	Yr 3	Yr 4	Yr 5	Yr 6	Yr 7	Yr 8	Yr 9	Yr 10
Adjusted Cashflows		**(8.5)**	**(4.2)**	**12.0**	**19.2**	**23.0**	**23.3**	**23.7**	**24.3**	**24.9**	**25.5**
Terminal Value											392.1
Timing		0.50	1.50	2.50	3.50	4.50	5.50	6.50	7.50	8.50	9.50
Discount Factor		0.95	0.87	0.79	0.72	0.66	0.60	0.55	0.50	0.46	0.41
NPV	**250.5**	**(8.2)**	**(3.7)**	**9.5**	**13.9**	**15.2**	**14.0**	**13.0**	**12.1**	**11.3**	**173.3**

Source: McGrathNicol

Capex projections included in the Grant Samuel financial model totalled $124 million over the ten year forecast period. The capex projections were based on FF&E reserves of between 2 and 3 % of total revenues, five year specific project expenditure forecasts prepared by PPM in July 2010 and an allocation of 2.5% total revenues for project capital expenditure in the longer term.

GS capital expenditure projections

The GS financial model included projections for capital expenditure ("capex") totaling $124 million over the ten year period following the proposed acquisition. The capex projections in the financial model included separate allowances for:

- furniture, fittings and equipment ("FF&E") reserves ($45 million over 10 years); and
- project capex ($78 million over 10 years).

$ millions	Total	Y1	Y2	Y3	Y4	Y5	Y6	Y7	Y8	Y9	Y10
FF&E Reserves	45.4	2.2	2.3	2.6	3.0	3.4	5.7	6.0	6.4	6.8	7.2
Project Capex	78.1	19.4	19.1	6.7	4.1	4.4	4.6	4.7	4.9	5.0	5.2
Total Capex	**123.5**	**21.6**	**21.4**	**9.3**	**7.1**	**7.8**	**10.3**	**10.7**	**11.2**	**11.8**	**12.3**

Source: Grant Samuel ILC Financial Model_(21 Sep 10)_Sent to Banks_Final.xls

FF&E reserves

The FF&E reserve projections included in the GS financial model are based on a percentage of operational revenues over the 10 year period.

- In the immediate and medium term, FF&E reserve capex is allowed for at 2 % of total revenue between years one and five of the projections.
- In the longer term, the FF&E reserves are allowed for at 3 % of total revenue for the years six to 10 of the projections.

Additionally, the FF&E reserve is adjusted for inflation at 3 % per annum over the period of the financial model's projections.

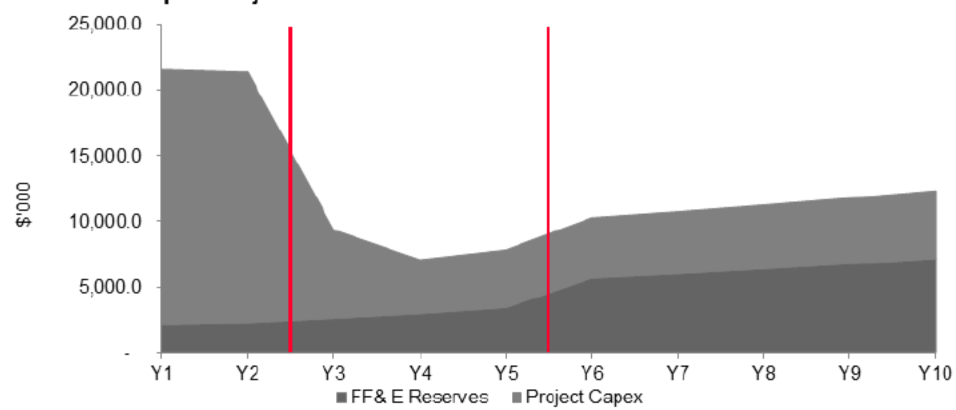
Project capex

In the immediate and medium term, the projections of project capex were based on five year forecasts prepared by PPM in July 2010.

- The projections allocate significant capex in the immediate two years following the transaction for specifically identified projects, totalling approximately $38.5 million project capex.
- Specifically identified projects continue to underlie the projections in the medium term, with a further $15.2 million allowed for project capex in the third to fifth years following the transaction.

In the longer term forecasts, project capex projections did not appear to include any specifically identified projects and were based on an allowance of 2.5% of total revenues for the years six to 10 after the transaction.

GS Model Capex Projections



3.5 Grant Samuel financial model assumptions - Capex projections

PPM were engaged to prepare capex projections in late 2008, and provided revised projections based on instructions to focus on essential capex rather than improve standards of accommodation to higher levels. The GS financial model capex projections in the short to medium term exceed the projections prepared by the physical due diligence consultant. Limiting capex assumptions to essential requirements only may not be consistent with increased occupancy assumptions as incorporated into the GS financial model.

PPM capital expenditure projections:

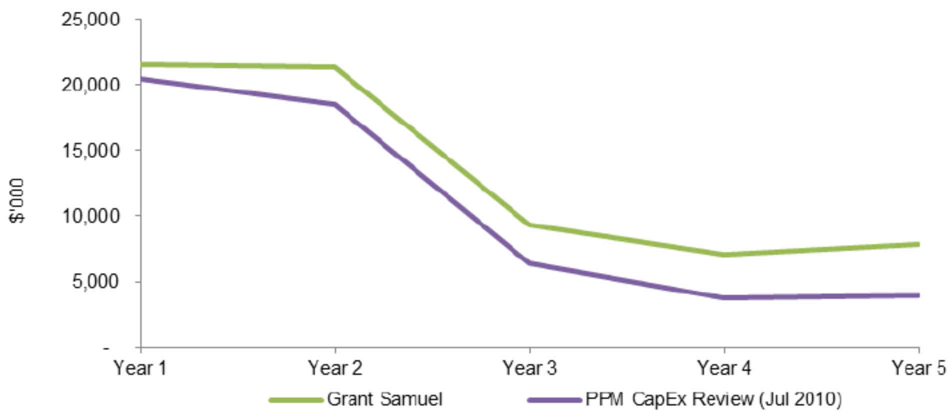
In late 2008, PPM were engaged to prepare capex projections based on the initial ARR Information Memorandum. PPM's initial projections totalled $77 million over five years and were revised to $69 million following on site review.

Further revisions to $53 million were made in July 2010, under instructions to *"focus on essential infrastructure and service tasks to ensure functionality and reliability of essential services throughout the complex"* , and not upgrading hotel rooms *"to higher levels of luxury or increased star levels"* (PPM July 2010, page 2).

$'000	Total	Year 1	Year 2	Year 3	Year 4	Year 5
PPM CapEx Review (Jul 2010)	53,053	20,506	18,550	6,342	3,753	3,902
PPM CapEx Review (Feb 2009)	68,928	33,280	19,247	6,075	5,376	4,950
PPM CapEx Review (Nov 2008)	76,630	28,250	22,260	12,190	7,890	6,040

Source: PPM, November 2008, Due Diligence Technical Review for THE GPT Group; PPM, February 2009, Post Due Diligence Review for RED ROCK PROJECT; and PPM, July 2010, Capital Expenditure Variance Review for RED ROCK PROJECT

Capex: PPM vs GS Financial Model



GS financial model short to medium term capex

Project capex for the first five years in the GS financial model was based on PPM's capex projections, and exceeds PPM projections over the first five years.

$'000	Total	Year 1	Year 2	Year 3	Year 4	Year 5
PPM CapEx Review (Jul 2010)	53,053	20,506	18,550	6,342	3,753	3,902
Grant Samuel Project Capex	53,739	19,412	19,106	6,728	4,101	4,392

Source: Planned Property Management, July 2010, Capital Expenditure Variance Review for RED ROCK PROJECT, and Grant Samuel ILC Financial Model_(21 Sep 10)_Sent to Banks_Final.xls

Differences between the PPM and GS capex projections were based on 3% p.a. inflation, and the following adjustments made in Year 1:

- removed $600K for contamination related capex to be provided by GPT; and
- reduced IT Capex by $463K for updated figures in August 2010.

As identified earlier, the Grant Samuel financial model also allowed for FF&E reserves at 2 % of total revenue, which is in addition to the project capex based on PPM's projections.

Accordingly, the GS financial model capex projections in the short to medium term exceed the projections prepared by the physical due diligence consultant.

However, we note the following in relation to our consideration of the capex projections:

- in email correspondence from a hotel industry expert due diligence consultant to the ILC with respect to the PPM capex projections, it was noted that they had been instructing David Wylie (PPM) to reduce projections, and that they were indicating the revisions were reaching a level where *"[David Wylie] could not put his name to it"*. Although, PPM did issue the revised report in July 2010; and
- capex based on essential requirements may not be consistent with increased occupancy assumptions as incorporated into the GS financial model, as discussed at page 32.

Capex projections over the long term were included in the GS financial model based on 5.5 % of revenue projections in years six to 10. In comparison to the capex projections in the Colliers and CBRE valuations, the capex projections included in the GS financial model appear conservative, allowing for greater levels of capex.

GS financial model long term capex

The GS financial model capex projections in years six to 10 were based on 5.5 % of revenue projections, including:

- FF&E reserves allowed at 3 % of revenues; and
- non-specific project capex allowed at 2.5 % of revenues.

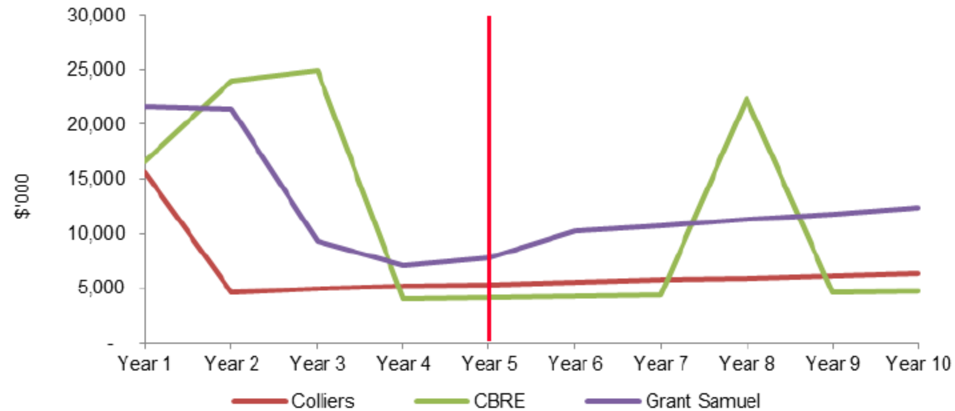
Similarly, the Colliers and CBRE valuations allowed for long term capex based on percentage of revenue allocations:

- Colliers allowed for capex at 4 % of revenues in Years six to 10; and
- CBRE allowed for capex at 3 % of revenues in Years six to 10, with an additional amount of $17 million project capex in year eight.

In comparison to the capex projections in the Colliers and CBRE valuations, the capex projections included in the GS financial model appear more conservative:

- GS projections exceed both Colliers and CBRE over a 10 year period;
- the GS financial model allows for ongoing capex between $10 million and $12 million per annum in the long term, whereas Colliers and CBRE allow between $4 million and $6 million; and
- although CBRE allows for $17 million additional project capex in year eight, the GS projections for years six to 10 exceed the CBRE projections by $16 million over the same period, and include $24.4 million project capex.

Capex: Grant Samuel vs CBRE and Colliers Capex Projections



$'000	Total	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10
Colliers	65,172	15,622	4,567	4,892	5,130	5,344	5,522	5,717	5,925	6,121	6,332
CBRE	113,895	16,545	23,966	24,907	4,024	4,153	4,266	4,383	22,284	4,624	4,743
Grant Samuel	123,518	21,580	21,383	9,337	7,065	7,811	10,273	10,729	11,237	11,770	12,333

Source: Colliers International, December 2008, Valuation Report Ayers Rock Resort; CBRE, 26 May 2009, A Valuation Report prepared for THE INDIGENOUS LAND CORPORATION AND NATIONAL AUSTRALIA BANK of Ayers Rock Resort; and Grant Samuel ILC Financial Model_(21 Sep 10)_Sent to Banks_Final.xls

3.5 Grant Samuel financial model assumptions - Capex projections

Capex projections included in the GS financial model appear consistent with the PPM projections and conservative (allowing for greater levels of capex in comparison to the Colliers Valuation and CBRE Valuation). However, it appears that the PPM capex projections reflected essential capex only, and may not have been at levels that would support the forecast growth in operating projections outlined in the GS financial model.

GS financial model capex projections and operating projections

As identified above, we note the following in respect of capex projections included in the GS financial model:

- immediate and medium term projections were based directly on projections prepared by independent physical due diligence consultants PPM; and
- long term projections exceeded the ongoing capex projections allowed for in the CBRE and Colliers valuations.

Capex projections prepared by PPM had initially been estimated at a total of $76.6 million over five years in November 2008, and were revised to $53.0 million over five years in July 2010. The revisions were based on a:

- $7.7 million reduction in estimated required capex to $68.9 over five years, following an on site review of facilities by PPM in February 2009; and
- further $15.9 million reduction in projected capex over five years, under instructions for PPM to reflect "*essential infrastructure and service tasks to ensure functionality and reliability of essential services throughout the complex*", and not upgrading hotel rooms "*to higher levels of luxury or increased star levels*" (PPM July 2010, page 2).

We also noted above that the ILC's hotel industry consultant assisting with due diligence stated in an email that he was seeking to reduce PPM's capex projections from the original estimates to a lower estimate.

As identified on page 32 the occupancy growth projected in the GS financial model may be considered optimistic given long term occupancy trends specific to the ARR prior to the transaction. As the PPM capex projections were reduced to reflect essential capex only, it is possible that the projected capex may not have been at levels required to support the forecast growth in operating projections.

Accordingly, it is arguable that a higher amount of capex would need to be factored into the GS financial model in the earlier years, to reflect more than "*essential infrastructure*", and to improve the standard of accommodation to *"higher levels of luxury or increased star levels"*, in order to assist in achieving the increased occupancy projections.

We note that factoring in additional capex at the levels originally estimated by PPM in November 2008 or February 2009 would reduce the GS financial model NPV of ARR cashflows by approximately $15 to $20 million.

NPV of ARR cashflows based on PPM capex November 2008

$' millions		Year 1	Year 2	Year 3	Year 4	Year 5
GS Model Capex		(19.4)	(19.1)	(6.7)	(4.1)	(4.4)
PPM Capex November 2008		(28.3)	(22.3)	(12.2)	(7.9)	(6.0)
Difference in Capex		**(8.8)**	**(3.2)**	**(5.5)**	**(3.8)**	**(1.6)**
Timing		0.50	1.50	2.50	3.50	4.50
Discount Factor		0.95477	0.87034	0.79338	0.72323	0.65928
Net impact on NPV	**(19.3)**	**(8.4)**	**(2.7)**	**(4.3)**	**(2.7)**	**(1.1)**
GS Model NPV	292.3					
Adjusted NPV	**273.0**					

Source: McGrathNicol

NPV of ARR cashflows based on PPM capex March 2009

$' millions		Year 1	Year 2	Year 3	Year 4	Year 5
GS Model Capex		(19.4)	(19.1)	(6.7)	(4.1)	(4.4)
PPM Capex March 2009		(33.3)	(19.2)	(6.1)	(5.4)	(5.0)
Difference in Capex		**(13.9)**	**(0.1)**	**0.7**	**(1.3)**	**(0.6)**
Timing		0.50	1.50	2.50	3.50	4.50
Discount Factor		0.95477	0.87034	0.79338	0.72323	0.65928
Net impact on NPV	**(14.1)**	**(13.2)**	**(0.1)**	**0.5**	**(0.9)**	**(0.4)**
GS Model NPV	292.3					
Adjusted NPV	278.2					

Source: McGrathNicol

It does not appear that GS presented the ILC Board with any sensitivity analysis with respect to the NPV calculation in the GS financial model prior to entering into the transaction in October 2010. In November 2010 GS did provide the ILC with two sensitivity scenarios in the GS financial model, which did not extend to highlighting the impact on the calculation of the NPV. The NPV calculation would have been reduced to between $237 million and $274 million based on the sensitivity scenarios.

GS financial model sensitivity analysis

As discussed on page 28 above, it does not appear that GS presented the ILC Board with clear sensitivity analysis with respect to the NPV calculation in the Grant Samuel financial model prior to entering into the transaction.

However, GS provided the ILC with two sensitivity scenarios to assist in responding to Minister Wong's request for sensitivity analysis on 8 November 2010. The two scenarios prepared by GS included the impact on the refinancing requirement in Year five after the transaction based on:

- Scenario 1 – Growth on ARR EBITDA is limited to 3 % p.a.;
  - Scenario 1 A – Based on reducing projected occupancy rates; and
  - Scenario 1 B – Based on reducing projected Average Daily Rates ("ADR");
- Scenario 2 – Assuming a 5 % reduction in:
  - Scenario 2 A – occupancy rates; and
  - Scenario 2 B – ADR.

Although the above sensitivity analysis to the financial model was presented to the ILC, it did not extend to highlighting the impact on ARR cash flows, nor the calculation of the NPV.

In comparison to the GS NPV of ARR cash flows presented to the ILC Board (calculated as $292 million), the GS NPV calculation would have been reduced to between $237 million and $274 million based on the less favorable trading conditions set out in the above sensitivity scenarios:

- Scenario 1 A – $273.6 million;
- Scenario 1 B – $273.3 million;
- Scenario 2 A – $236.8 million; and
- Scenario 2 B – $271.4 million.

Summary of Grant Samuel Sensitivity Scenario Impacts on NPV $'millions

GS Original model		Yr 1	Yr 2	Yr 3	Yr 4	Yr 5	Yr 6	Yr 7	Yr 8	Yr 9	Yr 10
Occupancy %		53%	53%	56%	59%	65%	67%	67%	67%	67%	67%
ADR $		256	262	280	297	307	317	327	336	347	357
NPV	**292.3**	**(8.2)**	**(3.7)**	**9.5**	**13.9**	**16.2**	**16.2**	**15.4**	**14.4**	**13.4**	**205.2**

Scenario 1A		Yr 1	Yr 2	Yr 3	Yr 4	Yr 5	Yr 6	Yr 7	Yr 8	Yr 9	Yr 10
Occupancy %		52%	52%	55%	58%	64%	66%	66%	66%	66%	66%
S1A NPV	**273.6**	**(9.0)**	**(4.6)**	**8.6**	**12.9**	**15.2**	**15.4**	**14.6**	**13.6**	**12.7**	**194.2**

Scenario 1B		Yr 1	Yr 2	Yr 3	Yr 4	Yr 5	Yr 6	Yr 7	Yr 8	Yr 9	Yr 10
ADR $		245	250	267	283	293	303	312	321	331	341
S1B NPV	**273.3**	**(9.0)**	**(4.6)**	**8.6**	**12.9**	**15.2**	**15.4**	**14.5**	**13.6**	**12.7**	**194.0**

Scenario 2A		Yr 1	Yr 2	Yr 3	Yr 4	Yr 5	Yr 6	Yr 7	Yr 8	Yr 9	Yr 10
Occupancy %		51%	50%	53%	56%	62%	64%	64%	64%	64%	64%
S2A NPV	**236.8**	**(10.6)**	**(6.4)**	**6.8**	**11.1**	**13.4**	**13.7**	**12.9**	**12.1**	**11.3**	**172.5**

Scenario 2B		Yr 1	Yr 2	Yr 3	Yr 4	Yr 5	Yr 6	Yr 7	Yr 8	Yr 9	Yr 10
ADR $		243	249	266	282	292	301	310	320	329	339
S2A NPV	**271.4**	**(9.1)**	**(4.7)**	**8.5**	**12.8**	**15.1**	**15.3**	**14.5**	**13.5**	**12.6**	**192.8**

Source: McGrathNicol, based on Grant Samuel ILC Financial Model_(21 Sep 10)_Sent to Banks_Final.xls and Sensitivity Scenarios included in ILC Financial Model_(20 Oct 10)_Sensitivities Analysis.xls

As stated in GS's 1 October 2010 presentation to the ILC Board, the NPV of ARR cashflows was based on a WACC of 9.7%. The methodology for the WACC calculation used to determine the NPV based on the GS financial model appears to be have been applied appropriately. The assumptions underlying GS's WACC calculations appear consistent with, or more conservative than, the discount rates used by the independent valuers, and the Voyages Board of Directors.

GS financial model discount rate

As stated in the GS 1 October 2010 presentation to the ILC Board, the NPV of ARR cashflows was based on a WACC of 9.7%.

WACC is a method for calculating the discount rate to determine the present value of future cashflows. The key components of WACC include:

- cost of debt ("Kd") – interest rate payable on debt finance; and
- cost of equity ("Ke") – rate of return expected on invested equity, based on:
  - risk free interest rate ("Rf") – Government bond rates are typically accepted as a proxy for the Rf;
  - market risk premium ("Rm") – expected market rate of return in addition to the Rf. Typically accepted between an additional 6 to 8 %; and
  - Beta ("β") – the rate of correlation to the Rm. Determining an appropriate β is subjective, and typically based on comparable transactions.

GS financial model WACC

The October 2010 version of the GS financial model (*ILC Financial Model_(20 Oct 10)_Sensitivities Analysis.xls*) includes the basis for the calculation of the 9.7% WACC:

- Kd = 4.34%– 6.5% interest rate after tax;
- Ke = 11.96%– based on:
  - Rf = 5.06%– 10 Year Government Bond Rate 29 September 2010;
  - β = 1.15 – the model did not state the basis for the assumed β; and
  - Rm = 6.06%.

Although the basis for the Beta applied was not explained in the GS financial model, it is difficult to identify a directly comparable listed company or transaction with an available Beta to use as a basis for determining an appropriate Beta. However, the methodology for the calculation of the WACC used to determine the NPV based on the GS financial model appears to be have been applied appropriately.

Comparison to other valuation discount rates

The discount rates used in other DCF valuations of the ARR include:

- 12% – Colliers Valuation (December 2008);
- 11.75%– CBRE Valuation (May 2009) ; and
- 13%– Voyages Director's Valuation (June 2013).

Each of the above discount rates were used to determine the value of the ARR based on projected EBITDA, which excludes interest and tax payments. Accordingly, the above discount rates are not equivalent to a WACC.

Although not directly comparable, we note the cost of equity (Ke = 11.96 %) underlying the GS WACC is in line with the above discount rates.

For a direct comparison, the cost of equity would need to be grossed up to take into account the impact of excluding tax payments from the cash flows, resulting in a higher rate. Accordingly, the cost of equity underlying the WACC applied by GS appears consistent with, or more conservative than, the discount rates used by the independent valuers and the Voyages Board of Directors.

GS provided advice to the ILC in respect of the negotiation of the transaction price. Negotiations with GPT for the purchase of the ARR extended from late 2008 to September 2010. Whilst it appears that the ILC was the only interested purchaser of the ARR, and that GPT was a motivated seller, GPT was not prepared to sell at any price, apparently seeking a headline sale price of $300 million. Despite some Board opposition, the ILC appears to have been a motivated purchaser. Documentation indicates that the ILC considered valuation advice and attempted to negotiate the transaction price with GPT (but not with the benefit of having updated the CBRE valuation).

Negotiation of net purchase price

As illustrated in Section 2.2 of this report, the final net purchase price was $292 million. However, interpreting the actual price paid at the date of acquisition is not straight forward. This is because the final transaction price is based on a series of payments to GPT subject to vendor finance, allowances for capital expenditure over the five years following the acquisition, and a capital uplift based on the valuation of the ARR 5 years following the acquisition.

We are advised by GS that the transaction structure was designed to provide GPT with a headline number of $300 million, and the ILC with an effective transaction price that was closer to $270 million, and this motivated the respective parties in their negotiations.

In its role as lead advisor, GS provided advice to the ILC in respect of the negotiation of the transaction price, and was directly involved in conducting negotiations with GPT.

In assessing whether the ILC (with assistance of GS) negotiated the best possible transaction price and transaction structure, we have considered the following:

- Did the ILC consider if GPT was an anxious seller, and if so, did the ILC's negotiation strategy attempt to exploit this?
- Did the ILC obtain and utilise advice regarding the valuation of the ARR in its negotiation strategy?
- Did the ILC consider the likely level of other interest in the purchase of the ARR, and was this reflected in its negotiation strategy?
- Is there evidence of robust negotiation concerning the transaction price and structure?
- Did the ILC attempt to make use of all relevant information, and advice of consultants in negotiating the transaction price?
- Was the ILC an anxious buyer, prepared to enter into the transaction irrespective of the transaction price?

Negotiation consideration	ILC negotiation strategy
Was GPT an anxious seller?	In an email dated 24 October 2008 to a group including Director Baffsky and the ILC General Manager, GS advised that it considered GPT likely to be forced sellers. However, in November 2009, GPT was prepared to withdraw from negotiations with the ILC. It appears that GPT was a motivated seller, but only for the right price. GS advised McGrathNicol that their view was that GPT required a headline price of $300 million.
Did ILC obtain and utilise valuation advice?	ILC was provided with a full speaking valuation from CBRE and GS conducted NPV modelling throughout the negotiation process.
Was ILC the only interested purchaser?	Given the length of time the ARR was on the market, and the time GPT allowed for the ILC to conduct its due diligence, it is reasonable to assume that the ILC was the only interested purchaser. GS advised McGrathNicol that the ILC was aware of this, but the view was that whilst the ILC was not negotiating against other interested parties, they were negotiating against GPT not selling the ARR. Though it is noted that Director Baffsky advised his view was that other selling parties may have been interested in various assets associated with GPT and the ARR.
Is there evidence of robust negotiation?	ILC commenced negotiating with GPT in late 2008, and negotiations were not concluded until September 2010. Accordingly, it is considered that there is evidence that the ILC pursued robust negotiations.
Did the ILC make use of all available information?	Upon receiving advice from Horwath that the ARR's first half 2010 performance was below forecast, the ILC sought to renegotiate the transaction price (notwithstanding that they did not seek to update the CBRE valuation, as discussed on page 26). Other advice from GS and other consultants was followed by the Board. Accordingly, it is considered that there is evidence that the ILC attempted to negotiate the purchase price.
Was the ILC an anxious buyer?	The fact that the ILC pursued the transaction for over 2 years indicates it had a strong interest in purchasing the ARR. Also, Board minutes indicate that certain Board members were strongly supportive of the transaction. It is reasonable to conclude that the ILC was a very motivated purchaser, but the length of the negotiation period and the ILC's rejection of various offers GPT put to the ILC indicate that it was not prepared to purchase the ARR at any price.

The ILC agreed to provide WU with 7% equity in the ARR upon the earlier of repayment of all loans and ILC monies or ten years, in return for WU not exercising its first right of refusal with GPT to purchase the ARR assets. WU had no capacity to purchase the ARR on its own and there appeared to be no other parties interested in purchasing the ARR. Accordingly, the first right of refusal was of little or no value. The equity provided to WU is significant, and appears to have been granted in order to obtain the support of an organisation with links to the local Indigenous community. This relationship is difficult to value and there is limited documented evidence of the negotiations.

Wana Ungkunytja

WU is an Aboriginal corporation representing communities around Uluru. WU was formed in 1993 as the business arm of the Nyangatjatjara Aboriginal Corporation. WU operates Anangu Tourism based at Uluru. WU was represented on the Board of the ARR from 1993 to 1997, the ARR Management Voyages Board from 1997 to 2000, and the GPT / WU Advisory Board from 2003 through to the date of the transaction.

In 1997, WU signed a deed and first right of refusal with GPT to purchase the ARR assets. The first right of refusal allowed WU to match any "concrete offer" from another party for the ARR, if it could raise funds to match the offer by itself or in a joint venture with another entity (in which WU holds at least 20% equity). As WU did not have the capacity to undertake the transaction on its own, it approached the ILC to form a consortium to purchase the ARR.

Draft 2008 agreement

In late 2008, an agreement was drafted for the ILC and WU to work together in respect of the acquisition of the ARR. However, this agreement was not signed by the ILC. The draft agreement proposed that in return for WU foregoing its first right of refusal, it would be provided with an immediate equity stake in the ARR entity of 3%, and a further 17% equity in the ARR entity once income equivalent to the ILC's capital investment has been earned.

Final agreement for an equity allocation to WU

The ILC Board meeting minutes of 1 October 2010 record that the ILC Board resolved to enter into the following arrangements in relation to WU's participation in the purchase of the ARR:

+ Reimbursement of up to $100,000 in legal and consultant costs incurred by WU since 2008 and payment of $200,000 to WU on settlement of ARR in consideration of WU either foregoing or not exercising its first right of refusal;
+ Granting of 7% equity in ILC tourism after the earlier of all loans and ILC monies having been repaid, or ten years following the date of the sale agreement;
+ Two WU directors to sit on the Voyages Board, but with only one vote; and
+ Anangu tours continuing to be operated by WU at ARR, with an ILC commitment to supporting the promotion of Anangu Tours.

This agreement was entered into on 17 May 2011.

Justification for the equity allocation to WU

The SLA Proposal (dated 1 October 2010) recommended that the Board enter into the agreement with WU as detailed above. The SLA Proposal stated that "*the General Manager believes that the above proposal will benefit the ILC in dealing with Traditional Owners of Uluru, as well as its dealings with the surrounding Indigenous communities. WU is keen to have a strong working relationship with the ILC, and they will be integral to promoting local Indigenous employment at ARR*".

Negotiation of the agreement with WU

WU advised the ILC that they valued the first right of refusal at $10 million. Accordingly, ILC initially proposed a 3% equity allocation to WU. This was rejected by WU on the basis that they would not receive the equity interest for 10 years, and by this time $10 million invested in a bank would be worth approximately $17 million. Further, WU advised that they sought an equity interest of 20%, because they believed a 20% interest in a entity or joint venture was a requirement of the first right of refusal offer. ILC countered with an offer of 7% equity which was accepted by WU.

Reasonableness of the equity agreement with WU

WU had no ability to acquire the ARR on its own. Also, there did not appear to be any other interested parties at the time the initial agreement with WU was entered into, nor by the time the final agreement was entered into in October 2010. Accordingly, the first right of refusal is considered to have little or no value.

The equity provided to WU is significant, and appears to have been granted in order to obtain the support of an organisation with links to the local Indigenous community. This relationship is difficult to value (albeit important to the operation of ARR) and there is limited documented evidence of the negotiations. Accordingly, from the information available, we are not able to conclude whether this negotiation was conducted in the best interest of the ILC. To conclude on this, discussions would need to be held with the ILC representative who negotiated the agreement , the former ILC General Manager.

ANZ Bank provided a $60 million facility to assist with the capital expenditure requirements of the ARR and to partly fund a vendor financing instalment payment. We have reviewed whether the loan arrangements negotiated with the ANZ are appropriate and were undertaken at arm's length.

Scope

Were the loan arrangements negotiated with the ANZ appropriate and undertaken at arm's length?

Process undertaken

In approaching this scope point we undertook the following steps:

- reviewed the terms and conditions of the loan arrangements with ANZ; and
- considered whether the ANZ facility's terms and conditions are reflective of a typical market transaction.

Background

The ILC initially put its ARR acquisition financing requirements to the ANZ, nab, Westpac and Commonwealth Bank of Australia ("CBA") in the first half of the 2009 calendar year. The ILC requested letters of offer for a $200 million debt facility (reflecting an 80% loan to value ratio ("LVR") for a $250 million purchase price, an offer which was not ultimately put to GPT).

Of the four banks, the following responses were received:

- CBA declined the opportunity to provide funds;
- nab informally declined the opportunity, but indicated it would be willing to consider a lower LVR of circa 40%;
- ANZ did not appear make a formal loan offer; and
- Westpac made an informal and highly conditional offer of $250 million, which comprised $210 million to assist with acquisition, $30 million capex uplift, and a further $10 million in contingent limits. At this time, the ILC had requested from the Australian Government a change in legislation to guarantee annual payments to ILC from the Land Account of a minimum of $45 million. The Westpac offer was contingent on this change of legislation.

2010 loan tender process

In July 2010, at the time the ARR acquisition due diligence had been reinvigorated, GS and ILC jointly conducted another tender process with the four banks, seeking a five year $60 million cash advance facility to fund capital expenditure for the ARR, and to assist with making part payment of the purchase price.

Credit offers were received from ANZ, nab and Westpac. CBA did not receive credit approval and therefore did not submit an offer.

GS prepared for the ILC Board a Debt Facility Update, dated September 2010, which provided a summary of the offers received and a recommendation for the preferred bank to provide funding. We provide the following summary of the three offers received:

Comparison of offers received for $60 million cash advance facility

Bank	Margin over bank bill rate offered	Other comments
ANZ	*0.80%*	Interest only facility. Did not require covenant reporting.
nab	*1.38%*	Non complying as nab internal legal approval had not been obtained. Mortgage security requirement not outlined in the paper.
Westpac	*1.80%*	Offer was subject to financial covenants, cash cover requirements and amortisation. Mortgage security requirements not outlined in the paper.
CBA	*n/a*	CBA did not submit an offer

ANZ's offer to provide a $60 million facility was accepted on 15 December 2010. We have set out on the next page a table which details the terms, conditions and interest rates offered by ANZ.

Conclusion- 2010 loan tender process

McGrathNicol considers that the loan arrangements with the ANZ were conducted at arm's length, and resulted from a competitive process in which other banks were invited to participate.

The terms and conditions of the facility are consistent with those that would reasonably be expected by a bank providing a secured credit facility, and are not considered inappropriate or excessive. The interest rate margins offered by ANZ are considered to be competitive. when compared to the offers made by the other competing banks as well as prevailing market conditions.

4.1 ANZ debt financing arrangements

The below table sets out the terms, conditions and interest rates offered by ANZ in relation to the $60 million facility. The facility was offered as a result of an arm's length competitive process in which others banks were invited to participate. The terms and conditions of the facility appear reasonable, and interest rate pricing is considered competitive when compared to the offers made by the other competing banks as well as prevailing market conditions.

ANZ Facility Terms and Conditions Analysis

Detail		McGrathNicol comments
Borrower	ILC Tourism Pty Limited	-
Guarantor	Indigenous Land Corporation	-
Loan amount	AU$60 million	-
Purpose	Funding capital expenditure for ARR, and to assist in making part payment of the first deferred vendor finance instalment of $81 million (a.k.a "One Year Instalment Balance Owing").	-
Term	5 years	To coincide with bullet payment due to GPT 5 years post settlement.
Interest	ANZ Bank Bill Rate (linked to the Bank Bill Swap Rate) plus 0.8% margin	This appears to be an attractive margin and likely reflects the low loan-to-value ratio. This conclusion has been formed with reference to average spreads over swap rates (103 basis points) and spreads over bonds issued by Australian Government (151 basis points) as at June 2010[Note 1], around the time that the finance was negotiated.
Key Conditions precedent	1. Draw downs in relation to the First Year instalment are subject to satisfactory evidence that the ILC will have sufficient funds to meet the remaining balance of the First Year instalment on the due date. 2. Several legal opinions to be sought at borrower cost in relation to loan facility documentation. 3. Legal opinion regarding ILC's capacity to enter into a guarantee.	The Conditions Precedent to funding appear straightforward and standard for a transaction of this size and nature.
Security	1. Fixed and Floating Charge over ILC Tourism 2. Registered Mortgage over ARR 3. Mortgage over lease (Ayers Rock (Conellan) Airport) 4. Mortgage over lease (Sydney office space) 5. Guarantee by ILC supported by equitable mortgage of shares	The Security requirements for a loan of this nature appear straightforward and standard for a lending transaction of this nature.

Note 1: http://www.rba.gov.au/statistics/tables/pdf/f03hist.pdf?accessed=2013-09-26-14-21-24

McGrathNicol has undertaken an assessment of the appropriateness and commerciality of the vendor financing arrangements negotiated with GPT. GPT and ILC agreed upon a net purchase price of $292 million, which was payable to GPT via installment payments totalling $300 million, and a guaranteed valuation uplift payment of $17 million due to GPT after five years. Offsetting these amounts was a $25 million capital expenditure allowance for ILC, in recognition of the ARR's intensive capital upgrade requirements.

Scope

Were the loan arrangements negotiated with the vendor appropriate and undertaken at arm's length?

Process undertaken

In approaching this scope point we undertook the following steps:

+ reviewed the terms and conditions of the vendor financing arrangements with GPT; and
+ reviewed the extent to which the terms and conditions were reflective of a typical market transaction.

Vendor financing arrangements

As outlined in Section 4.2 of this report, the ILC experienced difficulties in obtaining term finance for the ARR purchase from the Big Four banks. In light of this, and to assist in continuing the transaction, GPT and ILC agreed to explore other options to finance the ILC's purchase of the ARR.

The initial financial structure agreed between ILC and GPT involved a purchase price of circa $300 million, of which approximately 54% would be paid upon settlement, and the remaining 46% would be covered by five-year convertible preference shares, in effect a put option which ILC could choose to exercise after five years.

However, we are advised by the ILC COO that ILC received legal advice that the ATSI Act prohibited the issuance of securities. We understand that this led to GPT and ILC moving negotiations to a vendor financing structure.

This revised purchase arrangements involved a net purchase price of $292 million, structured as follows:

+ the payment of a series of installments totalling $300 million over a period of five years; plus
+ a valuation uplift payment of up to 46% of total ARR valuation increase after five years (guaranteed at no less than $17 million); less
+ a $25 million capital expenditure allowance for the ILC's benefit (in recognition of the intensive capital upgrade requirements of the ARR).

The interest rate negotiated on the deferred installments was 6.5%. However, through the introduction of the guaranteed valuation uplift payment of $17 million, the effective interest rate was increased to 8.5% p.a. The 8.5% effective interest rate was required by GPT to align with the original convertible preference shares arrangement, and in recognition of the inherent risks of providing vendor financing.

The details of this structure are set out in the table on the next page of this report.

Set out below is a summary of the vendor financing arrangements accepted by the ILC and its subsidiary Voyages. McGrathNicol does not consider that the payment structure of the vendor financing arrangements was unreasonable. The 8.5% p.a. effective interest rate does not appear to be excessive given GPT's subordinated security position, and the prevailing market interest rates at the time of the transaction. On page 46 of this report we have reviewed the extent to which ARR borrowings complied with the ATSI Act, in particular the borrowing limits set out under this legislation.

Vendor finance analysis

Vendor finance technical details		Comments
Counterparty	ILC Tourism Pty Limited	
Payment structure	Deposit $13,500,000 Completion payment: $67,500,000 First Year payment: $81,000,000 Five Year payment: $138,000,000 **Subtotal: $300,000,000** *Less:* $25 million capital expenditure allowance payable to ILC *Plus:* Valuation uplift payment to GPT of at least $17 million after five years **Total: $292,000,000**	The deferred consideration arrangements were offered by GPT to the ILC in light of the finding that, per the requirements of the ATSI Act, ILC was not legally able to issue the five-year convertible preference shares originally agreed between GPT and ILC Tourism. The $25 million capital expenditure allowance was negotiated in acknowledgement of the extensive capital uprades required to the ARR. The minimum $17 million guaranteed valuation uplift payment due to GPT after five years was negotiated in recognition of the risks involved in vendor financing. While $17 million is the minimum valuation uplift payment, GPT is entitled to a payment equal to 46% of of the total valuation uplift. We have undertaken our interest rate analysis based on the minimum guaranteed amount as a base case scenario.
Term	5 years	Final deferred payment due within five years of completion.
Interest rate	6.5% simple interest calculated daily and charged quarterly in arrears. The effective interest rate of this arrangement is 8.5% based on the guaranteed uplift payment of $17 million payable by the ILC.	The weighted average rate of credit outstanding for large business in September 2010 was 6.55% p.a.[Note 1] The higher effective rate of 8.5% p.a. reflects the subordinated security position accepted by GPT.
Security	1. Mortgage over ARR 2. Fixed and Floating charge over ILC subsidiary 3. Mortgage over airport lease 4. Mortgage over Sydney office space lease	The mortgage security provided to GPT is subordinated to the ANZ's security position.

Note 1: RBA Indicator Reference Rates, <www.rba.gov.au>, accessed 12 November 2013

Conclusion - Vendor Financing

As set out in the table contained on the preceding page, the vendor financing structure was entered into due to the difficulties experienced by the ILC in sourcing external bank financing.

McGrathNicol does not consider that the payment structure of the vendor financing arrangements was unreasonable. The 8.5% p.a. effective interest rate does not appear to be excessive given GPT's subordinated security position, and the prevailing market interest rates at the time of the transaction.

Whilst a vendor financing arrangement can never be conducted at arm's length, McGrathNicol has identified no evidence to support that the ILC accepted an arrangement that is uncompetitive or disadvantageous. On Page 46 of this report, we have reviewed the extent to which ARR borrowings complied with the ATSI Act, particularly the borrowing limits set out under this legislation.

Section 193M of the ATSI Act sets out that the ILC is subject to a borrowing and guarantee limit, reviewed on an annual basis. ILC sought advice from Corrs Chambers Westgarth and the Australian National Audit Office ("ANAO") regarding whether its proposed borrowing arrangements would meet legislative requirements. It appears that the vendor financing and ANZ lending arrangements entered into do not exceed the ILC's borrowing and guarantee limits.

Legislative requirements

Section 193M of the ATSI Act sets out that the ILC is subject to a borrowing and guarantee limit, reviewed on an annual basis.

The ILC's borrowings prior to the ARR acquisition were minimal, and the ILC Board and Management were conscious that the borrowings required to complete the ARR purchase would almost exhaust their borrowing and guarantee limit. It was therefore important that the ILC considered whether or not entering into the vendor financing and ANZ facilities would result in a breach of the ATSI Act.

Expert advice sought

ILC sought legal advice from Corrs Chambers Westgarth ("Corrs") in April 2011 in relation to the ability of ILC and its subsidiaries to enter into lending arrangements.

Corrs' advice confirmed that the ILC was permitted to borrow funds, and was also permitted to lend money to its subsidiaries. However, the scope of advice did not address whether the proposed vendor finance and ANZ lending facility would breach the ILC's Lending and Guarantee limits.

The ANAO performed agreed upon procedures in May 2011, assessing whether the borrowings and guarantees entered into exceeded the borrowing and guarantee limits of ILC (confirmed at $300,936,439 by ANAO).

ANAO concluded that the total borrowings and guarantees of the ILC and its subsidiaries did not exceed the borrowing limits applicable at the time. McGrathNicol notes that this advice was received over five months after entering into the ARR contract of sale and lending facility agreement.

Conclusion

Based on the advice received from Corrs in April 2011, and the ANAO agreed upon procedures in May 2011, it appears that the vendor financing and ANZ lending arrangements entered into did not exceed the ILC's borrowing and guarantee limits as prescribed by section 193M of the ATSI Act.

McGrathNicol notes that the ANAO advice was received in May 2011, more than five months after the ARR acquisition contract of sale and lending agreements were entered into. It is considered that seeking this advice prior to entering into a contract of sale would have been prudent, given the constraints on ILC cash in respect of applying it to the ARR acquisition.

McGrathNicol has examined whether the risk strategies adopted to mitigate the ARR acquisition risks identified were appropriate. In doing so, we have reviewed external advice received, analysed the quality of the ILC's Project Risk Management Plan prepared and reviewed risk assessment advice provided to the Board.

Scope

Were the risk strategies adopted to mitigate the risks identified at the time of the purchase appropriate.

Process conducted

In determining whether the ARR risk assessment process was adequate, we undertook the following processes:

- reviewed external due diligence advice provided by Horwath on 10 August 2010;
- Reviewed ILC document entitled "Phase 1: Acquisition Risk Identification and Treatment (Red Rock)" ("Phase 1 Risk Assessment Document" (undated);
- reviewed Risk Assessment contained at section 9.2 of the Strategic Land Acquisition Proposal of 1 October 2010 ("SLA Proposal Risk Assessment");
- reviewed the ILC's 2010 "Risk Management Framework and Corporate Risk Management Plan", dated July 2010.

ILC Risk Rating Matrix

Risk rating		Definition
Low		Controlled by standard procedures.
Moderate		Should be managed by specific monitoring procedures
High		Requires attention from corporate management - a treatment plan is required
Extreme		Demands immediate action in conjunction with corporate management - a treatment plan is required

Source: ILC risk rating matrix

ARR transaction risk assessment

As part of the ARR acquisition due diligence process, the Phase 1 Risk Assessment Document was prepared by the ILC. In accordance with the ILC's risk framework, assessment of each risk incorporated consideration of the:

- likelihood; and
- consequence of the project risks, rated in accordance with the ILC risk matrix.

Risks were rated in accordance with the ILC's risk matrix per the table set out across the page:

ARR transaction risk assessment- continued

For each risk identified, the ILC rate the risk in accordance with the risks contained in the table above. In accordance with the ILC's risk framework in place at the time, a treatment plan was required for all extreme and high risks.

The ILC's Phase 1 Risk Assessment formed the basis of the SLA Proposal Risk Assessment. This was the final transactional risk assessment submission provided to the Board on 1 October 2010 in its consideration of whether or not to proceed with the purchase of the ARR.

The SLA Proposal Risk Assessment appears to have substantially incorporated external advice received from a number of external consultants involved in the acquisition due diligence process. We particularly highlight the inclusion of the SWOT analysis prepared by Horwath that formed part of its wider due diligence advice.

One of the key documents prepared by the ILC and presented to the Board at the meeting of 1 October 2010 was the SLA Proposal, which included a SWOT analysis and risk assessment. The SWOT analysis and risk assessment documentation appear to have substantially incorporated external advice received from a number of external consultants involved in the acquisition due diligence process, particularly the SWOT analysis prepared by Horwath as part of its wider due diligence advice.

Horwath Due Diligence

Horwath was engaged by the ILC on 16 July 2010 to provide purchaser due diligence financial advice. The ARR acquisition SWOT analysis set out in their report to the ILC (dated 10 August 2010) identified a number of weaknesses and threats to the financial performance of the ARR that were able to be considered by the ILC in developing the Project Risk Management Plan.

Based on the SWOT analysis, Horwath identified five key issues in respect of the ILC's acquisition of the ARR. The five key issues identified by Horwath were:

- recent downturn in trading;
- long term revenue in a trend of decline;
- risk of Virgin Blue reducing services / raising prices;
- future capital expenditure issues; and
- closure of the Uluru climb.

For each of these key issues, Horwath detailed the nature of the issue in depth, and the risks applicable to the acquisition of the ARR.

As noted, many of the threats and weaknesses identified in the Horwath SWOT analysis appear to have been used as the basis for the ILC's Project Risk Management Plan.

SLA Proposal Risk Assessment

As previously indicated, one of the key documents prepared by the ILC and presented to the Board at the meeting of 1 October 2010 was the SLA Proposal.

In accordance with the risk assessment provided in the SLA Proposal, the ILC identified nine risks that had a pre-treatment risk rating of Extreme or High. In the Strategic Land Acquisition Proposal, all of the nine risks given a pre treatment rating of Extreme or High were reduced to either Medium or Low following the application of risk treatments.

SLA Proposal Risk Assessment- risks identified

The SLA Proposal includes (at Section 9) a SWOT and risk assessment. The SWOT analysis is a copy of the Horwath SWOT analysis contained in their August 2010 report. The table below details for each of the extreme and high risks identified in respect of the ARR acquisition:

- the pre treatment risk rating;
- the mitigation strategies identified by the ILC to manage these extreme and high risks;
- the post risk treatment rating; and
- our comments on the reasonableness of the risk mitigation strategies, and the accompanying reduction in the risk ratings.

ARR acquisition risk assessment provided to the ILC Board

Risk	ILC Pre-treatment risk rating	Risk treatments	ILC Post-treatment risk rating	McN comments
Purchase price paid for the ARR over the five year period is not commensurate with the value	Extreme	+ Due diligence conducted by professional consultants + Full speaking valuation (CBRE) + 10 year financial forecast developed	Moderate	Due diligence was undertaken and 10 year financial forecasts were prepared. The other risk treatment, to obtain a full speaking valuation, was sound in reasoning. However, a valuation prepared 17 months earlier was used, and may have been out of date at the time the transaction was entered into. Accordingly, the actual treatment undertaken by the ILC is regarded as unsatisfactory.
ILC is not able/eligible to obtain certification and authorisation requirements to operate the airport	Extreme	+ Obtain certification as a precondition of sale. + Obtain Ministerial approval + Achieve public liability insurance requirements + Engage Aspiron to update manuals	Moderate	Risk treatments and post risk rating are regarded as reasonable.
Decision/acquisition not supported by Sector/ Government	High	+ garner ministerial support + engage other agencies in collaborative arrangements + development of a thorough project plan for operations and intended outcomes at ARR	Moderate	The moderate post treatment rating is based on an "unlkely" likelihood of this risk transpiring. Given the high level of concern identified by the Government in letters provided to the ILC in the days before the 1 October 2010 Board meeting, a likelihood rating of "possible" or "lkely" appears to be more appropriate. It is noted that a higher likelihood rating would result in a post treatment risk rating of high. Accordingly, the post treatment risk rating is regarded as unsatisfactory.
Unable to change the focus of ARR following acquisition to achieve Indigenous training and employment outcomes.	High	+ Mitigation strategies outlined include utilising relationships with WU and relevant Indigenous schools, securing Government funding and developing support from key suppliers.	Moderate	Risk treatments and post risk ratings are regarded as reasonable.
Remoteness of ARR means visitor levels heavily dependent upon external parties (including QANTAS and Virgin)	High	+ Establish strong relationships with service providers + Develop marketing strategy with strong linkages to travel companies and tourism authorities + Meet with QANTAS and Virgin prior to contract exchange to establish ongoing support + Secure Voyages operating platform and travel agency	Moderate	The proposed risk treatments are regarded as reasonable. However, it is questionable whether these treatments are sufficient to reduce the risk rating from High to Medium. To a significant extent, the ARR will always have a reliance on the airline companies and limited ability to influence the number of flights to Ayers Rock Airport. Accordingly, the post treatment rating for this risk should have been "High", and the ILC Board should have then considered whether it was appropriate to proceed given this post treatment high risk.

This table is continued over-

ILC Strategic Land Acquisition Proposal Risk Assessment, 1 October 2010

ARR acquisition risk assessment provided to the ILC Board- continued

Risk	ILC Pre-treatment risk rating	Risk treatments	ILC Post-treatment risk rating	McN comments
Deferral of capital expenditure during recent years indicates that this expenditure will be required in the short / medium term to maintain standard at an appropriate level.	Extreme	+ Ensure financial viability analysis includes the costs to undertake this work + ensure acquisition price reflects work to be done, or GPT capex contr bution + Develop capex program for the first five years	Moderate	The financial analysis of the ARR projected capex in the first five years is consistent with the independent expert assessment. These capex forecasts were based on "essential capex" only, to maintain the standard of the ARR. However, we note that this does not appear consistent with the optimistic operating forecasts discussed on page 36 of this report.
Environmental issues identified involve significant expenditure to rectify.	High	+ Renegotiate subleases to include environmental responsibilities and compliance with laws + Engage environmental due diligence consultants + Resolve indemnities for environmental matters through contract negotiation	Moderate	Risk treatments and post risk rating are regarded as reasonable.
Access to and climbing of Uluru is banned by the Board of Management of the National Park and impacts visitation to ARR.	High	+ Negotiate and build relationships with Indigenous stakeholders + Develop other Indigenous experiences to draw visitors + Work with National Parks to promote Kata Tjuta walks	Moderate	Risk treatments and post risk rating are regarded as reasonable.
Significant slump in visitor numbers as a result of further downturn in world economic conditions impacts earnings.	High	+ Development of a thorough project plan including marketing strategy + explore ways of increasing duration of guest stays + 10 year financial forecast based on conservative occupancy	Moderate	A key proposed risk treatment was the development of a sensitised 10 year financial forecast based on conservative occupancy, reflecting a downturn in world economic conditions. The Board do not appear to have been presented with a sensitised forecast. Accordingly, the treatments proposed are regarded as reasonable but do not appear to have been implemented satisfactorily.

Our review of the ILC's risk assessment processes in respect of the ARR acquisition indicates that the ILC prepared a comprehensive risk management plan specific to the ARR project, with risks assessed in accordance with an appropriate risk framework. Prior to the 1 October 2010 board meeting to decide on the proposed acquisition, the ILC Board were provided with a SLA Proposal Risk Assessment which detailed Extreme and High pre-treatment risks and the treatments identified to mitigate those risks. We have identified a number of instances in which risks and associated treatments do not appear to have been adequately considered.

Board assessment of the acquisition risks

It is clear that the Board was provided with the risk assessment detailing the key project risks. However, from our review of the Board minutes and Board papers there is no evidence of a discussion regarding the risk assessment.

Accordingly, there is no confirmation from the Board that it has:

+ considered the SLA Proposal Risk Assessment;
+ challenged or questioned the Strategic Acquisition Proposal Risk Assessment's content;
+ factored the content of the Strategic Acquisition Proposal Risk Assessment into their final decision to acquire the ARR; and
+ ultimately accepted the moderate post-treatment risks, and considered that those risks were outweighed by the benefits of the transaction.

Conclusion

Our review demonstrates that the ILC prepared a comprehensive risk management plan specific to the project, with risks assessed in accordance with an appropriate risk framework. It appears that key risks were identified, with treatment strategies identified to mitigate Extreme, High and Moderate Risks.

Prior to the 1 October 2010 board meeting, the ILC Board was provided with the SLA Proposal Risk Assessment, which represented an extract of the full project risk assessment and detailed Extreme and High pre-treatment risks and the treatments identified to mitigate those risks. No Extreme or High post-treatment risks were identified. In respect of this, we note the following:

+ One of the treatments to reduce the risk that the purchase price paid did not represent value, was to obtain a full speaking valuation. Whilst a full speaking valuation was obtained, it was 17 months old at the date the transaction was entered into. Based on actual results subsequent to the valuation date, the valuation is considered to be out of date at the time of the transaction decision.

Conclusion- continued

+ The risk that the acquisition does not have the support of the Government was reduced to Moderate, as a result of a reduction in the likelihood from "possible" to "unlikely". Correspondence from the Minister for FaHCSIA and the Minister for Finance and Deregulation in the days leading up to the date the risk assessment was presented to the Board highlighted that the Government had significant concerns regarding the transaction. If the likelihood of this risk was increased to "possible" or "likely" this risk would have been rated as High.
+ A post treatment rating of Moderate was determined for the risk that visitor levels are heavily dependent on the airline companies. This was based on a number of treatment strategies aimed at strengthening relationships with key service providers. However, it is questionable whether these treatments are sufficient to reduce the risk rating from High to Medium. To a significant extent, the ARR will always have a reliance on the airline companies, and limited ability to influence the number of flights to Ayers Rock Airport.
+ Accordingly, it appears that there were a number of ARR transaction risks and associated treatments presented for Board consideration which do not appear to have been adequately considered and/or communicated.

Further, McGrathNicol notes that the 1 October 2010 board meeting minutes provide no confirmation that the risks set out in the SLA Proposal Risk Assessment were considered and accepted by the Board as part of its decision to acquire the ARR.

6.1 Consultation with Australian Government stakeholders

McGrathNicol has considered the ILC's engagement with key Australian Government stakeholders, particularly the ILC Board's communication with those stakeholders. In doing so, we have considered the legislative obligations of the ILC in relation to the transaction, including relevant provisions within the CAC Act and the ATSI Act.

Scope

Examine any matters deemed relevant to providing an assurance to the Parliament that this purchase was in the best interests of the ILC and Indigenous people.

Process undertaken

In addressing this scope point, we have considered the ILC's engagement with key Australian Government stakeholders, including:

+ what obligations the ILC had to keep the Australian government informed;
+ whether any approval of the transaction was required from the Australian Government;
+ the correspondence from the Australian Government, requests for information and the responses to those requests by the ILC; and
+ regardless of whether there was a requirement, was it appropriate for the ILC to obtain the agreement of the Australian Government to enter into the transaction.

The ILC requirements to consult with Australian Government stakeholders

In accordance with Section 191H of the ATSI Act, "*the ILC has power to do all things that are necessary or convenient to be done for or in connection with the performance of its functions*".

Section 191L of the ATSI act states that "*except as expressly provided in this Act or the Commonwealth Authorities and Companies Act 1997, the Minister is not empowered to direct the ILC in relation to any of its activities*".

However, it is noted that in accordance with Section 191N (6) of the ATSI Act, "*the ILC must give a copy of the national indigenous land strategy and a copy of any changes it has made to the national indigenous land strategy to the Minister within 2 months of the Board agreeing to the strategy or change*".

In accordance with Section 16 (1) of the CAC Act, the ILC must give the responsible Minister and the Finance Minister any reports, documents and information they require in relation to the operations of the ILC.

In accordance with Section 15 (1) of the CAC Act, the ILC is required to immediately notify the responsible Minister of the decision to acquire or dispose of a significant business.

ILC Communication with Australian Government stakeholders

Over the page is a table setting out the correspondence between ILC and the Ministers for FaHCSIA and DoFD (and their respective departmental representatives). This table is also set out in timeline format at Appendix 4.

The table highlights that a number of significant concerns were identified by the Australian Government. The ILC attempted to respond to these concerns through the provision of further information.

It is noted that some of these responses were provided to the Australian Government after the ARR transaction had been entered into (e.g. correspondence to Minister Wong on 5 November 2010).

Conclusion

From our review of the relevant legislation, and correspondence between the ILC and the Australian Government, it appears that:

+ the ILC met its requirements under the ATSI Act to keep the Minister informed of the transaction; and
+ the ILC was not required to obtain the approval of the Minister before entering into the transaction.

However, from the documentation made available for our review:

+ FaHCSIA and DoFD and their respective Ministers Macklin and Wong, did not express their support for the transaction and had provided strongly worded letters cautioning the ILC about the transaction;
+ FaHCSIA, DoFD and their Ministers did not seek to direct the ILC, highlighting the ILC's statutory independence; and
+ Minister Wong set out her concerns regarding the financial risks of the transaction, and that appropriate sensitivity analysis should be conducted. Whilst the ILC's letter of 5 November 2010 outlines the sensitivity analysis conducted by Grant Samuel, this analysis was provided after the transaction was entered into on 15 October 2010. The sensitivity analysis showed the impact of sensitivities on cash flows. However, there was no reference to the impact of sensitivities on the value of the ARR. As discussed at Section 3.5 above, limited sensitivity analysis appears to have been included in the GS financial model presented to the ILC Board at the meeting of 1 October 2010 to assist their assessment of whether to proceed with the transaction.

6.1 Consultation with Australian Government stakeholders

Prior to the acquisition of the ARR, Australian Government representatives including the Minister for FaHCSIA, Minister for Finance and Deregulation and representatives from the departments raised a number of issues in relation to the transaction.

Summary of issues raised of Australian Government stakeholders

A number of issues regarding the transaction were raised by Australian Government representatives in the lead up to the ILC entering into the transaction.

The key concerns raised by FaHCSIA, Minister for FaHCSIA (Jenny Macklin, MP), and the Minister for Finance and Deregulation (Senator Penny Wong) are detailed in the table below:

ARR transaction- Australian Government correspondence

Correspondence	Concerns raised	ILC response
19 August 2009 Letter from Minister Macklin to the ILC Chair	In accordance with Section 15(1) of the CAC Act, the Minister requested that the ILC provide written particulars of the proposed transaction. This included a request for details of the proposed financing arrangements and the impact on the ILC's debt levels and the projected profit or loss from the project.	The ILC did not provide the requested information to the Minister.
13 August 2010 Letter from the Secretary of the Department of Families, Housing, Community Services and Indigenous Affairs ("FaHCSIA") to the ILC Chairperson	In accordance with Section 15(1) of the CAC Act, the Minister requested that the ILC provide written particulars of the proposed transaction, including the financing arrangements and projected profit or loss of the project. This request included details of any borrowings required for the purchase of the resort.	In a letter of 27 August 2010 to the Secretary of FaHCSIA, the ILC CEO states that the ILC is of a view that it met its obligations under Section 15(1) of the CAC Act by providing a letter dated 10 August 2010 advising that the transaction has advanced to non binding heads of agreement. The letter of 10 August 2010 confirms that the proposed acquisition constitutes a proposal for the purposes of Section 15(1) of the CAC Act. The letter does not provide the information requested by the Minister in her letter of 19 August 2010. The ILC CEO states that due to the sensitive nature of negotiations any premature publicity could jeopardise the ILC's position, but the Minister will be kept appropriately informed. It is noted that in an email dated 15 August 2010, the ILC CEO advised FaHCSIA of the proposed borrowings for the project.
23 August 2010 Letter from Ms Donna Moody (FaHCSIA) to the ILC Chair	States that the Department has a strong view that the ILC not enter into borrowing funds for the purchase of the ARR in advance of the completion of a review by the Department of Finance and Deregulation of the ILC's borrowing and guarantee limits, planned for October 2010.	In a letter of 27 August 2010 to the Secretary of FaHCSIA, the ILC CEO states that the ILC Board notes this view, but does not accept it, and it is not prepared to suspend its power to borrow funds, pending completion of such a review.
22 September 2010 Letter from Minister Macklin to the ILC Chair	The Minister raised concerns regarding the impact such a significant investment would have on the ILC's ability to deliver outcomes across Australia for Indigenous people. She asked the ILC to advise how the acquisition will not limit the ILC's ability to carry out its functions, or hinder future strategic investment opportunities. The Minister also raised concerns regarding compliance with the ATSI Act including the divestment of the property, and the proposed borrowings given the upcoming DoFD review of these powers.	The ILC responded to the Minister on 23 September 2010 purporting to address the questions raised by the Minister. The ILC also stated in the letter that the reason they did not respond to the Minister's request for information in the letter of 19 August 2009 was because negotiations on the transaction were suspended at that time.
29 September 2010 Letter from Minister Wong to the ILC Chair	Minister Wong stated that she was concerned about financial and other risks that could arise from the proposal, and requested additional information urgently including confirmation of the ILC's compliance with the ATSI Act, evidence of due diligence and advice on how the ILC will meet its obligations if the financial projections for the project are not met. Minster Wong requested that this information be provided in sufficient time for it to be considered prior to the ILC proceeding with the proposed purchase.	The ILC responded to Minister Wong's letter on 30 September 2010, outlining the due diligence undertaken and the basis for concluding that the transaction was in accordance with the ATSI Act. In response to the Minister's request for additional time, the ILC advised that it would need to carefully weigh up the timing of the request against the statutory independence of the ILC, and the risk that any ongoing delay may jeopardise the transaction.
8 October 2013 Letter from Minister Wong to the ILC Chair	The Minister states that she remains concerned with the potential financial viability of the proposed purchase and the impact on the ILC's ability to perform its broader obligations, highlighting the medium to long term risks identified in the Horwath's review. She also again raised the benefit of undertaking independent sensitivity analysis to test the assumptions of the financial viability of the resort. The Minister requested additional information be provided within 28 days in the event that the ILC proceeded with the transaction.	The ILC responded on 5 November 2010, reinforcing their previous assurance to the Minister that significant due diligence was undertaken. The ILC provided the Minister with limited sensitivity analysis conducted by Grant Samuel, but sensitivities did not extend to the calculation of net present values. The response was provided within the 28 day timeframe, but post the ILC entering into the transaction.

McGrathNicol has undertaken a review of the consultancies commissioned by the previous ILC Board in respect of the ARR acquisition in order to determine compliance with ILC purchasing policies, as well as generally accepted governance procedures. This review included an examination of the engagement of lead advisor GS by ILC, as well as a review of other various consultancies entered into as part of the acquisition.

Scope point

Were all the consultancies commissioned by the previous ILC Board consistent with ILC purchasing guidelines and generally accepted governance procedures?

Process undertaken

- reviewed the ILC's policies and procedures with respect to procurement; and
- reviewed available documentation in relation to ARR consultancies engaged as part of the acquisition due diligence processes.

Consultancy services procured by the ILC in respect of the ARR acquisition

We have focused our review on the consultants engaged to provide advice to the ILC in respect of the acquisition of the ARR.

ILC engaged a wide range of consultants to assist with the ARR acquisition due diligence process. Consultancy areas included:

- deal advisory (a key consultancy, held by GS);
- Legal;
- Accounting;
- industry (tourism and hospitality);
- risk management;
- Marketing;
- environmental management; and
- miscellaneous others.

The table across contains an overview of the various consultancies commissioned as part of the acquisition, and the approximate fees charged by each advisor.

ARR acquisition consultancies

Consultant name	Role	fees $
Aspiron	Advice on airport and operations	34,115
Baker McKenzie	Legal advice on all aspects of the proposed acquisition and ongoing operations and financing	1,631,147
Beachframe (Bob Teague)	Review and report on future captial expenditure needs	48,766
CBRE	Valuation for National Australia Bank	48,500
Colliers	Valuation	56,929
Corrs Chambers	Review proposed legal structure and tax implications, assistance with issues raised by potential financiers	149,198
Grant Samuel	Deal advisory including debt facility negotiation	3,242,246
E Horner & Associates	Review existing IT and comms and identify cost of replacement/upgrade	33,332
Horwath HTL	review and report on accounting, tax and information technology	522,064
Mallesons	Lawyers for ANZ	88,644
Planed Property Management (David Wylie)	Review of building and technical service reports. Assess capital expenditure and identify energy consumption metering.	89,272
PWC	Company structure and tax advice	32,400
Simon Barlow	Hotel industry advisor	146,423
URS	Provision of environmental advice and identification of significant liabilities	41,685
All other consultancy costs	Includes expense reimbursements and a number of small consultancy fees	85,911
Total		**6,250,632**

Source: ILC, September 2013

Whilst the ILC is not strictly required to adhere to the Commonwealth Procurement Rules (or Commonwealth Procurement Guidelines ("CPGs") that were in place at the time of the transaction), its procurement and purchasing policies were premised on the key principles within the CPGs. Our review indicates that the ILC procurement policies in place at the time of the transaction were appropriate and consistent with generally accepted governance practices for an agency such as the ILC.

ILC and its procurement policy framework

In considering the appropriateness of the ILC procurement practices as part of the ARR transaction, we have examined the policy framework in place at the time of the transaction.

The ILC procurement policy framework in place at the time of the transaction due diligence and acquisition of the ARR was as follows:

Legislation	Commonwealth and other guidance documents	ILC policy
• CAC Act 1997 • CAC Regulations 1997 • ATSI Act 2005	• CPGs • National Indigenous Land Strategy	• *Purchasing – User Guide"*, updated May 2007; • *"Purchasing Responsibilities and Decision Making Principles";* • *"Practice Note 8.06b – Contracts Practice"*, updated 4 April 2003

ILC and the CPGs

The ILC is a Commonwealth Authority and is therefore subject to the requirements of the CAC Act.

The Department of Finance and Deregulation released a governance policy document in August 2005 entitled *"Governance Arrangements for Australian Government Bodies"* ("Governance Arrangements Document"). The Executive Summary of the document notes that CAC bodies are "*both legally and financially separate from the Commonwealth*". It further notes on page 3 that "*certain CAC Act bodies are listed in the CAC Regulations as subject to section 47A of the CAC Act, under which the Finance Minister can direct them to apply the Commonwealth Procurement Guidelines to certain procurement activities.*"

McGrathNicol has reviewed the list of CAC Act bodies subject to section 47A of the CAC Act (Parts 1 and 2 of Schedule 1 of the CAC Regulations refers). The ILC is not listed as a CAC Agency that is required to apply the CPGs.

Based on the above, legislation did not require the ILC to adhere to the CPGs in procuring consultancies in relation to the ARR acquisition. Notwithstanding this, we note the ILC's internal procurement policies are premised on the key principles of the CPGs. Further information regarding these key principles is outlined across the page.

ILC procurement policies

Over the period of the ARR due diligence and transaction process, the following procurement policy documents were in place at the ILC:

+ *"Purchasing – User Guide"*, updated May 2007 ("Purchasing User Guide");
+ *"Purchasing Responsibilities and Decision Making Principles"*; and
+ *"Practice Note 8.06b – Contracts Practice"*, updated 4 April 2003 ("Contracts Practice Note") (collectively referred to as the "ILC Procurement Policies").

The Purchasing User Guide is a practical guidance document to assist the ILC in purchasing goods and services. The key aspects of this document are as follows:

Key requirements of the ILC Purchasing User Guide

Section	Policy
1	"The CPG's….. are to be referred to during the purchasing function"
1	If the good or service is a non-standard purchase with a value in excess of $400,000…a tender is required"
3	"The ILC conducts its purchasing activity applying the key principles of the CPG's which are: • Value for money; • Encouraging competition; • Efficient, effective and ethical use of resources; and • accountability and transparency"
6	If the purchase is for greater than $2,000 (GST inclusive) written quotes are to be sought. Three quotes are generally considered the standard. If three quotes are not obtained, there is a requirement to document reasons for not obtaining three quotes. Exceptions to obtaining quotes are as follows: • Using quotes that are less than six months old; • In emergency situations; • For purchases less than $2,000; • When using a pre-qualified supplier.

Source: ILC "Purchasing User Guide", updated May 2007

ILC procurement policies conclusion

The ILC's procurement policies in place at the time of the transaction appear to be premised on the CPGs. The policies appear to be appropriate and consistent with generally accepted governance practices for an agency such as the ILC.

GS was engaged in October 2008 as lead advisor to the ILC in respect of the ARR acquisition. The engagement of GS appears to have facilitated through an engagement letter prepared by GS setting out the terms and conditions of the consultancy (which was signed by the ILC CEO as agreeing to the terms). McGrathNicol has examined the appropriateness of the processes undertaken by the ILC in engaging GS in light of the ILC's procurement policies and better practice procurement principles.

The engagement of Grant Samuel

GS was engaged on 20 October 2008 as lead advisor to the ILC to assist with management of the acquisition, including:

- development of a bidding strategy;
- advice on valuation;
- appointing legal, accounting and tax advisors;
- development of a financial model to facilitate transaction analysis;
- negotiations with JLL and GPT; and
- negotiations with potential lenders.

McGrathNicol has been advised by GS that it was initially engaged to provide due diligence advice to WU in respective of the ARR acquisition. GS indicated that they were introduced to the ILC at the time that WU approached the ILC to form a consortium to acquire the ARR.

The engagement of GS was made by way of an engagement letter prepared by GS setting out the terms and conditions of the consultancy. Following approval by the ILC Board, this letter was signed off by the ILC General Manager to evidence acceptance of the engagement terms. The letter states that it represents the entire agreement between the ILC and GS with respect to the consultancy.

Fee structure for GS services

In accordance with the ILC Board Minutes dated 22 October 2008, GS originally proposed a fee of 1.5% of total purchase price of the ARR. The minutes indicate that Director Baffsky advised the Board that he had negotiated a 1% fee and considered this represented a pricing arrangement in line with industry guidelines.

In accordance with the GS agreement, the fees payable by the ILC to GS were as follows:

- a retainer of $70,000 (GST exclusive) per month, payable monthly; and
- assuming the ILC acquired the ARR, 1% of the total consideration payable (less the sum of retainer fees already paid).

Evidence of seeking quotations for the engagement of GS

In accordance with the ILC's "Purchasing – User Guide", when engaging the transaction advisory services ultimately awarded to GS, the ILC should have sought a minimum of three quotations or clearly demonstrated why three quotations were not required.

Based on the range of purchase prices contemplated by the ILC for the ARR, it was foreseeable at the time GS was engaged that transaction fees would be significant, and in excess of the ILC's required tender threshold of $400,000.

Additionally, based on our review of data room documents and discussions with ILC staff, we have found no evidence to support that the ILC sought multiple quotations for the lead advisor role. Further, we have found no documentation to support why the ILC did not believe that the procurement process should involve a tender or obtaining three quotations.

In respect of the procurement for GS's services, the ILC does not appear to have applied the key principles of the CPGs, most notably the requirement to encourage competition and transparency.

GS contract form

As previously outlined, the engagement of GS was made by way of an engagement letter prepared by GS setting out the terms and conditions of the consultancy.

In accordance with the ILC's Contracts Practice Note, the process for establishing a new contact is to include:

- completion of the "Form F15 Checklist" providing a summary of the information required by legal when preparing a contract;
- review by legal, the project officer, and finance of the draft contract; and
- delegate approval.

McGrathNicol has considered the ILC's engagement of GS in order to determine compliance with ILC purchasing policies, as well as generally accepted procurement practices. We have been unable to substantiate that the engagement of GS was compliant with the ILC's procurement policies (which required a competitive tender or quotation process). Further, the form and content of the GS engagement letter did not meet the key requirements of the ILC Contracts Practice Note.

GS contract form– continued

The ILC Contracts Practice Note sets out that, in certain circumstances, ILC Legal may opt to draft a contract in short form, i.e. in letter format. Legal may exercise this option where:

- the contract is for value of less than $15,000;
- the contract is for an extremely short term; or
- contracts are drafted by other parties in this format.

However, the Practice Note states that these contracts should still be developed in accordance with the Practice Note.

Furthermore, we note that the GS engagement letter also does not include the following information that is commonly incorporated into contracts with Commonwealth Government agencies:

- some level of liability of the consultants beyond the fees for the assignment;
- details of hourly rates of the consultant's staff (although our experience of market practise suggests it would be unusual for engagements of this nature to be based on hourly rates in the commercial sector); and
- the ability for the Commonwealth to retain ownership in any intellectual property generated as a result of the consultancy.

GS contractual inclusions

The Contracts Practice Note sets out at Attachment E a number of general inclusions and consultancy contract specific inclusions that are required to be included in an ILC contract.

Required inclusions that were not present in the agreement entered into between the ILC and GS include:

- clear performance measures by which standards can be tested;
- specified personnel who will perform the services; and
- information regarding the consultant's insurance arrangements.

Conclusion- The engagement of GS

Page 57 of this report sets out the key requirements of the ILC's Purchasing User Guide that was in place at the time of the acquisition of the ARR. This policy document is premised on key CPG principles such as:

- encouraging competition;
- promoting transparency, and
- achieving value for money.

We have been unable to substantiate that the engagement of GS was compliant with the ILC's procurement policies. That is, GS was not engaged through a competitive tender process or through a process where multiple quotations were sought from competitor firms. Furthermore, the ILC has not documented why it did not require a tender process or a process where quotations were sought.

GS was engaged by way of a letter of engagement (initiated by GS), effectively a "short form" contract per the ILC's Contracts Practice Note definition. It appears that in entering into the short form letter of engagement between ILC and GS dated 20 October 2008, the ILC has not applied the key requirements of its Contracts Practice Note (albeit it is consistent with our understanding of market practice for engagements of this nature in the private sector).

The ILC's Contracts Practice Note contains a number of general inclusions and consultancy contract specific inclusions that should be incorporated into ILC contracts. Key inclusions such as performance measures, specified personnel and insurance arrangements were not included in the GS engagement letter. Common Commonwealth Government agency contract terms relating to liability, hourly rates and intellectual property were also absent from the GS engagement letter. Accordingly, it appears that the ILC did not comply with its Contracts Practice Note, or good practice for a Commonwealth entity in respect of the form and content of the contract entered into with GS for the provision of lead advisor services.

McGrathNicol was advised that, in relation to the procurement of other consultants, GS made recommendations to the ILC as to the appropriate parties to engage. In applying this procurement approach the ILC has not complied with its own procurement policies and has not demonstrated adherence with a number of generally accepted procurement principles.

Engagement of other consultants

The COO of the ILC advised that the following process was implemented for procuring consultants required to assist in the ARR acquisition:

- When a consultancy need was identified, GS was empowered to make recommendations to ILC regarding potential candidates/options to fulfil the requirements;
- ILC would directly engage the consultant based on GS advice; and
- the GS recommendations would be used in lieu of a competitive engagement process run by the ILC (per the requirements of its the Procurement Policies).

This approach is consistent with our review of available documentation.

In determining whether the engagement of consultants was conducted in accordance with ILC purchasing guidelines and generally accepted procurement principles, we have considered :

- use of competitive procurement processes (i.e. tenders and requests for quotations)
- fairness and impartiality
- record keeping
- consistency and transparency
- identification and management of conflicts of interest
- confidentiality arrangements

The table across sets out our general findings in respect of the governance processes associated with the ILC's procurement of consultants (excluding the GS engagement which is discussed in preceding pages of this report).

Consideration of ARR processes against review criteria

ILC Procurement policies	Finding
"The ILC applies the key principles of the CPGs, including….encouraging competition, and efficient and effective….use of resources" *"If the purchase is for greater than $2000 (GST inc.) written quotes are to be sought. Three quotes are considered to be standard. If three quotes are not obtained, there is a requirement to document reasons for not obtaining three quotes.*	A competitive process was not run by ARR, as GS was empowered to seek suitable suppliers. We have not located evidence that GS ran competitive, fair and impartial tender processes for consultancies recommended in accordance with ILC policy. Whilst we are advised by GS that a competitive process was run for the engagement of the ARR financial consultant (Horwath), we have not been provided with evidence that three quotations were sought for this particular or any other consultancies engaged (or reasons documented as to why the quotations were not sought).
"The ILC applies the key principles of the CPGs, including….accountability and transparency"	There does not appear to be records maintained by ILC regarding consultants selection process. Record keeping of consultancy agreements extends to a copy of consultancy agreements, and in some instances email/letter correspondence between ILC and the supplier. Accordingly, it cannot be demonstrated that the selection process for consultancies awarded was transparent and accountable.
"The ILC applies the key principles of the CPGs, including….the ethical use of resources"	McGrathNicol has confirmed that a conflict of interest register was not maintained as part of the ARR transaction. We have not been able to evidence whether or not consultancies awarded were ethical and awarded free of conflicts of interest.

Source: McGrathNicol analysis, ILC transaction records, and ILC Procurement Policies

Conclusion

In respect of the engagement of consultants advising on the purchase of the ARR, we have found no evidence that competitive tender or quotation processes were used by the ILC in making procurement decisions. Furthermore, the ILC is unable to demonstrate that its procurement processes were conducted in accordance with the ILC purchasing guidelines and generally accepted procurement principles.

McGrathNicol has examined whether a transparent audit trail was established to record ILC Board decisions, and whether the advice provided by consultants was followed by the Board. In addressing these scope points we have considered the quality of minutes recording Board meetings and decisions, and sought evidence that the advice of consultants was considered and followed by the ILC Board in making the decision to acquire the ARR.

Scope

- Was a transparent audit trail established that records ILC Board decisions and their implementation?
- Was the advice provided by consultants followed by the previous ILC Board and reflected in the negotiations?

In addressing these scope points, we have considered the following:

- the quality of minutes recording Board meetings, and Board decision making;
- whether advice of consultants was followed by the Board; and
- Audit and Risk Management Committee ("ARMC") involvement in the transaction.

Process undertaken

The Board papers and Board minutes are the key evidence within ILC that supports the Board decision making process. In completing fieldwork for this scope point we undertook the following procedures:

- reviewed the board meeting minutes and Board papers for the period 27 August 2008 to 20 June 2011;
- reviewed the ARMC minutes for the period June 2008 to March 2011; and
- held discussions with the ILC Board Secretariat.

General observations- quality of minutes recording Board decision making

Our main focus has been on the quality of board minutes and decision making in relation to the 1 October 2010 decision to acquire the ARR. However, based on our review of all board meeting minutes for the period 27 August 2008 to 20 June 2011, we make the following general observations:

- the ILC has a dedicated board secretariat function. Board packs appear to have been prepared and made available to directors in advance of each meeting;
- for each of the board meetings reviewed, the secretariat would personally attend, draft the minutes, and finalise the minutes after implementing any required changes. McGrathNicol was able to locate minutes for each of the board meetings held over the relevant period; and
- the Board meeting minutes appear to record the key decisions of the board, important discussions, and the resolutions passed.

ARR acquisition decision- quality of minutes recording Board decisions

The final decision to acquire the ARR was made in the board meeting of 1 October 2010.

The Directors were provided with board papers in advance of the meeting, including the SLA Proposal, a document setting out the costs and benefits of the transaction, and how risks would be managed.

The Directors were also provided with a number of due diligence reports and advice prepared by the consultants. A number of these consultants presented those reports to the meeting attendees. Legal due diligence supported the ILC's ability to enter into the transaction. The report presented by the lead advisor GS provided a clear recommendation that the ILC proceed with the acquisition as contemplated, at a net purchase price of $292m. In addition to these reports, a number of consultants made presentations to the Board concerning the specific due diligence activities they had undertaken.

Board Minutes and Board Land Acquisition Decision

The 1 October 2010 board meeting is recorded in both the Board Minutes, and a specific decision paper "Board Land Acquisition Decision". The Board Minutes set out the key proceedings that took place within the meeting, although little detail was contained regarding specific questions asked by Directors, or the discussions held.

The Board Land Acquisition Decision document sets out the information and factors considered in making the acquisition decision, including detailed notes on why the ILC had authority to enter into the transaction, and a high level summary of the due diligence conducted.

Whilst there is a statement in the Board Land Acquisition Decision that the transaction was in the ILC's best interests and for its benefit, there were no reasons set out as to why this was the case.

Conclusion- quality of minutes recording Board decisions

From our review of the Board minutes and the Board Land Acquisition Decision dated 1 October 2010, we note that whilst the Board Land Acquisition Decision provides a summary of the due diligence work undertaken, it does not clearly set out the findings of the due diligence activities and the relevance to the decision to pursue the acquisition.

The ILC Board resolved that the transaction was in the ILC's best interests and for its benefit. It is considered prudent to support an overarching comment such as this with a summary of the reasons why the transaction was considered to be in the best interests of the ILC.

On 16 June 2010, the Board resolved to progress negotiating the acquisition of the ARR. On 1 October 2010, the Board resolved to acquire the ARR. Whilst voting on these resolutions appears to have been in accordance with the ATSI Act, it is clear that at least two of the seven directors had significant concerns regarding the acquisition, and abstained from voting in respect of the resolutions. Further, Director Gorringe has advised McGrathNicol that he had not supported the acquisition. The minutes only record clear support of three of the seven directors. Accordingly, the Board should have considered the appropriateness of passing the resolution to acquire the ARR in the absence of a clear majority from the Board.

Board meeting # 134 – 16 June 2010

The minutes record that the Chairperson requested that all Directors be present as a decision must be made at this meeting as to whether to progress negotiations with GPT to purchase the ARR.

The meeting was attended by all Directors except Director Gorringe.

The minutes record that "*Directors Jeffries, Baffsky and Goolagong-Cawley expressed their support for the proposal. Director Trust stated that he was supportive but had concerns about the number of people willing to move to the resort for training. Director Driscoll stated that he was concerned that checks and balances are put in place*". The minutes do not state the view of the ILC Chairperson, Ms Shirley McPherson ("Director McPherson").

The following resolution was put to the Board:

"*that the Board approves to progress negotiations with GPT to purchase ARR, subject to:*

- *Finance being secured;*
- *The Land Account legislation being passed;*
- *Further due diligence; and*
- *Acceptable legal documentation*".

The resolution was moved by ILC Director Jeffries ("Director Jeffries") and seconded by ILC Director Evonne Goolagong-Cawley ("Director Goolagong-Cawley"). The minutes record that Directors Trust and Driscoll abstained.

The minutes do not record that a formal vote was taken. Based on the minutes it appears that three of the seven directors were in support of progressing negotiations, with the support of one Director unclear (Director McPherson), two directors abstaining (Directors Trust and Driscoll) and one Director absent (Director Gorringe).

Section 192J of the ATSI Act requires at least four directors to be present to constitute a quorum. In accordance with Section 192J(6), questions are to be determined by a majority of the votes of directors present and voting. Accordingly, whilst voting of all directors was not recorded, the passing of the resolution with support of the three directors appears to be compliant with the ATSI Act.

Board meeting # 136 – 1 October 2010

The minutes record that at this meeting the Board were presented with the due diligence undertaken by the ILC and its consultants in respect of the proposed acquisition of the ARR.

The minutes states that the Board asked questions of consultants over a period of two hours, though these questions and answers are not recorded in the minutes.

The meeting was attended by all seven Board members, with Directors Driscoll, Trust and Gorringe attending via teleconference. Director Driscoll left the meeting early stating that "*he wished to have recorded in the minutes that he will abstain from voting on any resolution in relation to the acquisition of the ARR*".

The following resolution was put to the Board:

"*that the Board resolves to implement the decisions, as drafted by Baker and McKenzie, that approve the acquisition of ARR. Further, that the implementation of these resolutions is subject to the Chairperson having regard to any valid, substantive issues that might be raised within the next seven days by the Minister for Finance and Deregulation, Senator Penny Wong, regarding Directors' duties under the CAC Act*".

The resolution was moved by Director Jeffries and seconded by Director Goolagong-Cawley. The minutes record that Directors Trust and Driscoll abstained.

As for the meeting of 16 June 2010, the minutes do not record that a formal vote was taken. Based on the minutes the voting intention of Directors Baffsky, McPherson and Gorringe is unclear. It is reasonable to assume based on previous Board minutes that Director Baffsky supported the acquisition. Director Gorringe advised McGrathNicol that he had not supported the acquisition. The minutes do not indicate whether Director McPherson did or did not support the acquisition.

Given the significance of the proposed acquisition to the ILC, strong governance would have been for the minutes to clearly record the support of a majority of the Board (at least 4 of the 7 directors). If there was not clear support of at least four directors, then the Board should have considered the appropriateness of passing the resolution.

We reviewed whether advice provided by external consultants was noted by the previous ILC Board and reflected in the ARR purchase negotiations. It appears that the consultants' advice was generally followed. However, we note the Horwath HTL due diligence report which contained warnings regarding a decline in value of the ARR.

Was the advice of consultants followed by the Board?

The table below sets out the key pieces of due diligence advice obtained by the ILC Board, the headline findings of the advice, and McGrathNicol's assessment regarding the extent to which the advice was followed by the ILC Board.

ARR acquisition key consultancies and advisors

Due diligence advisor	Role	Key advice	Was the advice followed by the ILC Board?
Grant Samuel	Coordination of the due diligence and business structure proposal (lead advisor)	In their report to Board dated 1 October 2010, Grant Samuel recommended that the ILC purchase the ARR on the terms proposed.	Yes
Corrs Chambers Westgarth	Legal compliance	Determined that the transaction was in compliance with the ATSI Act (including the ILC's land acquisition function), and in compliance with the CAC Act.	Yes
Baker and McKenzie (including counsel advice from Mr Neil Hutley, SC)	Legal due diligence of the properties and businesses	Provided a range of advice to ensure the protection of the ILC in respect of the terms and conditions in the sale agreement.	Yes
Horwath HTL	Accounting / financial due diligence	Identified that the ARR EBITDA for first half of 2010 was a 26% year on year decline, and that the 2010 forecast appeared to be highly optimistic. Horwath concluded that the ARR value had materially declined as a result, with a risk of further decline. Horwath also prepared a SWOT analysis and identified key risks.	As set out in Section 3.4 of this report, the ILC contacted GPT following the receipt of the Horwath's advice, seeking to renegotiate the acquisition price. Ultimately the ILC proceeded with the acquisition despite Horwath's warnings regarding a decline in value of the ARR. Horwath's SWOT analysis and key risks identified were incorporated into the ILC's risk assessment and treatment plan.
Planned Property Management	Property due diligence	Conducted a detailed review of the physical condition of the property and the capital expenditure requirements of the ARR for the next 5 years.	Yes, as discussed at Section 3.5 above, the capex forecasts were incorporated into the ARR cashflow model. However, it is noted that PPM's initial estimate of approximately $77 million was revised to $53 million following the ILC requesting that PPM reduce estimates to include essential capital expenditure only.

Source: ILC data room, and McGrathNicol analysis

Whilst not specifically part of the scope item, we examined the involvement of the ILC Board's Audit and Risk Management Committee ("ARMC") in supporting the wider ILC Board with respect to the ARR acquisition decision. We found that the only ARMC meeting for which the minutes record discussion of the ARR acquisition was the meeting dated 22 March 2011. Given the high risk nature of the acquisition, the lack of involvement by the ARMC is considered a deficiency in the ILC's then governance processes.

Conclusion- was the advice of consultants followed by the Board?

Based on our review it appears that the ILC Board substantially followed the advice of the consultants. The key exception to this is that Horwath advised of a decline in the value of the ARR as a result of the decline in EBITDA in the first half of 2010. Following the receipt of this advice the ILC tried to negotiate a lower transaction price with GPT. However, they do not appear to have reflected the lower EBITDA results into their financial modeling.

The advice from Horwath was clear and very significant. At a minimum, the ILC should have considered the need for an updated valuation and reflected lower EBITDA forecasts in their ARR financial model. As discussed at Section 3.4, this did not occur.

Audit and Risk Management Committee

Whilst not specifically part of this scope item, we examined the involvement of the ILC Board's ARMC in supporting the wider ILC Board with respect to the ARR acquisition decision.

We reviewed the minutes of the ARMC for the period June 2008 (meeting #38) to March 2011 (meeting #48). We found that the only ARMC meeting for which the minutes record discussion of the ARR acquisition was the meeting dated 22 March 2011. At this meeting, the ARMC discussed the progress of the settlement of the ARR purchase, including the status of updated ARR budgets and cash flows.

It is clear from the minutes that the ARMC had almost no role in the oversight or consideration of the acquisition of the ARR. We find this unusual given the length of the transaction spanned approximately two years.

Section 2.1 of the ANAO "Public Sector Audit Committees" Better Practice Guide (dated August 2011, an update to the August 2005 version) states that "*Better practice committees will also generally have a key role in providing assurance that management has in place effective risk management practices when implementing high risk projects, programs and/or activities*".

Conclusion- Audit and Risk Management Committee

Given the high risks of the transaction, and material nature of the ARR investment in relation to the ILC's existing investments and asset base, it is considered a deficiency in the ILC's then governance processes that the ARMC had almost no involvement in the transaction to purchase the ARR. In light of the duration of the due diligence and negotiation activities, we believe that the ARMC should have given some consideration as to the risk management practices in place within the ILC for this specific transaction (more detail in Section 5.1 of this report).

McGrathNicol has considered whether the ILC was legally able to enter into the ARR purchase transaction and if it was reasonable for the ILC to consider that the acquisition would not have an impact on the ILC's existing operations. In considering this, we have reviewed applicable legislation, reviewed correspondence between ILC and government stakeholders and reviewed due diligence undertaken by ILC and its consultants.

Scope

Examine any matters deemed relevant to providing an assurance to the Parliament that this purchase was in the best interests of the ILC and Indigenous people.

In addressing this scope point, we have considered:

+ whether the ILC obtained sufficient advice to confirm that it was legally able to enter into the transaction; and
+ whether it was reasonable for the ILC to consider that the acquisition would not have an impact on the ILC's existing operations.

Procedures undertaken

In considering the above, we have undertaken the following steps:

+ reviewed applicable legislation;
+ reviewed correspondence between the ILC and government stakeholders; and
+ reviewed due diligence undertaken by the ILC and its consultants in relation to the legality of the acquisition.

Applicable legislation

The key legislation and documentation setting out the objectives and powers of the ILC is:

+ the ATSI Act;
+ the CAC Act; and
+ The NILS for the period 2007-2012.

McGrathNicol highlights that this section of the review does not constitute a legal opinion regarding legislative compliance. Rather, our review is focused on the approach taken by ILC in the due diligence phase to satisfy itself and relevant Commonwealth stakeholders of compliance.

ATSI Act

Section 191C of the ATSI Act sets out that the ILC has the following functions:

+ land acquisition; and
+ land management.

The acquisition of the ARR appears to meet the definition in the ATSI Act of a Land Acquisition function. This was confirmed by two separate pieces of legal advice provided to the ILC by Corrs and Mr Neil Hutley, SC.

In accordance with Section 191D (1) of the ATSI Act, the land acquisition functions of the ILC include:

a) to grant interests in land to Aboriginal or Torres Strait Islander corporations; and

b) to acquire by agreement interests in land for the purpose of making grants under paragraph (a).

The following sections of the ATSI Act are key to determining whether or not the ARR acquisition was compliant with legislation:

+ Section 191E (5)(a)- the ILC's land management functions include carrying on a business that involves the use, care or improvement of land.
+ Section 191D (3)(b) - where the ILC acquires an interest in land for the purpose of making a grant of the interest to an Aboriginal or Torres Strait Islander corporation, the grant is to be made within a reasonable time after that acquisition.
+ In accordance with Section 191N of the ATSI Act, the ILC must prepare the NILS. In accordance with section 191Q of the ATSI Act, for the performance of its functions, the ILC must have regard to the NILS.

In short, it appears that the following criteria had to be met for the ARR acquisition to be ATSI Act compliant:

NILS Strategy	• the purchase should have been consistent with the ILC's strategy set out in the NILS
Transfer to an ATSI Corporation	• The purchase should have been made for the purpose of transfer to an Aboriginal and Torres Strait Islander corporation
Transfer timeframe	• the transfer to an ATSI corporation should be intended to be effected within a reasonable timeframe

Extensive discussions regarding legislative compliance were held during the acquisition due diligence period. The external legal advice obtained by the ILC supports that the acquisition and management of the ARR (with a long term view to transfer ownership) is permitted in accordance with the ATSI Act, and the CAC Act. However, it is unclear whether or not the proposed lease-back arrangement of the resort as a going concern would be consistent with the ILC's functions and objectives. The ILC does not appear to have obtained legal advice in this regard.

Background- the Land Account

As previously outlined, the Land Account provides annual funds to the ILC for its land acquisition and management activities, as prescribed by the ATSI Act. The establishment of the Land Account was part of the Australian Parliament's response to the High Court's decision in the Mabo case. Accumulated Land Account funds were used as the ILC's cash contribution in the purchase of the ARR.

McGrathNicol is aware that there was some question at the time of the acquisition as to whether the purchase and operation of a complex tourism business was outside of the intended purpose of the Land Account and the ILC's functions and objectives.

Indicators of compliance with the relevant legislation

Given the questions raised regarding the appropriateness of the purchase, with reference in particular to the ATSI Act, extensive discussions were held during due diligence regarding legislative compliance, which was supported by multiple legal opinions. The following factors illustrate the steps taken by ILC to explore the acquisition's legislative compliance:

+ The SLA Proposal presented to the Board on 1 October 2010 states that the land on which the ARR operates will be granted to an appropriate Indigenous title holding body when secured and unencumbered title is available through the discharge of the ILC's financial and security obligations (projected to be in 10 years' time). The ILC notes that it will work with Traditional Owners and local Indigenous people to identify a suitable Indigenous corporation to grant the land to. The grant was to occur with a lease back arrangement to ensure the ongoing operation of ARR. The SLA Proposal states that there is precedent for a 99 year leaseback arrangement with Traditional Owners over Uluru Kata Tjuta National Park.
+ Mr Noel Hutley, SC, provided legal advice dated 11 August 2010 to the ILC under instruction from Baker & McKenzie on a range of ARR acquisition legal issues. Mr Hutley examined in detail whether the acquisition of the ARR operating business (as distinct from the ARR land) would fit within the ATSI Act's acceptable purposes. He concluded that the conduct of the business after acquisition would be within the scope of the function of the ILC.

Indicators of compliance with the relevant legislation- continued

+ the 2007 – 2012 NILS does not appear to have been updated to include reference to the acquisition of the ARR. The NILS is required to be reviewed at least annually and revisited if required. Given the commercial in confidence nature of the acquisition, this may have prevented the NILS being updated prior to the ARR acquisition, however it may have been appropriate for the ILC to update the NILS following the acquisition.
+ Corrs provided legal advice dated 13 August 2010 to the ILC, advising that assuming it remains the intention of the ILC to grant the assets to a suitable ATSI corporation at an appropriate time in the future, the ILC will comply with its functions under the ATSI Act. Corrs' advice discusses the ARR assets, and it is unclear whether this refers to the land assets or the resort as a going concern business as well.

CAC Act

McGrathNicol reviewed the CAC Act and did not identify any specific provisions of the CAC Act that would prevent the ILC (either in its own capacity of through its subsidiary ILC Tourism) from entering into the transaction.

Conclusion- compliance with ATSI Act and CAC Act

During the 1 October 2010 Board meeting, the Directors concluded that based on the legal advice received, the acquisition of the ARR was permitted under the ATSI act.

The external legal advice obtained by the ILC supports that the acquisition and management of the ARR (with a long term view to transfer ownership) is permitted in accordance with the ATSI Act, and the CAC Act.

However, the expectation of the ILC at the time of the acquisition appears to be that the ARR operating business (i.e. the going concern) would be leased back after the transfer of the land, potentially for a 99 year term. This would result in the ILC becoming the long term operators of the resort. The legal advice obtained by the ILC does not appear to consider whether a long term lease-back is consistent with the ILC's functions and objectives.

The ILC strongly countered concerns raised by the Ministers for FaHCSIA and Finance & Deregulation that the ARR acquisition would impact its existing operations and future land acquisition opportunities. McGrathNicol regards that, given the significant scale of the acquisition, even where the ILC Board considered that the ARR acquisition could be self-funding, it was unrealistic to assert to key Government stakeholders that a purchase of this materiality would not have a significant impact on its other operations and financial investments in the future.

Impact of the acquisition on the ILC's existing operations

As outlined in Section 3 of this report, the net purchase price for the acquisition of the ARR was $292 million, and was funded by a mixture of debt funding and the ILC's cash reserves.

In the SLA Proposal presented to the Board on 1 October 2010, it is stated that "*the ILC has been careful to ensure that all due diligence, planning and financial forecasts for the acquisition and operation of ARR provided for the ILC maintaining its current and future planned operations*".

As discussed at Section 6.1 of this report, the Ministers for FaHCSIA and DoFD were also concerned that the acquisition would have an impact on the ILC's existing operations and future investment opportunities. The ILC strongly countered these concerns in letters to the Ministers and their respective Departments.

The below table sets out the movement in the asset and liability base of the ILC (on a consolidated basis), demonstrating the material change in the ILC's financial profile as a result of the ARR transaction.

ILC consolidated balance sheet

(A$'000)	30-Jun-11	30-Jun-10	Movement
Financial assets	117,475	162,076	(44,601)
Non financial assets	563,568	246,173	317,395
Total assets	**681,043**	**408,249**	**272,794**
Payables	254,126	6,205	247,921
Provisions	130,732	119,942	10,790
Total liabilities	**384,858**	**126,147**	**258,711**
Net assets	**296,185**	**282,102**	**14,083**

Source: ILC Annual Report, 30 June 2011

Impact of the acquisition on the ILC's existing operations

Given the significant scale of the acquisition in the context of the ILC's existing operations and balance sheet, and the inherent challenges and risks involved in acquiring a large and complex tourism business, a variety of pre and post-acquisition time and cash impacts should have been assumed regardless of the success of the acquisition. These challenges and risks are set out below:

Potential impacts of the ARR acquisition on ILC operations

Impact	Pre-acquisition	Post-acquisition
Time	ILC COO, Group Counsel and other staff time invested heavily in the delivery of the transaction.	Restriction on the ability to pursue other land acquisitions.
	Establishment of the ILC Tourism Management team	ILC required to provide post acquisition implementation support to ILC Tourism Management team.
	Diversion of the time of ILC Board members away from other ILC business to ARR matters.	Establishment of effective communication channels between ILC and ILC Tourism Board.
Financial	Due diligence and consultancy costs otherwise available for lower risk projects.	Potential ARR cash flow shortfalls or unforecast capex needs would require ILC funding.
	Use of cash reserves to contrbute to ARR purchase.	Inherent risks of the ILC Tourism loan guarantees. Significantly reduced capacity to invest in other land projects as a result of both restriction in the ILC's capital reserves, and the ability to borrow in the future.

Source: McGrathNicol analysis

Conclusion

McGrathNicol considers that it was unrealistic to assert to key stakeholders that a purchase of this materiality would not have a significant impact on the ILC's operations and land acquisitions in the future. It is clear that an ongoing and active management of the post-acquisition implementation would be required, regardless of the success of the acquisition.

The CAC Act imposes duties on the directors of the ILC to act with care and diligence, act in good faith, and not make improper use of their position and information. There is no evidence to suggest that ILC directors have acted contrary to their CAC Act duties in respect of the acquisition of the ARR. Section 191F(1) of the ATSI Act requires the ILC to act in accordance with sound business principles. Given the concerns of stakeholders, and the significance of the transaction, and required borrowings, to the ILC, we believe the ILC was deficient in documenting the appropriate deliberation and assessment required to demonstrate sound business principles.

Directors' duties

In accordance with Section 22 of the CAC Act, the following general duties apply to directors:

- Section 22(1) Care and diligence – *an officer of a Commonwealth authority must exercise his or her powers and discharge his or her duties with the degree of care and diligence that a reasonable person would…*
- Section 22 (2) Business judgment rule – an officer of a Commonwealth authority who makes a business judgment is taken to meet the requirements of Section 22(1), and their equivalent duties under the general law, in respect of the judgment if he or she:
  - Makes the judgment in good faith or for a proper purpose; and
  - Does not have a material personal interest in the subject matter of the judgment; and
  - Informs himself or herself about the subject matter of the judgment to the extent he or she reasonably believes to be appropriate; and
  - Rationally believes that the judgment is in the best interests of the Commonwealth authority.

It is noted that Section 22(2) also states in respect of the application of the "Business judgement rule" that in accordance with this section, the officer's belief that the judgement is in the best interests of the Commonwealth authority is a rational one unless the belief is one that no reasonable person in his or her position would hold.

In accordance with Section 23 of the CAC Act, an officer must exercise his or her powers in good faith and in the best interests of the Commonwealth authority, and for a proper purpose.

In accordance with Sections 24 and 25 of the CAC Act, officers must not use their position or information to gain advantage for themselves or to cause detriment to the Commonwealth authority or another person.

Conclusion

Based on the comprehensive analysis conducted by the Board, the due diligence conducted into the transaction, and recommendations of key advisors (such as GS), there is no evidence to suggest that the ILC Board have acted contrary to their CAC Act duties.

Section 191F of the ATSI Act – Sound Business Principles

In accordance with Section 191F(1) of the ATSI Act, "*the ILC must act in accordance with sound business principles whenever it performs its functions on a commercial basis*".

The acquisition and operation of the ARR is considered to be a commercial function, and therefore the demonstration of sound business principles is required.

The ATSI Act does not define sound business principles. However, the ATSI Act test of "sound business principles" appears to be a sterner test than the CAC Act duty imposed on directors in accordance with the business judgment rule"

The "sound business principles" clause focusses on the act of performing functions on a commercial basis. It does not have a clear defence to the "no reasonable person" defence. It also does not focus on the belief of a director as to whether they have exercised sound business judgment.

Conclusion

Clear and strong warning signs were being expressed by the Minister for DoFD and the Minister for FaHCSIA, cautioning the ILC about the ARR purchase.

Significant risks were identified by the ILC's consultants in respect of the transaction. Whilst risk treatment activities were identified, these do not appear to have been significantly progressed by the ILC to manage the risks to an acceptable level.

The scale of the transaction was extraordinarily large in light of the ILC's ordinary business operations. The transaction absorbed the ILC's existing cash reserves and all but exhausted the ILC's borrowing limits under the ATSI Act.

In the light of these matters we believe the ILC was deficient in documenting the appropriate deliberation and assessment required to demonstrate sound business principles. This does not of itself mean that the acquisition was inappropriate. However, a transaction of this scale opens the ILC up to the charge that it did not adequately protect itself against downside risk.

We have also considered whether there were conflict of interest issues in respect of the ARR acquisition. As part of the fieldwork undertaken for this scope point we have undertaken a number of search processes to identify whether individual directors had undeclared conflicts of interest with the ARR vendor and other key suppliers.

Scope

Were appropriate declarations and recording of conflicts of interest made?

In addressing these scope points, we have considered the following:

- the processes the ILC had in place to identify and manage conflicts of interests; and
- whether there were conflict of interest issues in respect of the ARR acquisition.

Process undertaken

In considering the above, we have undertaken the following steps:

- reviewed Board minutes;
- held discussions with the ILC COO; and
- undertook searches to identify any conflicts between the ILC Directors and GPT.

Conflicts of interest

We have sought to identify any conflicts of interest between the ILC Directors in relation to the acquisition of the ARR. In particular, we have focused our review on:

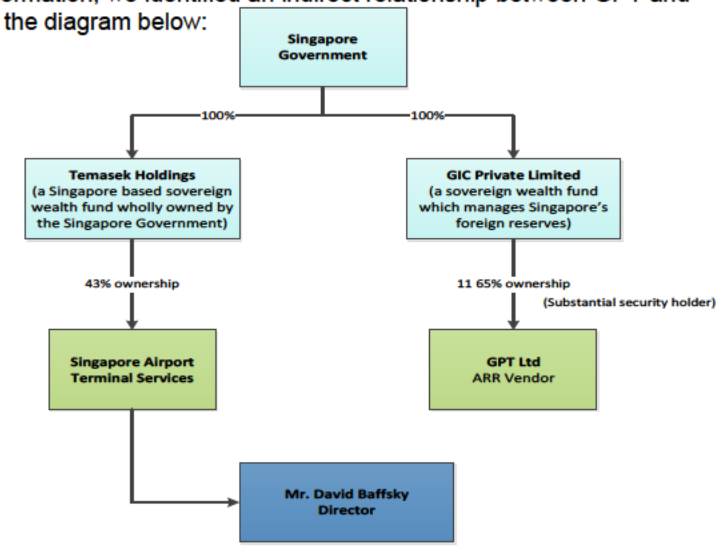
- potential conflicts of interest between the individual ILC Directors and the ARR vendor, GPT;
- potential conflicts of interest between other key suppliers engaged as part of the ARR acquisition; and
- whether the GS fee arrangement was structured in such a way that gave rise to a professional conflict of interest.

As part of our review, we sought to ascertain whether a conflict of interest register for ILC Directors and employees was in place at the time of the ARR transaction. We have confirmed that no register was in place at the time of the transaction, and the ILC relied on employees and/or directors to declare conflicts as they arose.

Conflicts of interest- review of whether there was an existing relationship with GPT

McGrathNicol undertook a review to consider whether there were any potential conflicts of interest between the ILC Directors and GPT. In doing so, we undertook a series of Australian Securities and Investment Commission and Australian Securities Exchange searches to determine whether any prior relationships existed at the time of the transaction.

Using publicly available information, we identified an indirect relationship between GPT and Director Baffksy, set out in the diagram below:



Conclusion

McGrathNicol has no further knowledge regarding this connection, and therefore cannot conclude whether or not it represents a conflict of interest. However, the connection appears to be remote. A review of the ILC Board Minutes over the period of the transaction indicates that the above connection was not disclosed by Director Baffsky.

McGrathNicol did not identify any further potential Director-related conflicts of interest from our testing. However, it is considered a shortcoming in the ILC's governance framework that a formal conflict of interest register for ILC Directors and employees was not maintained at the time of the ARR transaction. The implementation of a conflict register, along with a formal process of actively requiring Directors and employees to regularly declare potential conflicts of interest (or attesting that there are no conflicts), increases the likelihood that potential conflicts are declared and effectively dealt with in a transparent manner.

At the time of the transaction, Director Baffsky held the role of Honorary Chairman of Accor Asia Pacific, the successful party for the ARR hotel services provider contract. It appears that Director Baffsky was transparent about declaring this relationship and was not involved in Accor's selection. The GS advisory fee structure reflected common industry practice (i.e. fee based on a percentage of transaction price). However, these arrangements do not incentivise an advisor to seek the lowest possible price or advise against entering into a transaction.

Conflicts of interest- the Accor hotel service provider

In December 2010, Mr Koos Klein (consultant for Voyages at the time) commenced a tender process for the selection of a hotel service provider for the ARR. Six parties were invited to tender, including Accor Asia Pacific Limited ("Accor"). Director Baffsky had held the role of Honorary Chairman of Accor since February 2008, and prior to then had held the Executive Chairman role at Accor. Appropriately, Director Baffsky declared a conflict of interest in relation to Accor's involvement in the tender process.

A board meeting was held on 1 July 2011 to select the preferred hotel service provider. The Board Paper, prepared by CEO Koos Klein, provided a comprehensive review of the tender process conducted, as well as an assessment of the various tenders against key criteria including:

- indigenous credentials;
- branding;
- pricing; and
- other "value add" offerings.

As part of the 2013 ILC Governance review undertaken by Deloitte, Director Baffsky advised that due to the conflict of interest, an independent ILC Tourism board committee was formed to oversee the appointment, which he was excluded from. The Board Paper of 1 July 2011 reviewed by McGrathNicol supports this advice.

Conclusion

Director Baffsky declared his conflict of interest in relation to Accor. Further, the Voyages Board appear to have taken appropriate steps to manage this conflict of interest.

The Voyages Board's decision to appoint Accor appears to have been made with the benefit of a comprehensive Board Pack which contained comparative financial and other relevant analysis across the range of tenders received. The information pack supported the Voyages CEO's recommendation that Accor should be appointed based on its credentials and value for money when compared to competing tenders.

Director Baffsky was excluded from an independent committee that was formed to make a recommendation on the service provider, and did not participate in the final vote to award Accor the engagement.

Conflicts of interest- GS fee structure

As discussed at Section 6.2 above, the GS fee for the lead advisor role was a $70,000 (GST exclusive) per month retainer, with a completion fee of 1% of the consideration paid or payable in respect of the transaction. The monthly retainer was rebateable against the completion fee.

The fee arrangement was approved at the Board meeting of 22 October 2008. The meeting minutes note that Director Baffsky had discussed the arrangement with the independent member of the ARMC, with the view formed that the GS fee structure was within industry guidelines for such an acquisition.

Whilst we concur that the GS advisory fee structure reflected common industry practice, we note the following:

- As at July 2010, GS's monthly retainer fees earned to that date totaled $770,000, significantly lower than the completion fee payable to GS if the ARR was acquired (approximately $3 million based 1% of the proposed purchase price at that time of $300 million). Accordingly, there was a significant financial benefit for GS if the transaction proceeded. As noted in this report, GS provided a recommendation to the Board that they enter into the transaction. We make no finding that GS acted improperly in this respect and again highlight that completion fee arrangements for advisors are relatively common in the financial services industry. However, the structure of the fee arrangement with GS meant an inherent conflict where GS would benefit (significantly) from the transaction proceeding.
- A fee based on a percentage of the total consideration paid provides a greater fee to GS the higher the amount of the purchase consideration. Given that a component of Grant Samuel's role was to negotiate the best outcome for the ILC, this fee structure did not operate to incentivise GS in a manner optimal for the ILC. We make no finding that GS acted improperly in this respect and again highlight that completion fee arrangements for advisors are relatively common in the financial services industry.

Conclusion

The GS advisory fee structure reflected common industry practice. However, these arrangements do not incentivise an advisor to seek the lowest possible transaction price or advise against entering into a transaction. McGrathNicol does not imply that GS sought to take advantage of this arrangement. Rather, it may have been prudent for the ILC to consider and negotiate an alternate fee structure.

7 Establishment of Voyages

7.1 Voyages establishment and Director appointments

McGrathNicol has examined whether the establishment of Voyages, selection of Directors, length of appointment and setting of remuneration was done in accordance with normal practice. We have also examined compliance with relevant legislation such as the ATSI and CAC Acts. It appears that establishing Voyages for the purposes of the ARR transaction was done in accordance with the ATSI Act, and we have concluded that the notification of the Minister for FaHCSIA regarding the impending purchase transaction met the requirements of the CAC Act.

Scope

Was the establishment of Voyages, selection of Directors, length of appointment, and setting of remuneration in accordance with normal practice?

Process undertaken

As part of our review of the ILC Tourism board appointments, we reviewed the following documentation:

+ emails dated 12 August 2010, 9 August 2010, 29 July 2010 between the ILC COO and Baker & McKenzie regarding the ILC Tourism Pty Ltd draft constitution (since renamed to Voyages Indigenous Tourism Australia Pty Ltd ["Voyages"]);
+ ILC Board Decision 274 (dated 25 August 2010) which established the ILC Tourism entity and appointed the first two directors, David Baffsky and the ILC General Manager, as well as the company secretary, the then ILC General Counsel, Mr Paul Hayes. Also resolved on this date was that the ILC GM would be empowered to agree the contents of the Voyages constitution;
+ written resolution of the sole Member (the ILC) dated 13 December 2013 (share transfer provisions);
+ agenda- Board meeting April 20 2011 (including CVs of potential external directors, Deloitte remuneration report);
+ Board Decision paper for meeting 141- to approve amendments to the Voyages constitution (including the appointment of an associate director, the removal of the existing cap on director numbers, the amendment of the directors' maximum term to 5 years, and a change of company name to Voyages);
+ ATSI Act;
+ CAC Act;
+ CAC Regulations; and
+ miscellaneous guidance documents issued by DoFD in relation to the CAC Act.

Establishment of Voyages - ATSI Act and CAC Act considerations

Voyages was registered on 30 September 2010, having been established by resolution of the ILC Directors on 25 August 2010. The board further resolved on 1 October 2010 that Voyages would be the asset holding and operating entity of the ARR. The creation of a subsidiary was enabled by a formal arrangement in accordance with Section 191(G) of the ATSI Act, which sets out that ILC subsidiaries may perform functions corresponding to the ILC's functions.

In July 2010, prior to the establishment of Voyages, the ILC COO had sought legal advice from Corrs as to whether, among other things, the use of a subsidiary vehicle through which the ILC's statutory functions in respect of the ARR would be allowable under the requirements of the ATSI Act. Corrs concluded that *"Provided that such an arrangement is put in place either before or at the time the ARR (enters into the ARR purchase transaction) then….there will be compliance with section 191G(1)"*. Section 191G(1) of the ATSI Act sets out that ILC subsidiaries may perform functions corresponding to the ILC's functions. McGrathNicol has sighted confirmation of the Section 191G(1) arrangement having been entered into on 11 October 2010, prior to the ARR purchase transaction being entered into.

The Voyages constitution was prepared by Baker & McKenzie, and was based on a basic subsidiary template.

The Minister for FaHCSIA was advised of the establishment of Voyages on 10 August 2010, per the requirements of the CAC Act (Section 15(1), which requires a CAC body that forms a company must immediately inform their Minister of the proposal.

Conclusion- Compliance of Voyages establishment with ATSI Act and CAC Act

In establishing the Voyages entity for the purposes of the ARR transaction, it appears that the ILC has acted in accordance with the ATSI Act (section 191G(1) refers).

Additionally, in immediately notifying the Minister for FaHCSIA of the establishment of the subsidiary Voyages, the requirements contained in section 15(1) of the CAC Act appear to have been adhered with.

McGrathNicol examined whether the selection of Directors, including the length of their appointment and setting of their remuneration, was in accordance with normal practice. It does not appear that ILC Tourism (as a subsidiary) is bound by the CAC and ATSI Acts and their requirements for setting up a board of directors and constitution. Accordingly, we have considered the Voyages board appointments with reference to generally accepted best practice for Commonwealth entities, rather than CAC Act requirements.

Voyages board appointment requirements

McGrathNicol examined whether the selection of Directors, including the length of their appointment and setting of their remuneration, was in accordance with normal practice.

A Commonwealth Company is a company registered under the Corporations Act 2001 and which the Commonwealth "controls". Section 34 of the CAC Act defines the Commonwealth as controlling a company if, and only if, it:

+ controls the composition of the company's board (including through a veto power); or
+ has the ability to cast a majority of votes (more than one-half of the maximum number of votes) at a general meeting of the company's members; or
+ holds more than one-half of the issued share capital of the company and has the ability to cast a majority of votes (more than one-half of the maximum number of votes) at a general meeting of the company's members; or
+ holds more than one-half of the issued share capital of the company.

Voyages' status as a Commonwealth Company (or otherwise) is relevant in understanding the appropriate board appointment processes, noting that for a Commonwealth Company, the relevant Minister is responsible for appointing its Board.

Set out in the table adjacent is a number of references which indicate that Voyages does not appear to be a Commonwealth Company (and accordingly, not subject to a Minister-appointed board of directors).

Conclusion

Currently there is nothing to suggest that the Voyages subsidiary is bound by CAC Act/ATSI Act provisions as it relates to the implementation of a board of directors.

Accordingly, we have considered the Voyages director appointments, including the length of their appointment and setting of their remuneration, with reference to generally accepted best practice for Commonwealth entities, rather than against CAC Act or ATSI Act requirements. This analysis is set out in page 76 of this report.

Commonwealth Company considerations

Source	Reference	Excerpt	Comment
CAC Act	Section 7(2)(a)	"None of the following are Commonwealth authorities…. Corporations Act companies;"	This reference suggests that ILC Tourism is not a CAC body
CAC Act	Section 34	"In this Act, Commonwealth company means a Corporations Act company that the Commonwealth controls. However, it does not include a company that is a subsidiary of a Commonwealth authority or Commonwealth company."	This reference suggests that ILC Tourism, as a subsidiary of the ILC which is a recognised CAC body, is not a Commonwealth company.
ANAO "Corporate Governance in C'wealth Authorities and Companies"	Page 29	"….subsidiaries are not CAC bodies for the purposes of the CAC Act…"	This reference indicates that ILC Tourism, as a subsidiary, is not bound by CAC Act requirements relating to the board of directors appointments.

7.1 Voyages establishment and Director appointments

In April 2011, the ILC Board made a number of resolutions relating to its subsidiary Voyages which resulted in six new board appointments, a number of which were existing ILC Directors and/or employees. McGrathNicol considers that it would have been appropriate to make corresponding changes to the constitution to ensure ILC was able to maintain Voyages Board control in the instance that those individuals ceased their ILC directorships and/or employment.

Voyages Board of Directors

As set out on the previous page, it was resolved on 25 August 2010 that the Voyages entity would be established, with the following initial office holders:

- David Galvin (Director);
- David Baffsky (Director); and
- Paul Hayes (Secretary)

6 months later, once the ARR contract of sale had been executed and was approaching completion, an additional 6 individuals were nominated for appointment to the Voyages board. It was resolved in the ILC Board meeting of April 2011 that the nominees would be appointed to the Voyages Board of Directors.

Set out in the table below is a summary table which outlines the nomination process for each of the directors:

Voyages inaugural directorship nominations

Name	Appointment	CV supplied?	Nomination process
David Galvin	Aug-10	No	No external process. Nominated by ILC Chair.
David Baffsky	Aug-10	No	No external process. Nominated by ILC Chair.
Shirley Macpherson	Apr-11	No	The Board Briefing paper provides the following information regarding the nomination process for these directors: "After consultations with the Chairperson and Director, it is proposed that, subject to the ARR sale agreement proceeding to completion, the following persons are appointed as Directors of ILC Tourism" There is no documentation on file to suggest that the board positions were open or advertised to other applicants. This wording also suggets that ILC Chair Macpherson was instrumental in her own nomination to ILC Tourism (although noting that she abstained from the ultimate vote).
Geoff Dixon	Apr-11	Brief website biography print out, no CV supplied.	
Richard Longes	Apr-11	CV supplied.	
Peter Barge	Apr-11	CV supplied	
Ronald Moroney	Apr-11	CV supplied	

Voyages Board of Directors- continued

McGrathNicol considers that a Voyages Constitution that conforms to generally accepted good practice would (among other things) have been drafted to ensure that the Voyages Board was controlled by a majority of directors common to the ILC Board (or individuals employed by ILC).

In effect, that would require that an individual serving on both the ILC and Voyages boards (or serving on the Voyages board whilst employed by ILC) resign from Voyages in the event that the ILC directorship or employment ceases. Without this provision, a loss of control of the ILC Tourism board could occur, resulting in the following risks:

- loss of full and unfettered visibility by ILC over Voyages' activities;
- that disparity between the ILC's objectives and functions and Voyages' activities could occur;
- difficulty on the part of the ILC to demonstrate that the requirements of section 29 of the CAC Act are met, specifically, that *"a Commonwealth authority must ensure that none of its subsidiaries does anything that the authority does not itself have power to do".*

As set out in the adjacent table, the Voyages Constitution was amended in June 2011, approximately four months prior to new ILC Board members being appointed, extending the Voyages directors' maximum term from three years to five years.

The effect of this change was that, in the event that any of the ILC Directors Baffsky, Macpherson and Jeffries did not have their ILC directorship terms extended, they would nonetheless continue to serve the Voyages board, resulting in a board controlled by a majority of individuals external to the ILC. Additionally, as set out in the next page of this report, as external directors they would also be eligible for Voyages directors fees of at least $75,000 per annum.

7.1 Voyages establishment and Director appointments

In April 2011, the ILC Board made a number of resolutions relating to its subsidiary (Voyages). These resolutions resulted in six new board appointments with 5 year tenures, and a three year directors' fee pool of $1,477,500. The directors' fee pool approval was based on recommendations contained within a discussion paper prepared by Deloitte in March 2011.

Setting of remuneration

In April 2011, in addition to the appointment of directors, the Board of the ILC also considered a directors' fee pool for Voyages directors.

Prior to this Board meeting, the ILC had appointed Deloitte to provide advice regarding an appropriate director fee structure. Deloitte's recommendations of 18 March 2011 for Board remuneration were based on two elements:

+ an estimate of director workload, set relative to the total (assumed) fixed remuneration component of the Voyages Managing Director ($525,000); and
+ ASX benchmarks for companies of comparable scale and complexity, adjusted downwards to reflect the lowered governance risk of a private company.

Ultimately, a three year budget of $1,477,500 was approved, which represented the approximate midpoint of the Deloitte recommended range of fees.

ILC Tourism directors' fee pool

Position	Number of positions	Fees ($)	Annual ($)
Chairperson	1	150,000	150,000
Director	4	75,000	300,000
Committee Chair	2	21,250	42,500
Annual aggregated sum		246,250	492,500
Three year pool ($)			**1,477,500**

In accordance with section 194 of the ATSI Act, an ILC Director is entitled to remuneration and allowances. Notwithstanding this, it was proposed by the ILC Board that only externally appointed directors (i.e. Directors Dixon, Longes, Barge and Moroney who did not also hold positions on the ILC board) were approved for remuneration, in addition to the Chairman.

McGrathNicol examined whether the selection of Directors, including the length of their appointment and setting of their remuneration, was in accordance with normal practice. It appears that the processes followed in appointing the Voyages board did not align to generally accepted best practice for Commonwealth entities.

ILC Tourism inaugural board of directors appointments assessed against Better Practice

ANAO Better Practice	ILC Tourism
"Appointment processes should ensure that all statutory and administrative requirements are met and a wide range of suitable people are considered."	It does not appear that a panel of candidates was arranged to ensure that a wide range of suitable people were considered. It appears the directors were personally selected for consideration by either the ILC CEO, or the ILC.
"Decisions should be adequately documented."	Board minutes and packs do not adequately disclose how the directors were identified in the first instance, by whom, and the manner in which they were approached for an expression of interest.
"Consideration should be given to the skill requirements of the Board, and appointments made accordingly."	Board minutes and packs do not contemplate this issue. It is noted in the packs that the selected directors are of high calibre, however not documented is a record of their respective areas of relevant expertise.
"The Board should be consulted on the skills and experience it needs when new members are being considered for appointment."	As above.
"Directors should be subject to regular renomination, say every three years."	The constitution of Voyages was amended to allow directors' terms of 5 years. Whilst not applicable to Voyages, it is noted that the ATSI Act allows for terms of up to four years.
"All new directors should be provided with a letter of appointment setting out their duties and responsibilities."	No evidence has been located that this type of documentation was provided to new directors.
"Re-election should follow an agreed process to review the performance of directors."	Re-election has not yet occurred, therefore there has been no opportunity to demonstrate this, or otherwise.

Source: ANAO "Corporate Governance in Commonwealth Authorities and Companies Discussion Paper", May 1999 (page 20) and McGrathNicol analysis

Conclusions

Director appointment processes followed

Voyages is a wholly-owned subsidiary of a CAC body, and it is considered appropriate that decisions in relation to directorships are made with concern to generally accepted better practice for Commonwealth entities. Accordingly, we have analysed the director appointments with reference to ANAO Better Practice.

As indicated in the analysis set out in the table adjacent, it does not appear that the ILC Tourism director appointment process aligned with ANAO Better Practice. For the inaugural director appointments made in August 2010 and those in April 2011, McGrathNicol has not located any evidence to support that a range of suitable candidates were considered for appointment to the ILC Tourism board. The background behind how the directors were identified and on what basis has not been adequately documented on the files provided by ILC. The Board Briefing Paper of April 2011 states that "*the ILC is fortunate to have Directors of the calibre and experience of those recommended for appointment*". McGrathNicol does not disagree with this assertion, however notes that the nomination processes should be transparent and adequately documented.

Furthermore, there was no documentation located on file to demonstrate consideration of the skills required for the board, nor the specific skills of the individual directors. The ILC Board minutes indicate that appointment decisions were made without the benefit of comprehensive CVs for the candidates.

Term of appointment

Whilst section 191Z of the ATSI Act specifies that an ILC Director can not hold for a period in excess of four years, it does not appear that this applies to subsidiaries. The argument presented by the ILC for a 5 year appointment was that a longer term would provide organisational stability. Whilst this premise is not disputed, McGrathNicol considers it inappropriate that the Voyages Constitution of June 2011 did not contain a requirement that the Voyages Board was to be controlled by a majority of directors common to the ILC Board (or individuals employed by ILC). This gave rise to a number of unacceptable risks in relation to the operation of Voyages. We are advised that whilst a number of changes have been made to the Voyages Constitution since June 2011, it currently does not contain a requirement that its Board is to be controlled by a majority of directors common to the ILC Board (or individuals employed by ILC).

Fees

Fees were approved based on external advice received from Deloitte, with reference to market conditions. McGrathNicol has been provided with a copy of the Deloitte Director fees discussion paper dated 18 March 2011, and considers that the rationale for the fee pool ultimately approved appears sound.

Scope

In accordance with the consultancy agreement between the ILC and McGrathNicol of September 2013, the ILC has engaged McGrathNicol to undertake a forensic audit of the acquisition of ARR and establishment of Voyages.

The review requires McGrathNicol to examine all matters pertaining to the adequacy of the due diligence undertaken directly or on behalf of the then ILC Board in relation to the acquisition of the ARR and the establishment of Voyages. In particular:

1. Based on standard commercial norms, did the purchase represent value for money paid to the vendor, taking into account the GPT Capital Expenditure contribution; and the uplift payment?
2. Were the projections regarding capital refurbishment and maintenance requirements over the immediate, medium and longer terms realistic and appropriate?
3. Were the strategies adopted to mitigate the threats/risks identified at the time of purchase appropriate?
4. Were the projections regarding profitability and return on the investment appropriate and realistic given financial returns previously generated by previous owners of ARR and the then current and projected international and domestic tourism market across Australia and in central Australia in particular?
5. Were the loan arrangements negotiated with the vendor and the ANZ bank appropriate and undertaken at arm's length?
6. Were all the consultancies commissioned by the previous ILC Board consistent with ILC purchasing guidelines and generally accepted governance principles?
7. Was the advice and the valuation(s) provided by consultants realistic? It is expected that this may require seeking access and reviewing relevant working papers held by the consultants. The ILC will supply all necessary authorisations and releases to secure access to this information.
8. Was the advice provided by consultants followed by the previous ILC Board and reflected in the negotiations with the vendor and other relevant parties?
9. Based on available information, were the negotiations conducted in the best interests of the ILC?
10. Was the establishment of Voyages, selection of Directors, their length of appointment and setting of remuneration (in particular the arrangements made in relation to the then ILC Directors and CEO) in accordance with normal practice for a Commonwealth statutory body?
11. Was a transparent audit trail established that records ILC Board decisions and their implementation?
12. Were the appropriate declarations and recording of conflicts of interest by Directors and consultants made consistent with Commonwealth statutory guidelines?
13. Examine any other matters deemed relevant to providing an assurance to the Parliament that this purchase was in the best interests of the ILC and Indigenous people.

Documentation

In conducting the forensic audit we reviewed and relied on the following documentation concerning the acquisition of the ARR:

- ILC Board minutes, Board decisions and Board papers;
- Due diligence reports of consultants engaged to provide advice to the ILC in respect of the acquisition of the ARR;
- ILC policies and procedures;
- Relevant legislation including the ATSI Act and the CAC Act;
- Emails of ILC staff members and directors;
- Contracts and other correspondence relation to the engagement of consultants;
- Correspondence between the ILC and the Australian Government;
- The sale and purchase agreement for the ILC's acquisition of the ARR and related documentation;
- Financial models prepared by the ILC and Grant Samuel containing cashflow projections for the ARR;
- Industry reports;
- Independent valuations of the ARR;
- Loan documents, and related correspondence between prospective financiers and the ILC;
- Historical financial information for the ILC and the ARR;
- The project risk management plan and related documents;
- Settlement documents including correspondence related to the settlement adjustments;
- ASIC and other public searches of ILC directors; and
- Voyages financial information, Board minutes and Board papers.

McGrathNicol is aware of a review of the ILC's borrowing powers and guarantee limits commissioned by the Minister for FaHCSIA and undertaken by KPMG, and that this review was completed in early 2011. We have been advised that there is a limitation of the distribution of KPMG's report, and accordingly, it has not been provided to us.

Meetings

In the course of the engagement, McGrathNicol met with the following:

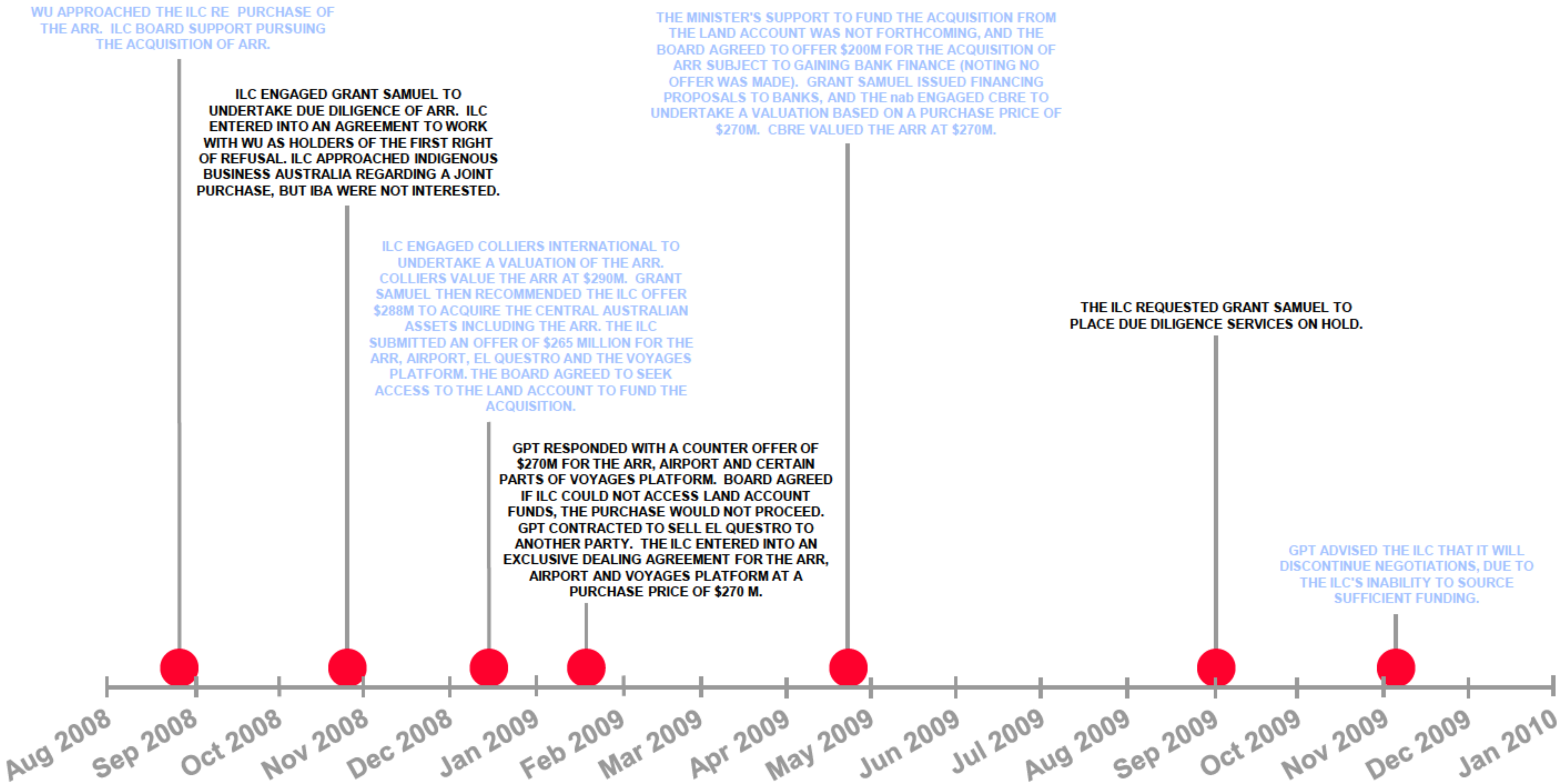
- Members of the current ILC Board including the current Chairperson;
- The current ILC Chief Executive Officer, Chief Operating Officer, General Counsel, and other ILC staff;
- Former ILC director, Mr. Kevin Driscoll;
- Former ILC director Mr. Max Gorringe;
- Current and Former* ILC director Mr. Ian Trust;
- Former ILC director Mr. David Baffsky; and
- Mr. Ross Grant, of Grant Samuel.

McGrathNicol also requested to meet with the following persons, though we either received no response, our request was declined, or the persons were unavailable.

- Former ILC Chairperson and former Voyages director, Ms. Shirley McPherson;
- Former ILC director Ms. Evonne Goolagong-Cawley;
- Former ILC Chief Executive Officer, Mr. David Galvin.

McGrathNicol also requested to meet with former ILC director and Voyages director Mr. Sam Jeffries, who provided a written response to our enquiries.

**Note: Director Trust was a member of the ILC Board at the time of the acquisition of the ARR, and continues to remain a member of the current ILC Board.*


WU APPROACHED THE ILC RE PURCHASE OF THE ARR. ILC BOARD SUPPORT PURSUING THE ACQUISITION OF ARR.
ILC ENGAGED GRANT SAMUEL TO UNDERTAKE DUE DILIGENCE OF ARR. ILC ENTERED INTO AN AGREEMENT TO WORK WITH WU AS HOLDERS OF THE FIRST RIGHT OF REFUSAL. ILC APPROACHED INDIGENOUS BUSINESS AUSTRALIA REGARDING A JOINT PURCHASE, BUT IBA WERE NOT INTERESTED.
ILC ENGAGED COLLIERS INTERNATIONAL TO UNDERTAKE A VALUATION OF THE ARR. COLLIERS VALUE THE ARR AT $290M. GRANT SAMUEL THEN RECOMMENDED THE ILC OFFER $288M TO ACQUIRE THE CENTRAL AUSTRALIAN ASSETS INCLUDING THE ARR. THE ILC SUBMITTED AN OFFER OF $265 MILLION FOR THE ARR, AIRPORT, EL QUESTRO AND THE VOYAGES PLATFORM. THE BOARD AGREED TO SEEK ACCESS TO THE LAND ACCOUNT TO FUND THE ACQUISITION.
GPT RESPONDED WITH A COUNTER OFFER OF $270M FOR THE ARR, AIRPORT AND CERTAIN PARTS OF VOYAGES PLATFORM. BOARD AGREED IF ILC COULD NOT ACCESS LAND ACCOUNT FUNDS, THE PURCHASE WOULD NOT PROCEED. GPT CONTRACTED TO SELL EL QUESTRO TO ANOTHER PARTY. THE ILC ENTERED INTO AN EXCLUSIVE DEALING AGREEMENT FOR THE ARR, AIRPORT AND VOYAGES PLATFORM AT A PURCHASE PRICE OF $270 M.
THE MINISTER'S SUPPORT TO FUND THE ACQUISITION FROM THE LAND ACCOUNT WAS NOT FORTHCOMING, AND THE BOARD AGREED TO OFFER $200M FOR THE ACQUISITION OF ARR SUBJECT TO GAINING BANK FINANCE (NOTING NO OFFER WAS MADE). GRANT SAMUEL ISSUED FINANCING PROPOSALS TO BANKS, AND THE nab ENGAGED CBRE TO UNDERTAKE A VALUATION BASED ON A PURCHASE PRICE OF $270M. CBRE VALUED THE ARR AT $270M.
THE ILC REQUESTED GRANT SAMUEL TO PLACE DUE DILIGENCE SERVICES ON HOLD.
GPT ADVISED THE ILC THAT IT WILL DISCONTINUE NEGOTIATIONS, DUE TO THE ILC'S INABILITY TO SOURCE SUFFICIENT FUNDING.
Aug 2008
Sep 2008
Oct 2008
Nov 2008
Dec 2008
Jan 2009
Feb 2009
Mar 2009
Apr 2009
May 2009
Jun 2009
Jul 2009
Aug 2009
Sep 2009
Oct 2009
Nov 2009
Dec 2009
Jan 2010

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Appendix 3 Acquisition Timeline – Early 2010 to Late 2010

FOLLOWING A MEETING BETWEEN GPT AND ILC DIRECTOR BAFFSKY, NEGOTIATIONS RECOMMENCE BASED ON GPT PROVIDING A LEVEL OF VENDOR FINANCE AND A $300M PRICE. GRANT SAMUEL PROVIDE AN UPDATED TRANSACTION PROPOSAL INCLUDING $162M FOR 54% OWNERSHIP ($81M ON COMPLETION, $81M DEFERRED TO 12 MONTHS AFTER @6.5% PA) AND A $138M PUT/CALL OPTION AFTER FIVE YEARS FOR THE REMAINING 46% PLUS A VALUATION UPLIFT (MIN $12M) AND 6.5% COUPON ON THE REMAINING 46% FOR FIVE YEARS.

ONGOING NEGOTIATION BETWEEN ILC AND GPT REGARDING PARTICULAR ELEMENTS OF THE TRANSACTION STRUCTURE.

GS PROVIDES UPDATED TRANSACTION PROPOSAL TO THE ILC BOARD $162M FOR 54% OWNERSHIP ($81M ON COMPLETION, $81M DEFERRED TO 12 MONTHS AFTER @6.5% PA) AND A $138M PUT/CALL OPTION AFTER FIVE YEARS FOR THE REMAINING 46% PLUS A VALUATION UPLIFT (MIN $17M) AND 6.5% COUPON ON THE REMAINING 46% FOR FIVE YEARS. ILC AGAIN APPROACHED IBA TO PARTNER IN THE PURCHASE, AND THE IBA DECLINED. GRANT SAMUEL SOUGHT $60M FINANCING PROPOSALS FOR CAPITAL EXPENDITURE FROM ANZ, CBA, NAB AND WBC

HEADS OF AGREEMENT ENTERED INTO FOR ARR AND VOYAGES, EXECUTED BY ILC GENERAL MANAGER.

ILC BOARD AGREES TO OFFER WU 3% OWNERSHIP. WU NEGOTIATES FOR 7% OWNERSHIP WITH ILC.

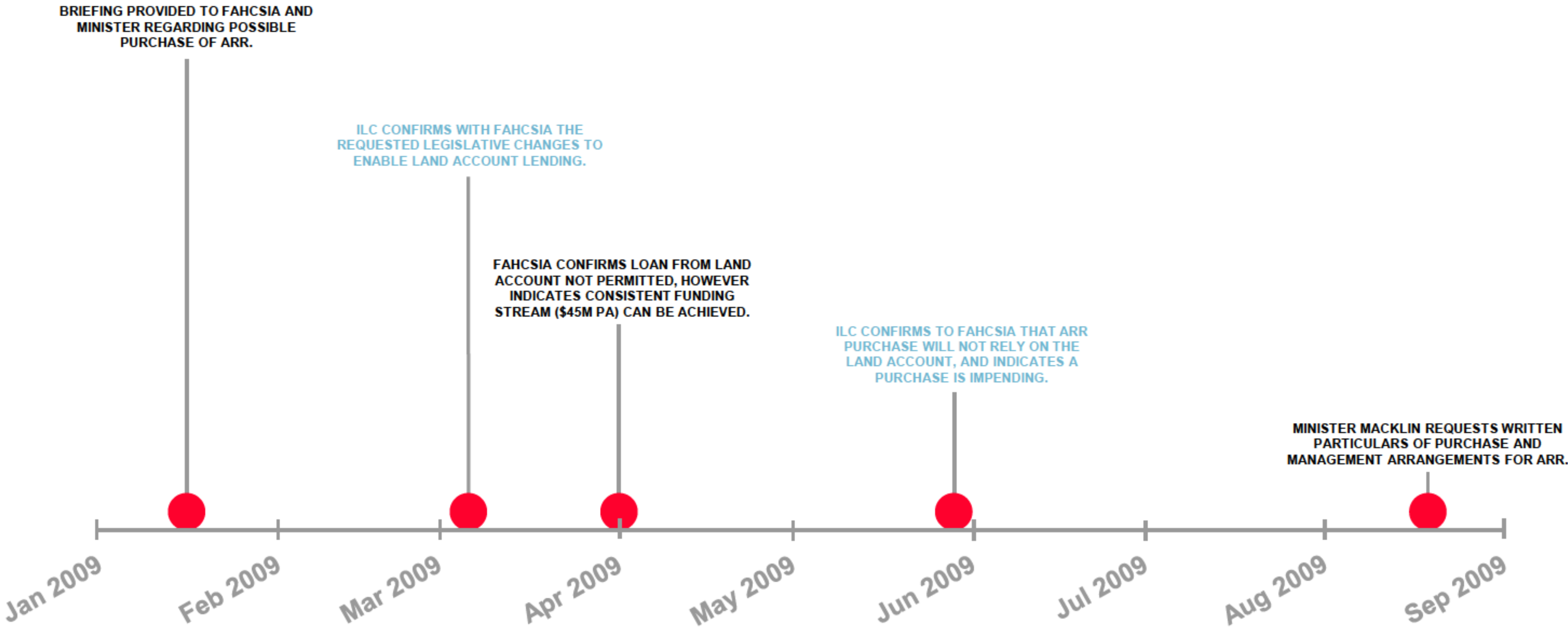
FOLLOWING THE RECEIPT OF THE HORWATH DUE DILIGENCE REPORT, ILC RAISES CONCERNS OVER RECENT TRADING RESULTS AND PROPOSE AN AMENDED SALE PRICE OF $270M TO GPT. GPT DECLINE THE REVISED OFFER, AND THE ILC CONTINUE TO SEEK TO NEGOTIATE THIS WITH GPT. ANZ IS SELECTED AS THE PREFERRED FINANCIER IN RELATION TO THE $60M CAPITAL EXPENDITURE FINANCE.

THROUGH NEGOTIATIONS WITH GPT REGARDING CONTINUING CONCERNS OVER RECENT TRADING RESULTS, THE ILC AGREE A NET $292M PURCHASE PRICE WITH GPT FACE PRICE OF $300M PAID THROUGH $81M ON COMPLETION, $81M DEFERRED TO 12 MONTHS @6.5% PA, 138M DEFERRED TO FIVE YEARS @6.5% PA, A MINIMUM VALUATION UPLIFT $17M AND GPT TO PROVIDE $25M CAPITAL CONTRIBUTIONS OVER FIVE YEARS.

GRANT SAMUEL PROVIDE A PRESENTATION TO THE ILC BOARD INCLUDING A $292M NPV VALUATION OF ARR CASHFLOWS, RECOMMENDATION THAT THE "ILC PURCHASE ARR AND THE VOYAGES PLATFORM ON THE TERMS PROPOSED". THE ILC BOARD RESOLVED TO PURCHASE ARR.

SPA EXECUTED.

Mar 2010 | Apr 2010 | May 2010 | Jun 2010 | Jul 2010 | Aug 2010 | Sep 2010 | Oct 2010 | Nov 2010


BRIEFING PROVIDED TO FAHCSIA AND MINISTER REGARDING POSSIBLE PURCHASE OF ARR.
ILC CONFIRMS WITH FAHCSIA THE REQUESTED LEGISLATIVE CHANGES TO ENABLE LAND ACCOUNT LENDING.
FAHCSIA CONFIRMS LOAN FROM LAND ACCOUNT NOT PERMITTED, HOWEVER INDICATES CONSISTENT FUNDING STREAM ($45M PA) CAN BE ACHIEVED.
ILC CONFIRMS TO FAHCSIA THAT ARR PURCHASE WILL NOT RELY ON THE LAND ACCOUNT, AND INDICATES A PURCHASE IS IMPENDING.
MINISTER MACKLIN REQUESTS WRITTEN PARTICULARS OF PURCHASE AND MANAGEMENT ARRANGEMENTS FOR ARR.
Jan 2009
Feb 2009
Mar 2009
Apr 2009
May 2009
Jun 2009
Jul 2009
Aug 2009
Sep 2009

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Appendix 4 Timeline of Ministerial Correspondence – Mid 2010 to Early 2011