13 August 2009

Hilton Denarau Owners Committee
c/- Knott & Associates
286 Maribyrnong Road
Moonee Ponds, Victoria 3039
AUSTRALIA

Attention: **Trevor Rogan**

Email: **lucky.jim@clear.net.nz** ***By Post and by Email***

HILTON DENARAU – CONTROL ISSUES

You have sought our assistance with identifying the legal position of the owners of villas (Villas) in the Hilton Denarau Resort on Denarau Island in Fiji (Resort), in relation to the developer of the Resort, Denarau Investments Limited (Developer) and the Developer's contracted manager of the Resort, Denarau International Limited (DIL). In particular, you have asked us to advise you as to:

- **the Owners' legal position in relation to Neville Mahon, the Developer, DIL and their related parties; and**
- **how the future management of the Villas and the operation of the Resort might be facilitated in the best interests of the Owners, having regard to the existing interests of Hilton Hotels (Hilton) and the Resort's financiers.**

This opinion is provided solely for the benefit of the Villa Owners Association which you and other Owners have formed (VOA) and should not be passed on to, or relied on by, anyone else without first checking with us.

INTRODUCTION

1. **We have based our opinion on the following documents provided to us by you prior to the date of this opinion, namely:**

   1.1 **Agreement for the grant of a Title Lease, construction of a Villa and purchase of Fittings, Fixtures & Equipment (FF&E) between each Owner and the Developer (Villa Sale Agreement).**

   1.2 **Title Lease between the Developer and each Owner (Title Lease).**

   1.3 **Management Agreement, providing for the management of Villa 10H in the Resort, between Wayne Foster and Rachael Rogan as trustees of the Bula Trust (Bula Trust) and DIL, the term of which commenced on 8 June 2006 (Owner Management Agreement).**

   1.4 **Correspondence between members of the VOA, including letters sent by Graeme Knott, and DIL and its representatives (including meeting notes).**

   1.5 **Internal VOA and Owners' correspondence.**

   1.6 **Fijian legal correspondence and pleadings.**

1.7 Correspondence between VOA (including letters sent by Graeme Knott) and Ernst & Young.

1.8 Correspondence between VOA (including letters sent by Graeme Knott) and Hilton Hotels, Sydney.

1.9 Documents and correspondence relating to the position of Strategic Finance Limited and its related entities (Strategic).

1.10 Documents and correspondence relating to the potential appointment of receivers of DIL.

1.11 Miscellaneous correspondence, information and media clippings.

2. We have also carried out limited research to the extent possible from our office, including:

2.1 Searches of the New Zealand Companies Office.

2.2 Internet Searches.

2.3 Debtor searches of Neville Mahon and his related New Zealand entities on the Personal Property Securities Register (in New Zealand).

3. We are aware of the following key contracts that we have been unable to procure copies of:

3.1 Agreement for the management of the Resort between the Developer (as appointor) and DIL (as manager) (DIL Management Agreement).

3.2 Agreement for the operation of the Resort between DIL and Hilton (Hilton Agreement).

4. Our legal analysis is predominantly focussed on an interpretation of the parties' contractual position, with a special focus on the Owner Management Agreement, given that the Owners' main concern is with the treatment of Villa income by DIL as governed by that Agreement.

5. We are not qualified Fijian legal advisors and, as the relevant contracts are all expressed to be subject to Fijian law, and most of the relevant events occurred in Fiji, we defer to the advice of your Fijian legal advisers in relation to any specific issues of Fijian law.

EXECUTIVE SUMMARY

6. We attach diagrams showing:

6.1 our understanding, based on the material provided to us, of the current operation of the Resort;

6.2 the corporate structure of the various related companies of Neville Mahon; and

6.3 the new structure for the Resort proposed by Graeme Knott.

7. It appears that Neville Mahon has created an overall structure whereby:

7.1 entities that Neville Mahon controls and owns (or at least in which he owns or controls a majority shareholding) sit (contractually) between the Native Land Trust Board, the Owners, the Resort operator (Hilton) and the Resort financiers, with the result that none of those parties have any direct contractual relationship with any of the others;

7.2 the Owners have no contractual relationship with each other and are not part of any Owners' representative body, that is to say, there is no "body corporate" entity; and

7.3 there are a myriad of ways in which Villa income can be directed into entities owned or controlled by Neville Mahon and, given the contractual structure, Owners have no available means of monitoring such activities.

8. In our view, Neville Mahon, the Developer and DIL are likely to be liable to the Owners in various respect, including (without limitation):

8.1 various breaches by DIL of the Owner Management Agreement;

8.2 various misrepresentations made by the Neville Mahon, the Developer and DIL to Owners and prospective Villa purchasers; and

8.3 the current structure provides Neville Mahon and his various associated entities with an ability to divert Villa income to themselves in various ways. We cannot tell whether all payments to those entities have been made in good faith and that can not be ascertained without a thorough understanding of the various flows of funds to those entities during the relevant periods.

9. The remedies available to the Owners under the Owner Management Agreement are limited, essentially, to recovery of debts owing to them by DIL. Importantly, the Owners are not entitled to terminate the Owner Management Agreement for breaches by DIL.

10. To the extent that Neville Mahon and the Developer have, in New Zealand, knowingly provided prospective Villa purchasers (who have subsequently become Owners) with untrue information regarding the Resort, those Owners are likely to be entitled to remedies in New Zealand under the Fair Trading Act 1986, the Contractual Remedies Act 1979 or both.

11. There is a risk that, whatever remedies might be available to Owners against Neville Mahon and his related entities, there may be little actual funds held by any of those entities by which successful claims may be satisfied.

12. Because of the limitations upon the remedies available to the Owners under the Owner Management Agreement, and the fact that there may be little actual funds available to satisfy any remedies that the Owners might be entitled to, in our view the most sensible approach at this stage is for the Owners to encourage the Resort financiers and Hilton Hotels to take steps to remove control of the Resort from Neville Mahon and his related entities, and enter into satisfactory arrangements with the Owners under which the Owners are properly represented, the financiers are repaid, construction of the Resort is completed and Hilton is able to operate the Resort into the future.

13. It may be that, once Neville Mahon and his entities are removed, a better picture will emerge indicating that some form of recovery action against those entities or Neville Mahon personally might be initiated. However, on the information available to us that does not appear the optimal course at this stage.

VILLA REVENUE & FORCE MAJEURE

Owner Management Agreement

14. Please note that, where we have used italicised terms in this opinion, we are referring to such terms as they are defined in the relevant Resort document.

15. The Owner Management Agreement provides for the income earned in respect of each individual Villa, in respect of each quarter, to be treated as follows:

15.1 Guests pay room rates to DIL (not to Hilton).

15.2 From this income DIL deducts amounts applicable to *Ancillary Services* (being goods or services provided to guests, at guests' cost, incidental to the use of the Villa). It is implicit that DIL pays the amount of such deductions to the suppliers of the *Ancillary Services*. The remaining amount of income is the *Accommodation Revenue* applicable to that Villa.

15.3 An amount equal to the *Specified Percentage* of the *Accommodation Revenue* (the *Retention Amount*) is to be applied in payment of the *Operating Costs*[1], which include, along with numerous other items, the following:

(a) Hilton's management fees.

(b) DIL's management fee which, when aggregated with the same allocation from all other Villas in the Resort, is to comprise an amount equal to 10% of the aggregate *Accommodation Revenue* earned in respect of all Villas in the Resort.

(c) Various other outgoings which could result in funds being directed to DIL or Lausanne Project Management Limited[2], a company of which Neville Mahon is sole director and effective majority shareholder (Lausanne).

The Owner Management Agreement does not provide for any other amounts taken from the *Accommodation Revenue* to be paid to Hilton or DIL.

15.4 The remainder of the of the *Accommodation Revenue* after the deduction of the *Retention Amount* is the *Villa Revenue*.

15.5 DIL is entitled to make the following deductions from *Villa Revenue*:

(a) Rent and other amounts payable by the Owner to the Developer under the *Title lease* (the Owner authorises DIL to administer such payments). This is clearly an important method by which the Developer derives ongoing revenue from the Villas.

(b) Costs of maintaining insurances in accordance with clause 12 of the Owner Management Agreement.

15.6 Finally, DIL is to pay the remainder of the *Villa Revenue* to the Owner.

Hilton Agreement

16. It appears that the Hilton Agreement provides for Hilton to receive a share of profits earned by the Resort and that, instead of Hilton charging a "management fee" which is deducted by DIL from the *Accommodation Revenue* and paid to Hilton as part of the *Operating Costs*:

16.1 Hilton's fee comprises 2% of the gross income of the Resort, together with a further 8% of the net profit of the Resort once that is determined; and

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[1] **The Owner Management Agreement makes no provision for the scenario where the Retention Amount is more than sufficient to cover the Operating Costs. Presumably the result of that scenario would be a profit for DIL. In any event the definition of Operating Costs allows for an extremely wide range of potential costs to be applied by DIL, and it may be unlikely that the *Operating Costs* would ever be less than the *Retention Amount*.**

[2] **11. A letter dated 1 May 2009, sent by DIL to the Owners, included a diagram indicating that Lausanne provides "management, accounting and administrative services" to each of DIL and the Developer. We assume that the *Operating Costs* included payments to Lausanne.**

16.2 it seems likely that Hilton controls the treatment of villa income up to the stage at which Hilton's fees have been paid[3].

17. Graeme Knott has also advised that Hilton has applied funds from the *Denarau International Limited (Hilton Managers Account)* towards costs of construction of the Resort, to enable certain essential services to be provided to the Resort. Neither DIL nor Hilton are entitled to apply Resort income towards construction costs of the Resort.

Actual treatment of Villa income

18. It seems likely that DIL and Hilton have actually treated Villa income as follows:

18.1 The income earned by each Villa is paid into an account named *Denarau International Limited (Hilton Managers Account)* – it seems likely that this account is controlled by Hilton.

18.2 Hilton then:

(a) deducts 2% of all gross amounts paid into such account as part of its fee; and

(b) deducts, from the remainder, operating expenses of the Resort (we do not know to what extent such operating expenses include the *Operating Expenses* specified in the Owner Management Agreement),

to arrive at a "net profit" figure;

(c) deducts 8% of that "net profit" as part of its fee; and

(d) pays the remaining amount to DIL.

18.3 DIL may then make certain further deductions before paying the Owner the remainder.

19. At some point during the above process, either Hilton or DIL presumably calculates the figures for the *Accommodation Revenue*, the *Retention Amount*, the *Operating Costs* and the *Villa Revenue* in terms of the Owner Management Agreement. Further, it is not clear at what stage in the process Hilton or DIL actually makes the deductions of amounts payable by the Owner to the Developer under the Title lease, and the costs of maintaining insurances in accordance with clause 12 of the Owner Management Agreement.

20. It has also been alleged that Hilton has been paid or deducted, from villa income at some stage in the above process, repayments of amounts it has advanced to DIL and the Developer towards Resort development and construction costs.

21. If the process set out at paragraph 18 above reflects the reality, then DIL is in clear breach of its obligations as to treatment of Resort income under the Owner Management Agreement.

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[3] There is some confusion as to whether DIL or Hilton controls the account into which villa income is paid:

- **DIL's legal advisors Munro Leys asserted in a letter dated 2 July 2009 that Resort income is received and controlled by DIL and not Hilton and that "*there is no surplus after paying operational costs of the Resort*". Given that *Operational Costs* include the management fees of both Hilton and DIL, that statement is of limited assistance.**
- **In a letter dated 3 June 2009, Strategic Finance Limited stated that "*DIL have no influence over the Hotel accounts…the trading account of the Hotel…is controlled by Hilton*".**

Non-Payment

22. Initially, the *Specified Percentage* was set at 50% of *Accommodation Revenue*.

23. It is clear that towards the end of 2008 DIL's method of operating the Resort and accounting for revenues and costs (whatever the actual detail of that method was) became impossible for DIL to maintain. It is reasonable to infer that low Villa income due to various external factors outside of DIL's control might have contributed to that. The extent to which those external factors caused the problem is, however, impossible to ascertain without thorough knowledge of all receipts and payments of Hilton, DIL, the Developer and Lausanne relating to the Resort during the relevant periods, in order to identify precisely how Villa income was disposed of.

24. The inherent conflict between the arrangements DIL has with Hilton and with the Owners must have, in our view, also contributed to the problems experienced by DIL.

25. DIL's solution to the problem was to:

25.1 withhold payment of any *Villa Revenue* to Owners in respect of the 4th quarter of 2008 (without taking any proper steps to comply with the Owner Management Agreement); and

25.2 subsequently increase the *Specified Percentage* to 100%, allegedly to cover the *Operating Costs*, claiming that it was entitled to do so under clause 5.3 of the Owner Management Agreement due to the occurrence of *Force Majeure Events*.

We have considered, by reference to DIL's actual rights and obligations under the Owner Management Agreement, whether DIL was entitled to take such actions.

Relevant Provisions

26. Clause 4.1 of the Owner Management Agreement obliges DIL to pay the *Villa Revenue* to the Owner by quarterly instalments in arrears.

27. The following provisions of the Owner Management Agreement provide DIL with the ability (in certain specified circumstances) to vary the amount, or suspend payment of, *Villa Revenue*:

27.1 Clause 5.2 enables DIL to vary the *Specified Percentage* in relation to a quarter where *Hotel Operating Costs* actually exceed the *Retention Amount* for at least the two consecutive preceding quarters, and DIL's auditor confirms that such will be the case for the following quarter. Such variation can only be to the extent that the *Retention Amount* is approximately equal to the *Hotel Operating Costs* for the upcoming quarter, and no such variation can be made at any time prior to the expiry of three years from the *Commencement Date* (by way of example, in the case of the Owner Management Agreement between DIL and the Bula Trust, such period expired on 6 June 2009).

27.2 Clause 5.3 enables DIL to vary the *Specified Percentage* in relation to a quarter where *Force Majeure Events* occur, during the period of occurrence of such events. Such variation can only be to the extent that the *Retention Amount* is approximately equal to the *Hotel Operating Costs* for the upcoming quarter, but can be made at any time upon 2 days' written notice.

27.3 Clause 11.4(a) enables DIL to deduct amounts from *Villa Revenue* where it becomes necessary to replace or repair the *FF&E* in the Villa as the result of a *Force Majeure Event* or any other extraordinary event.

27.4 Clauses 15.2 and 15.4 provide for the abatement of *Villa Revenue* where the Villa, the common property or the *Core Hotel Facilities* are destroyed, damaged such that they are a total loss, or condemned.

27.5 Clause 16 sets out various rights of DIL to withhold or set off *Villa Revenue* where the Owner or its guests or invitees are in breach.

Withholding of 2008 4th quarter *Villa Revenue*

28. On 18 February 2009, DIL wrote to all Owners, notifying them that the operation of the Resort had been adversely effected by various events and that, as a result of such events, and due to the need to "*maintain prudent levels of cash to meet the operating costs through these difficult trading conditions*", the Villa revenue due to Owners in respect of the quarter ending 31 December 2008 would not be paid. Such non-payment was purportedly to apply until the completion of an assessment of "*cashflow requirements for the Hotel for the balance of this year and next*".

29. None of clauses 5.2, 5.3 11.4(a), 15.2, 15.4 or 16 permit DIL to arbitrarily withhold payment of *Villa Revenue* altogether, as DIL did in relation to *Villa Revenue* for the 4th quarter of 2008. On the face of it, DIL is therefore in clear breach of clause 4.1.

30. However, clause 21.1 of the Owner Management Agreement provides that:

> ***Neither party will be liable for any delay or default in the performance of its respective obligations under this agreement if such delay or default is caused by or arises out of any Force Majeure Event.***

It may be that DIL considers that *Force Majeure Events* were already occurring during the 4th quarter of 2008, although it did not specifically seek to rely upon clause 21.1 when withholding the relevant payments.

31. A very important question, as regards the withholding of *Villa Revenue* for the 4th quarter of 2008, is whether any portion of the *Operating Costs* paid during that period was in fact applied for the benefit of companies in which Neville Mahon has an interest (whether DIL, the Developer or Lausanne). We cannot find an answer to that question in the material we have been provided. In our view, a thorough independent audit of the accounts of Hilton, DIL, the Developer and Lausanne during the relevant period is the only way by which that question could be satisfactorily answered.

Variation of the *Specified Percentage*

32. On 26 March 2009, DIL again wrote to all Owners, this time estimating that, in respect of the first quarter of 2009, *Hotel Operating Costs* would exceed the estimated *Retention Amount* due to the ongoing occurrence of certain *Force Majeure Events* and, as such, DIL would exercise its right under clause 5.3(a) of the Owner Management Agreement and increase the *Specified Percentage* from 50% to 100%, leaving no *Villa Revenue* available for payment to Owners. DIL further stated in that letter that it expected the *Force Majeure Events* to continue for the duration of 2009 and possibly longer.

33. Again, the obvious question that arises is: what were the *Operating Costs* during that period and to whom were they paid? We are unable to answer that question based on the information available.

34. Lowing, Nandan and Associates, in their written advice to Trevor Rogan dated 11 June 2009, has expressed the opinion that, with respect to the events and occurrences that DIL has specifically claimed were *Force Majeure Events*, only the floods of January 2009 could possibly fall within the definition of *Force Majeure Events*. We can see no reason to disagree with that view.

35. As regards the withholding by DIL of the 2008 4th quarter *Villa Revenue*, in our view DIL was clearly in breach of clause 4.1 of the Owner Management Agreement. The January 2009 floods had not even occurred at that stage and, in any event, no legal or contractual justification was even provided by DIL for that action in its letter dated 18 February 2009.

36. DIL did not seek to rely upon the occurrence of *Force Majeure Events* to justify its actions until its letter of 26 March 2009, where it cited such events in support of its variation of the *Specified Percentage*. As only the floods of January 2009 could possibly fall within the definition of *Force Majeure Events* and (as Lowing, Nandan and Associates have pointed out) the January 2009 floods ceased long before DIL sought to rely upon them in support of its actions, we do not consider that DIL is entitled to rely upon clause 5.3 to increase the *Specified Percentage*.

37. We also note that, where DIL seeks to rely upon any *Force Majeure Event*:

37.1 pursuant to clause 21, DIL must give prompt notice of the occurrence of any *Force Majeure Event* that is affecting DIL's performance under the Owner Management Agreement; and

37.2 where DIL seeks to rely upon any *Force Majeure Event* to justify an adjustment to the *Specified Percentage* under clause 5.3, DIL must give prompt notice of the cessation of that *Force Majeure Event*.

In this case, DIL did not give prompt notice the 2009 January floods, or any of the other so-called *Force Majeure Events* upon which it seeks to rely, when they occurred. Further, DIL did not give prompt notice of the cessation of any such events.

38. Had it given the proper notice and certification from its auditor then, following the expiry of 3 years from the commencement date of each Owner Management Agreement, DIL would have been entitled to adjust the *Specified Percentage* in accordance with clause 5.2 without reference to any *Force Majeure Event*. However, we are not aware of any evidence that it did so.

Misallocation of Resort income

39. It further appears that DIL and the Developer have looked to Hilton to assist financially with certain development costs of the Resort. Hilton have (as we understand it) looked to deduct repayments of such advances from Villa income before remitting any income to DIL for distribution to Owners.

40. We are not aware of the provisions of the Hilton Agreement, but DIL is certainly not entitled under the Owner Management Agreement to allocate Villa income to Resort development or construction costs. If Villa income has been diverted to cover those costs (whether as repayments of advances made by Hilton or otherwise) then that would constitute a clear breach of clause 4.1 of the Owner Management Agreement and the provisions of the Owner Management Agreement providing for the calculation of the *Accommodation Revenue*, the *Retention Amount* and the *Villa Revenue*.

41. Because of the manner in which *Operating Costs* are calculated and paid, and the ability for DIL and Lausanne to be paid fees from Resort income, there is at least a possibility that funds have been diverted to DIL and Lausanne other than in good faith for valuable services rendered.

Breach of Owner Management Agreement

42. The reality of the situation may well be that, as DIL claims, Villa income simply has not been sufficient to cover the actual operating expenses of the Resort, so that no profits have been available (however calculated) for distribution to Owners. In terms of DIL's obligations

under the Owner Management Agreement, however, for the reasons set out above we are of the view that:

42.1 DIL was and is prohibited, under the Owner Management Agreement, to treat Resort income differently to the manner contemplated in that agreement;

42.2 in withholding payment of the *Villa Revenue* for the 4th quarter of 2008, DIL is in clear breach of clause 4.1 of the Owner Management Agreement;

42.3 DIL is not entitled to rely upon any *Force Majeure Event* in support of any of the actions it has taken as regards the *Villa Revenue*;

42.4 because DIL was not entitled to adjust the *Specified Percentage* (so as to deprive Owners of *Villa Revenue* since the beginning of 2009), the proper *Specified Percentage* should be treated as having remained at 50% (at least until the expiry of 3 years from the commencement date of each Owner Management Agreement);

42.5 had it given the proper notice and certification from its auditor then, following the expiry of 3 years from the commencement date of each Owner Management Agreement, DIL would have been entitled to adjust the *Specified Percentage* in accordance with clause 5.2; and

42.6 DIL is therefore in breach of clause 4.1 of the Owner Management Agreement with respect to:

(a) its failure to treat Resort income in the manner contemplated in the Owner Management Agreement so as to arrive at the correct figure for *Villa Revenue*; and

(b) its failure to pay any *Villa Revenue* to Owners from the beginning of 2009 (at least up until the expiry of 3 years from the commencement date of each Owner Management Agreement, if not, as seems more likely, up to the present date).

43. Further, if it could be established that any funds have been improperly paid out of Resort income to DIL or Lausanne, then claims might be brought against those parties for fraud and breach of contract. That would be a very serious allegation, however, and cannot be established without a thorough disclosure of the accounts of those companies.

Insurance

44. According to notes taken at a meeting dated 24 June 2009, Neville Mahon stated at that meeting that insurance claims had been lodged with respect to the so-called *Force Majeure Events*. That should be followed up as, presumably, such claims may result in funds being available to be applied to *Villa Revenue*.

AUDITS AND REPORTING OBLIGATIONS

DIL obligations

45. Clause 6 of the Owner Management Agreement requires DIL to provide certain information to Owners, including:

45.1 Monthly statements (clause 6.1);

45.2 audited annual reports (clause 6.2); and

45.3 tax information within 3 months of the end of each financial year.

46. We understand that DIL has failed to comply with these obligations in several respects, however, we have not been provided with detailed information as to specific breaches in this regard.

Ernst & Young audit

47. Ernst & Young provided an "Independent Audit Report" dated 26 June 2009, being a one page letter. That audit was (according to Ernst & Young) commissioned by Hilton, and based on hotel financial information generated by Hilton and presented to DIL. The relevant part of that opinion stated that, in Ernst & Young's opinion, forecast hotel operating costs will exceed the *Retention Amount* for the period from 1 April 2009 to 30 June 2009, so that the *Retention Amount* for that period will be insufficient to pay such operating costs.

48. The difficulty with Ernst & Young's opinion is that (as we understand it) it was prepared within strict parameters, and was prepared on the basis of limited information. It does not deal with fundamental issues, such as whether the calculation of *Operating Costs* for the purposes of its opinion included fees payable to Hilton, DIL or Lausanne. It does not provide any real assistance in understanding how Resort income has in fact been received and treated by DIL and Hilton from time to time.

49. Accordingly, very little of practical use can be made of the Ernst & Young opinion. That is not a reflection on Ernst & Young at all; it simply follows from the limited scope of their instructions and a failure by DIL (we assume) to brief them on the issues we have identified above.

DEBTS, SECURITIES, INSOLVENCY & VAT

Strategic

50. It has been established that:

50.1 the Developer has granted a mortgages over its interest in the head lease of the Resort land to Strategic Nominees Limited (a wholly owned subsidiary of Strategic Finance Limited) (Strategic);

50.2 the Developer has granted debentures over its assets to Strategic, Credit Corporation (Fiji) Limited, Elders Finance Limited, Madison Trust Limited and South Canterbury Finance; and

50.3 DIL has granted a debenture over its assets to Strategic. Strategic has stated that such debenture encumbers (among other assets) Villa income. To the extent that Villa income is not the property of DIL, we do not consider that Strategic's claim in that regard is correct. In terms of the Owner Management Agreement, DIL only has a proprietary right to 10% of the aggregate *Accommodation Revenue*, such amount being payable to it by way of management fees.

51. We are not aware of any contractual provisions (contained in the Owner Management Agreement or elsewhere) prohibiting DIL or the Developer from granting such securities. However, if any action taken by the securityholders places DIL in breach of any of its contractual obligations to the Owners then DIL will be liable to the Owners for any such breaches.

52. In correspondence with the Owners, you have advised that DIL and the Developer have admitted to being unable to pay their debts. If such is the case, then we would have expected that the terms of the arrangements between DIL, the Developer and Strategic will

almost entitle Strategic to appoint receivers over the assets and undertakings of DIL and the Developer.

Insolvency

53. If DIL and/or the Developer are insolvent in terms of Fijian law, then we would have expected that the directors of those companies will be exposed to personal liability if they continue to cause those companies to trade. Your Fijian advisers will be in a better position than us to confirm that legal position.

VAT

54. We note your letter to the other Owners of 30 June 2009, advising that certain Owners had received demands from the Fiji Islands Revenue and Customs Authority for payment of VAT tax in respect of income earned by their units.

55. Pursuant to clause 2.3 of the Owner Management Agreement, DIL is liable to pay to each Owner any and all VAT payable in respect of any taxable supply made by the Owner. It appears the DIL has failed to do so and DIL is therefore in breach of that provision.

MISREPRESENTATION & BREACH OF PROSPECTUS

56. It seems clear that the Developer, DIL and/or Neville Mahon and others made (and continue to make) numerous representations to prospective purchasers of Villas in the Resort from time to time.

57. Many of those representations have subsequently failed to prove correct. A misrepresentation generally occurs at law where the person making the representation misrepresents a fact (representations as to a future intention, provided the intention is genuine, are legitimate even if the intention is later unable to be fulfilled).

58. An employee of our firm obtained advertising and promotional material from the Developer on 12 August 2009 including a number of representations which appear to be incorrect. For example, the material provided by the Developer contains a representation that Owners will receive 50% of Villa income. Given the current circumstances, that appears to be a clear misrepresentation and, on the face of it, we would expect that any person who purchased a Villa in reliance on that representation (and subsequently received less than the stated 50% of Villa income) might have an actionable claim against the Developer.

59. However, we have not seen the form of agreements documenting the purchase of Villas in the Resort and we would expect that those documents will contain numerous exclusions and disclaimers as regards representations made by the Developer. In considering any action for misrepresentation (which we assume would be the domain of your Fijian legal advisors) all relevant documents, contracts and aspects of Fiji law would need to be considered. We do not propose to explore those issues further in this opinion.

60. Promotional material released by the Developer as late as 12 August 2009 contains a statement that the Resort was designed by "*Lausanne Project Management, architects from Sydney, Australia*". We have investigated this statement and found that:

60.1 The website www.resortfiji.com states that *Lausanne Project Management Ltd of Auckland, New Zealand has acted as advisor and overseas design liaison for this development*.

60.2 We are not aware that Lausanne has ever have been regarded as a Sydney architectural firm.

60.3 Lausanne is in fact a New Zealand registered company, solely directed by Neville Mahon and owned by Montreux Trust Limited.

60.4 Montreux Trust Limited is a New Zealand registered company, directed and owned by Neville Mahon and Stewart Mahon. Neville Mahon holds a 51% shareholding in Montreux Trust Limited.

60.5 DIL sent a letter to Owners on 1 May 2009, in which DIL stated that Lausanne provides "*management, accounting and administrative services*" to each of DIL and the Developer.

It appears that, rather than being a Sydney-based firm of architects, Lausanne is in fact a New Zealand company controlled by Neville Mahon (and owned by a company of which he is the majority shareholder), which exists to provide various unspecified services to DIL and the Developer, presumably in return for payment of fees. The statement about Lausanne contained in the Developer's promotional material is therefore misleading.

61. We could not find, in any of the promotional material relating to the Resort that we have reviewed, any disclosure of the fact that, to a large degree, ownership and control of the Developer, DIL and Lausanne ultimately rests with Neville Mahon, and that all three entities have the ability to receive payments from Villa income, whether in the form of rental under the *Title Leases* or as various types of outgoings paid in accordance with the Owner Management Agreement. Had potential Villa purchasers been aware of these factors, they might have had serious concerns about their prospects of receiving any significant amounts of *Villa Revenue*.

FUNDS TO BE HELD IN TRUST

62. Clause 3.3 of the *Terms of Sale* of the Villa Sale Agreement requires that the Developer's stakeholder (being either the Developer's Fijian or New Zealand legal advisors) holds all deposits paid by Villa purchasers, and net interest earned on those deposits, in trust, to be paid to the Developer only upon settlement of each purchaser's purchase of the relevant Villa following practical completion of that Villa being achieved.

63. It has been alleged that the Developer may have spent, or lost control of, purchasers' deposit funds (such funds now presumably being comprised of deposits of stage 2 purchasers). We understand that Neville Mahon stated at a meeting dated 24 June 2009 that the deposit funds are now under the control of the Developer's financiers.

64. If such is the case, then the Developer would be in clear breach of its contractual obligations, and fiduciary duties (as regards the treatment of funds held in trust) owed to stage 2 Villa purchasers. Presumably, the Developer's stakeholders would also be in breach of their fiduciary duties as regards the deposit funds. We would be astonished if this were the case, as the Developer's stakeholders are reputable law firms, and in our view this issue warrants further investigation.

CONSTRUCTION OF THE RESORT

65. We understand that a significant amount of construction and development is required to fully complete the Resort in its originally intended form.

66. Clause 4 of the Villa Sale Agreement requires the Developer to construct the relevant Villa. However, clause 4.2 clearly states that the Developer will construct the overall resort project at its sole discretion, and will not be obligated to complete every stage of that project or fully develop the Resort. The Developer is not, therefore, in breach of any direct contractual obligation to the Owners in respect of its failure to progress the resort.

67. It does appear, however, at the Developer may have made various misrepresentations to Owners and to prospective Villa purchasers as to the prospects for completion of the various stages of the Resort.

REMEDIES

Owner Management Agreement

68. We are of the view that, regardless of whether DIL has available funds, DIL is liable to pay Owners 50% of the *Accommodation Revenue* in respect of all periods since the commencement of each Owner Management Agreement, because its variation of the *Specified Percentage* was illegitimate and therefore ineffective. Subject to any advice of your Fijian legal advisers, we would expect that the Owners' contractual remedies for that breach are as follows:

68.1 DIL is liable for the unpaid amount in accordance with clause 4.1

68.2 DIL is liable for default interest on the unpaid amount in accordance with clause 16.2(a) at the rate of 4% above the current overdraft interest rate of the Manager's principal bank.

69. DIL appears to have paid fees to Hilton, or allowed Hilton to deduct its fees, directly from gross Villa income and net Villa income. That is in clear breach of the Owner Management Agreement which only permitted Hilton's fees to be paid from the *Specified Percentage* as part of the *Operating Costs*. The Owners' principal remedy in respect of that breach is that, if it could be shown that such breach resulted in a lower *Villa Revenue* than would have been the case had it not occurred (which seems likely), the Owners will be entitled to default interest on any such outstanding *Villa Revenue*.

70. DIL has not dealt with Villa income in the manner provided for in the Owner Management Agreement. In particular, DIL has breached the provisions of the Owner Management Agreement providing for the calculation of the *Accommodation Revenue*, the *Retention Amount* and the *Villa Revenue*. We would expect that the Owners would have grounds, on that basis, to seek orders so as to enable the Owners to identify how Villa income has actually been treated, and further orders for specific performance by DIL of its obligations under the Owner Management Agreement. We understand that it was in this context that the current injunctions against DIL and Hilton were obtained.

71. The Owner are not entitled (pursuant to clause 16.2(b)) to claim damages and losses arising from breaches by DIL that relate to DIL's obligation to pay monies to the Owners.

72. DIL's breach of the audit and reporting requirements contained in the Owner Management Agreement would, in our view, entitle owners to bring a claim seeking orders that DIL complies with those obligations. The difficulty with this is that any reports that DIL does produce may be of limited assistance. For the Owners to identify the full extent of the treatment of Villa income by DIL, the Developer and their related entities, a full audit of all relevant entities would be necessary.

73. Clause 16.1 prevents the Owner from terminating the Owner Management Agreement for breaches by DIL. It may be, however, that the Owners could successfully establish that DIL's breaches are so fundamental that, despite clause 16.1, they are entitled to terminate that contract. That is a matter for your Fijian legal advisers to consider.

74. In terms of available steps for enforcing the debts owing by DIL to Owners, those options have been fairly well canvassed by your Fijian legal advisers.

Fair Trading Act 1986 & Contractual Remedies Act 1979

75. It appears that DIL, the Developer and Neville Mahon have made, and continue to make, a number of misrepresentations concerning the Resort, including misrepresentations as to:

75.1 the likely returns to Owners on their investments;

75.2 the nature and role of Lausanne; and

75.3 the timing of completion of various aspects of construction of the Resort.

76. In New Zealand:

76.1 misleading and deceptive conduct in trade is dealt with under the Fair Trading Act 1986 (FTA); and

76.2 misrepresentations, in the context of contracts, are dealt with under the Contractual Remedies Act 1979 (CRA).

To the extent that the Developer has, in New Zealand, knowingly made untrue or inaccurate statements, or provided information containing untruths or inaccuracies, to prospective Villa purchasers who have subsequently become Owners and suffered loss as a result of such untruths and inaccuracies, we would expect that those Owners would be entitled to remedies under the FTA, the CRA or both. We can advise further in that regard if necessary.

77. We are aware that the Neville Mahon and the Developer have gone to considerable lengths to promote the Resort in New Zealand. In that regard, even though the available remedies for DIL's breaches of the Owner Management Agreement are somewhat limited, there may be real value in the New Zealand based Owners pursuing Neville Mahon and the Developer in New Zealand under the FTA and the CRA and this option should not be disregarded.

78. In terms of Fijian law, we defer to the advice of your Fijian legal advisers as to what remedies might be available in respect of any misrepresentations that have been made. Depending on the extent to which the Resort has been promoted in other jurisdictions (such as Australia) you may wish to consider obtaining legal advice as to remedies that might be available in those other jurisdictions.

Receivers

79. Practically speaking, even if various claims could be successfully brought against any of Neville Mahon's companies, there may be little cash available to satisfy any orders made by the courts.

80. We understand that you have been negotiating with the Resort financiers (mainly Strategic) in an attempt to encourage them to:

80.1 exercise their rights (assuming those exist) to appoint receivers over DIL and the Developer; and

80.2 commit to a new structure that is satisfactory to them and to the Owners.

In our view that is certainly the best approach to take at this stage.

THE WAY FORWARD

Issues with the current structure

81. There a number of features of the current structure with are undesirable from the perspective of the Owners. Those include the following:

81.1 No body controlled by the Owners has any relationship with the Resort operator, Hilton.

81.2 The Owners have no contractual right to any information or details of the relationship between DIL and Hilton.

81.3 The Owners have no control over the calculation of any element of the *Hotel Operating Costs*.

81.4 The current structure does not include any corporate body formed to represent the interests of the Owners.

81.5 The developer of the resort, the manager (DIL) and one of the main service providers to those parties (Lausanne) are closely related parties, and this has resulted in:

(a) Resort income being potentially paid to those parties by various means without proper disclosure or accountability to the Owners;

(b) Resort income being encumbered with debt securities relating to funds borrowed by the Developer for construction of the Resort; and

(c) Resort income potentially being directed towards repayments of the Resort financiers (as well as repayments of contributions towards construction costs made by Hilton).

Replacement structure

82. Graeme Knott has suggested a new contractual and corporate structure for the operation of the Resort, and we attach a diagram illustrating that structure headed *Knott Proposal*. We have not had any input to that structure and the rationale for some aspects of it are unclear to us, but if that structure were to be established we note the following:

82.1 It is unclear to us, on the basis of the information we have seen, why two separate companies, Company A and Company B, are proposed instead of a single company. One company could (as far as we can tell) carry out the proposed functions of both companies and that would simplify the overall structure substantially.

82.2 As the proposal involves pooling for Villa income as among like Villas, and as the issue of units in two unit title schemes is proposed, the proposed Company A and Company B will be issuing participatory and equity securities. You will therefore need to obtain specialist advice as the promotion and issue of such securities in all jurisdictions where they are to be issued. We can advise you in that regard from a New Zealand perspective, however, you ought to obtain specialist Fijian and Australian advice (if applicable) in that regard as well.

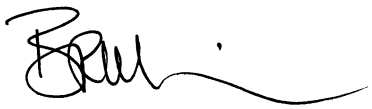
82.3 We are not entirely sure why it is proposed that unit trusts are formed, rather than simply companies. At least in the case of Company A we would have thought that, as regards the different types of Villas, Company A could simply issue different classes of shares to the Owners. In the case of Company B, we understand that there is a need to raise further funds so as to enable the repayment of financiers and completion of construction of the Resort and we do not have any particular objection to a unit title scheme in that regard. As a general comment we do encourage the view that structures should be kept simple to the extent possible.

82.4 Graeme Knott has suggested that, once the other structures are in place, a separate Owners' association be formed. In our view, if the Owners will hold the shares in Company A and Company B then, provided appropriate governance and reporting structures are enshrined in the constitutions of Company A and Company B, then the Owners will be well represented and there should be no need for an additional Owners' association.

83. If it becomes possible for a new structure to be established, we are in a good position to assist with advice on what the structure should be and with preparation of all necessary contracts and other documentation.

In conclusion, while we consider that the Owners almost certainly have the ability to bring a number of valid claims against DIL and the Developer and their related entities, the most sensible course at this stage is to work with the financiers. In the event that negotiations with the financiers fail and the Owners wish to take action against DIL and the Developer and their related entities, then as a priority they ought to pursue orders for a full disclosure of all arrangements between those entities (including a thorough audit of those entities) so as to properly identify the various parties' positions.

Yours faithfully
LOWNDES JORDAN



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