

**MERCHANT OPPORTUNITIES FUND**

**ARSN 111 456 387**

**ANNUAL FINANCIAL REPORT  
For the year ended 30 June 2013**

**Merchant Opportunities Fund**  
**ARSN 111 456 387**  
**For the year ended 30 June 2013**

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**Merchant Opportunities Fund**  
**ARSN 111 456 387**  
**Corporate Directory**

**Responsible Entity**

Capricorn Investment Partners Limited

**Directors of the Responsible Entity**

Stephen John Moss	-	Executive Chairman
David McKay French	-	Executive Director
Michael John Cranny	-	Non-Executive Director

**Secretaries**

Richard Joseph Symons

**Registered Office**

Level 2, Suite 1  
34 East Street  
Rockhampton QLD 4700

**Auditor of the Fund**

KPMG  
235 St Georges Terrace  
PERTH WA 6000

**Merchant Opportunities Fund**  
**ARSN 111 456 387**  
**Directors' Report**  
**For the year ended 30 June 2013**

The Directors of Capricorn Investment Partners Limited (ABN 26 095 998 771), the Responsible Entity of Merchant Opportunities Fund ("the Fund"), submit their report for the Fund for the year ended 30 June 2013, and the auditor's report thereon.

**DIRECTORS**

The names of the directors of Capricorn Investment Partners Limited, the Responsible Entity of the Fund from 5 April 2013 until the date of this report are:

*David McKay French – B.Econs, Dip.Corp Management*

David French is the Managing Director of Capricorn Investment Partners Limited. David was responsible for building the business of Capricorn Investment Partners to the point where it now looks after approximately \$430 million of investments for a range of clients across Australia. He has 24 years' experience in finance and economics, 19 of which are in investment markets.

David is also the responsible manager for the Capricorn Diversified Investment Fund and was rated one of the top three investment analysts in Australia for his sectors of responsibility. He holds a Bachelor of Economics and a Diploma of Corporate Management, and has completed a range of other courses relating to valuation of companies and investments. David is a past director of Rockhampton Regional Development Limited, The Rockhampton Chamber of Commerce, and is treasurer of Home Support Association Inc., a not for profit organisation assisting the needs of people with a disability.

*Stephen Moss – B. Divinity, Mstr Sacred Theology, Dr Ministry, Fellow Inst. of Co. Directors, Cert. Management Consultant, Fellow Aust Inst. of Co. Directors, Fellow Inst. Of Management Consultants*

Stephen Moss is a consultant/advisor with a background in law, psychology and business. Stephen's career includes 14 years as a Partner and Managing Partner of Price Waterhouse Coopers and Lybrand (now PWC), and Managing Director and CEO roles with a number of consulting firms including 2 years running IBM Consulting in Australia and New Zealand and International CEO of Cardno Acil, after he led the sale of ACIL Australia to Cardno Ltd.

He is currently Executive Chairman of Capricorn Investment Partners and is past principal of Eaton Capital, a corporate advisory and private equity investment firm specialising in working with professional service organisations, now owned by Capricorn Investment Partners. Until early 2013 Stephen was Vice Chairman of WDSScott, an international management consultancy firm based in London. He is a Co-founder of Advent Lawyers, Chairman of The Arch Institute of Advanced Global Studies and is currently Chairman of The Odin Institute in Europe.

*Michael Cranny – JP*

Michael Cranny is past Chairman of Capricorn Investment Partners Limited and Chairman of Tropical Pines, a large scale pineapple packer and marketer. Michael has previously held a number of board positions with the Yeppoon District Co-operative and Freshmark.

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**For the year ended 30 June 2013**

He has been an advisor to Golden Circle and has served as a councillor in Livingstone Shire Council, and been past Deputy Chairman of Capricorn Tourism and Economic Development. Outside of business he is involved in a large number of church and community activities.

*The names of the directors of Entrust Funds Management Ltd, the Responsible Entity of the Fund up until 5 April 2013 are:*

*Graeme Mark Yukich – B.Comm, CA, Dip.FP*

Graeme Yukich was appointed a director of the Responsible Entity on 22 October 2003. He is managing director of Entrust Private Wealth Management Pty Ltd, previously the parent company of the Responsible Entity. Graeme has extensive experience in the areas of stock broking and financial services and has been advising clients on their financial needs for over 20 years.

*Andrew Christopher Fry – B.Comm, CA*

Andrew Fry was appointed a director of the Responsible Entity on 22 October 2003. He is a director and Senior Investment Adviser of Entrust Private Wealth Management Pty Ltd, previously the parent company of the Responsible Entity. Andrew has considerable experience in the areas of stock broking and financial services both in a management and investment advisory capacity.

*Bradley William Gordon – SIA (Aff.) Fdn.DFP*

Bradley Gordon was appointed a director of the Responsible Entity on 22 October 2003. He is a director and Senior Investment Adviser of Entrust Private Wealth Management Pty Ltd, previously the parent company of the Responsible Entity. Bradley has extensive experience in the financial services industry, in stockbroking, financial planning and trustee services.

*David John Franklyn – B.Econs, Grad.Dip Applied Finance and Investment*

David Franklyn was appointed a director of the Responsible Entity on 2 August 2004. David has extensive experience in the financial services industry. He has in excess of over 20 years' experience in financial services, having been head of research for a national stockbroking firm, including the analysis and research of companies and has a broad understanding of many industry groups. David is responsible for the operations of Entrust Funds Management Ltd, which previously operated three investment schemes, totalling around \$95 million of funds under management.

**OPERATIONAL REVIEW FOR THE YEAR ENDED 30 JUNE 2013**

The Merchant Opportunities Fund (MOF) is now in its second year of operation, having changed the mandate from the Entrust Investment Fund in May 2012. As at 30 June 2013, MOF reported almost \$10 million of assets under management.

The nature of the fund's activities did not change significantly during the year, however on 20 December 2012 a General Meeting was held for unitholders to vote on the appointment of Capricorn Investment Partners Limited (CIPL) as the new Responsible Entity of the Fund.

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**For the year ended 30 June 2013**

Unitholders approved this change and CIPL became the Responsible Entity of the fund from 5 April 2013. In association, a new compliance committee was established, including Wayne Collins and Christina Kalanzis who are both experienced in the financial sector and in compliance matters generally.

Since its appointment as Responsible Entity, and in addition to normal administrative duties, CIPL has initiated a review of the assets in the Fund's portfolio, and participated in discussions aimed at improving the liquidity of the fund. A formal proposal regarding improved liquidity is expected to be considered by the management committee in October.

The Fund's mandate is to look for domestic (both short and long term) opportunities that are both listed on the ASX and unlisted. The Fund aims to have a concentrated portfolio of between 10 and 30 investments at all times and actively allocate capital to areas of the portfolio where the manager feels the greatest return on investment is possible. All investments during the year were undertaken in accordance with the Fund's constitution.

The small cap market was very weak over the 2012/13 financial year and the asset position of MOF suffered accordingly. Regardless, MOF finished the year with reasonable prospects for future capital appreciation. Throughout the year, MOF has maintained and sometimes built on its current core listed investments in the Oil & Gas, Coal, Mining Services and Healthcare Sectors of the market. The Fund also holds strategic investments in IT, Oil & Gas Services, as well as seed investment positions in the Coal, Copper, Vanadium and Iron Ore space. A number of these strategic positions relate to business plans which are expected to result in corporate activity over the coming year, providing opportunities to exit at expected higher prices.

The Fund maintains a holding in the Esplanade Property Fund which is an unlisted residual investment from the formerly named Entrust Investment Fund. This investment makes up around 14 per cent of the portfolio value and it is intended that when available, this investment will be sold down and funds moved into line with the Fund's broader operating investment mandate.

In conjunction with the 2011/12 change to the investment mandate, existing unitholders were provided with an opportunity to redeem units, if they did not desire to remain in the Fund. These redemption requests were met in full, and the Fund was frozen to further redemptions in August 2012 while a process of asset rebalancing was undertaken. A limited redemption facility was reinstated in September 2013, and the fund is currently open to redemptions pending the adoption of the liquidity plan.

Merchant Funds Management Pty Ltd remains the investment manager of the Fund and is responsible for the day to day management of the Fund.

The Fund did not have any employees during the year.

## **SCHEME INFORMATION**

Merchant Opportunities Fund is an Australian registered scheme, and was constituted on 18 October 2004. Capricorn Investment Partners Limited, the Responsible Entity of the Fund, is incorporated and domiciled in Australia.

**Merchant Opportunities Fund**  
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**Directors' Report (continued)**  
**For the year ended 30 June 2013**

Merchant Funds Management Pty Ltd was appointed the investment manager of the Fund on 12 April 2012, and along with this, is responsible for the day to day management of the Fund.

The registered office of the Responsible Entity is located at Level 2, Suite 1, 34 East Street, Rockhampton QLD 4700.

## **REVIEW OF RESULTS AND OPERATIONS**

### **Results**

The net operating income of Merchant Opportunities Fund is presented in the statement of comprehensive income. Loss from operating activities for the year ended 30 June 2013 was \$2,485,810 (2012: loss of \$1,940,597).

### **Distributions**

There was no distribution to unitholders (2012: 1.5 cents per unit) for the year ended 30 June 2013.

### **Indirect cost ratio**

The indirect cost ratio (ICR) is the ratio of the Fund's management costs over the Scheme's average net assets attributable for the year, expressed as a percentage.

Management costs include management fees and other expenses or reimbursements deducted in relation to the Fund, but do not include transactional and operational costs such as brokerage. Management costs are not paid directly by the unitholders of the Fund.

The ICR for the Fund for the year ended 30 June 2013 is 3.18% (2012: 2.25%)

## **UNIT PRICE HISTORY**

The ex-distribution exit prices and the highest and lowest exit prices for Merchant Opportunities Fund are shown below. All exit prices are exclusive of exit fees.

	<b>2013</b>	<b>2012</b>
	<b>\$</b>	<b>\$</b>
As at 30 June	0.5529	0.6955
Year to 30 June:		
High	0.6328	0.7956
Low	0.5245	0.6509

## **UNITS ON ISSUE**

17,801,987 units of Merchant Opportunities Fund were on issue at 30 June 2013 (2012: 17,359,455). During the year 1,230,236 (2012: 691,031) units were issued by the Fund and 787,704 units (2012: 8,895,630) were redeemed.

**Merchant Opportunities Fund**  
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**Directors' Report (continued)**  
**For the year ended 30 June 2013**

**SCHEME ASSETS**

At 30 June 2013 Merchant Opportunities Fund held assets to a total value of \$9,928,305 (2012: \$12,764,550). The basis for valuation of the assets is disclosed in Note 3 to the financial statements. The Responsible Entity does not hold any units in the Fund as at 30 June 2013.

**FEES PAID TO THE RESPONSIBLE ENTITY AND ASSOCIATES**

The following fees were paid to the Responsible Entity and its associates out of Fund property during the financial year:

Management fee for the financial period paid to the Responsible Entities & Merchant Funds Management Pty Ltd	\$92,067	(2012: \$150,556)
Preparation of Financial Reports	\$5,000	(2012: \$16,000)
Compliance Fees	\$7,688	(2012: \$10,250)
Expenses incurred by the Responsible Entity and reimbursed by the Fund in accordance with the Fund's constitution	\$0	(2012: \$35)

The interests in the Fund held by the Responsible Entity and its associates out of Fund property at the end of the year are disclosed in Note 13 to the financial statements.

**SIGNIFICANT CHANGES IN THE STATE OF AFFAIRS**

Other than the appointment of Capricorn Investment Partners Limited as the new Responsible Entity of the Fund, there were no significant changes to the state of affairs of Merchant Opportunities Fund during the year.

**LIKELY DEVELOPMENTS AND EXPECTED RESULTS**

The investment strategy of the Fund will be maintained in accordance with the Fund's Constitution and investment objectives.

**ENVIRONMENTAL REGULATION AND PERFORMANCE**

The Fund's operations are not subject to any environmental regulations under Commonwealth, State or Territory legislation.



**Merchant Opportunities Fund**  
**ARSN 111 456 387**  
**Directors' Report (continued)**  
**For the year ended 30 June 2013**

**INDEMNIFICATION AND INSURANCE OF OFFICERS OR AUDITORS**

The Constitution of the Responsible Entity requires it to indemnify all current and former officers of the Responsible Entity (but not including auditors) out of the property of the Responsible Entity against:

- (a) any liability for costs and expenses which may be incurred by that person in defending civil or criminal proceedings in which judgement is given in that persons favour, or in which the person is acquitted, or in connection with an application in relation to such proceedings in which the court grants relief to the person under the Corporations Act 2001; and
- (b) a liability incurred by the person, as an officer of the Responsible Entity or of a related body corporate, to another person (other than a Responsible Entity or a related body corporate) unless the liability arises out of conduct involving a lack of good faith.

During the financial year, the Responsible Entities and the Investment Manager paid an insurance premium in respect of a contract insuring each of the officers of the responsible Entity. The amount of the premium is, under the insurance contract, confidential. The liabilities insured include costs and expenses that may be incurred in defending civil or criminal proceedings that may be brought against the officers in their capacity as officers of the Responsible Entity or related body corporates. This insurance premium does not cover auditors.

The Fund has not indemnified or insured officers and auditors.

**EVENTS SUBSEQUENT TO BALANCE DATE**

There have been no events subsequent to balance date which would have a material effect on the Fund's financial statements at 30 June 2013.

**AUDITOR'S INDEPENDENCE DECLARATION**

The lead auditor's independence declaration is set out on page 8 and forms part of the directors' report for the year ended 30 June 2013.

This report is made in accordance with a resolution of the directors.



David French  
Director

Perth  
27<sup>th</sup> September 2013



***Lead Auditor's Independence Declaration under Section 307C of the Corporations Act 2001***

To: the directors of Capricorn Investment Partners Limited, responsible entity of Merchant Opportunities Fund

I declare that, to the best of my knowledge and belief, in relation to the audit for the financial year ended 30 June 2013 there have been:

- (i) no contraventions of the auditor independence requirements as set out in the Corporations Act 2001 in relation to the audit; and
- (ii) no contraventions of any applicable code of professional conduct in relation to the audit.

  
KPMG

  
Grant Robinson  
Partner

Perth

27 September 2013

**Merchant Opportunities Fund**  
**ARSN 111 456 387**  
**Statement of comprehensive income**  
**For the year ended 30 June 2013**

	Note	2013 \$	2012 \$
<b>Revenue</b>			
Interest income	7	19,349	122,902
Dividend and distribution income	7	40,813	437,025
Net gain/(loss) on financial instruments through profit and loss	8	(2,232,416)	(2,198,956)
Commissions		-	57,948
<b>Net investment income/(loss)</b>		<u>(2,172,254)</u>	<u>(1,581,081)</u>
<b>Expenses</b>			
Responsible Entity and Fund Manager fees	4(a)	(92,067)	(150,556)
Auditors' remuneration	4(b)	(59,893)	(42,197)
Consultants Fees		-	(385)
Custodian and administration fees		(50,414)	(55,114)
Compliance fees		(23,031)	(30,500)
Legal Fees		(20,119)	(4,826)
Other expenses		(68,032)	(75,938)
<b>Operating expenses before finance costs</b>		<u>(313,556)</u>	<u>(359,516)</u>
<b>Loss from operating activities</b>		<u>(2,485,810)</u>	<u>(1,940,597)</u>
<b>Finance costs</b>			
Distribution to unitholders	5(a)	-	(260,392)
<b>Changes in net assets attributable to unitholders / total comprehensive loss</b>		<u>(2,485,810)</u>	<u>(2,200,989)</u>

The above statement of comprehensive income should be read in conjunction with the accompanying notes.

**Merchant Opportunities Fund**  
**ARSN 111 456 387**  
**Statement of financial position**  
**As at 30 June 2013**

	Note	2013 \$	2012 \$
<b>Assets</b>			
Cash and cash equivalents	11(a)	14,396	281,795
Loans and receivables:			
Interest, dividends and other receivables	6	62,727	147,250
Financial assets held at fair value through profit and loss:			
Equity investments and units in listed and unlisted schemes	6	9,801,182	11,835,505
Convertible loan	6	50,000	500,000
<b>Total assets</b>		9,928,305	12,764,550
<b>Liabilities</b>			
Financial liabilities measured at amortised cost:			
Accrued expenses	6,9	66,600	52,385
Accounts payable	6	15,224	310,763
Distribution payable	5(a),6	-	260,392
Responsible entity and fund manager fees payable	6	3,511	21,154
<b>Total liabilities (excluding net assets attributable to Unitholders)</b>		85,335	644,694
<b>Net assets attributable to unitholders – Liability</b>	10(b)	9,842,970	12,119,856
<b>Represented by:</b>			
Net assets attributable to unitholders at redemption price	10(b)	9,842,970	12,119,856

The above statement of financial position should be read in conjunction with the accompanying notes.

**Merchant Opportunities Fund**  
**ARSN 111 456 387**  
**Statement of changes in equity**  
**For the year ended 30 June 2013**

The Fund's net assets attributable to unitholders are classified as a liability under AASB 132 *Financial Instruments: Presentation*. As such the Fund has no equity, and no items of changes in equity have been presented for the current or comparative year.

**Merchant Opportunities Fund**  
**ARSN 111 456 387**  
**Statement of cash flows**  
**For the year ended 30 June 2013**

	Note	2013 \$	2012 \$
<b>Cash flows from operating activities</b>			
Proceeds from sale of investments		2,395,100	12,301,435
Purchase of investments		(2,322,973)	(9,017,564)
Interest received		41,859	100,052
Dividends and distributions received		-	405,209
Receipts from commissions		-	49,768
GST Received		-	(4,085)
Payments to suppliers		(224,840)	(163,485)
Payments to responsible entity and fund manager		(105,127)	(196,476)
<b>Net cash flows from/(used in) operating activities</b>	11(b)	(215,981)	3,474,854
<b>Cash flows from financing activities</b>			
Cash distributions paid		(14,522)	(101,079)
Proceeds from application monies	10(b)	492,000	18,150
Payments on redemption of redeemable units	10(b)	(528,896)	(6,640,583)
<b>Net cash flows used in financing activities</b>		(51,416)	(6,723,512)
Net decrease in cash and cash equivalents		(267,399)	(3,248,658)
Cash and cash equivalents at 1 July 2012		281,795	3,530,453
<b>Cash and cash equivalents at 30 June 2013</b>	11(a)	14,396	281,795

The above statement of cash flow should be read in conjunction with the accompanying notes.

**Merchant Opportunities Fund**  
**ARSN 111 456 387**  
**Notes to the financial statements**  
**For the year ended 30 June 2013**

**Note 1 Reporting Entity**

Merchant Opportunities Fund (the Fund) is an Australian Registered Scheme, and was constituted on 18 October 2004 under the Corporations Act 2001. The Fund is a for profit entity. Capricorn Investment Partners Limited, the Responsible Entity of the Fund, is incorporated and domiciled in Australia. The registered office of the Responsible Entity is located at Level 2, Suite 1, 34 East Street, Rockhampton QLD 4700.

Merchant Funds Management Pty Ltd was appointed the investment manager of the Fund on 12 April 2012, and along with this, is responsible for the day to day management of the Fund.

The financial report of the Fund is for the year ended 30 June 2013.

**Note 2 Basis of Preparation**

**(a) Statement of compliance**

The financial report is a general purpose financial report which has been prepared in accordance with Australian Accounting Standards (AASBs) adopted by the Australian Accounting Standards Board (AASB) and the Corporations Act 2001. The financial report of the Fund complies with International Financial Reporting Standards (IFRSs) and interpretations adopted by the International Accounting Standards Board (IASB).

The financial report was approved by the Board of Directors of the Responsible Entity on 27<sup>th</sup> September 2013.

**(b) Basis of Measurement**

The financial statements have been prepared on a historical cost basis except for financial assets at fair value through profit and loss, which are measured at fair value.

**(c) Functional and presentation currency**

These financial statements are presented in Australian dollars, which is the Fund's functional currency.

**(d) Use of estimates and judgements**

The preparation of the financial statement in conformity with IFRS's requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from estimates. Estimates and underlying assumptions are reviewed on an ongoing basis, revisions to accounting estimates are recognised in the period in which the estimates are revised and in any future periods affected.

Note 12 and 13 contain information about the estimation of fair values of financial instruments.

**Merchant Opportunities Fund**  
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**Notes to the financial statements (continued)**  
**For the year ended 30 June 2013**

**Note 2 Basis of Preparation (continued)**

**(e) Changes in accounting policies**

There were no changes in the accounting policies of the Fund during the year.

**Note 3 Significant Accounting Policies**

The accounting policies set out below have been applied to all periods presented in these financial statements. The Fund has not early adopted any accounting standard.

**(a) Financial instruments**

**(i) Classification**

On 1 July 2005 the Fund classified all its listed and unlisted managed investment schemes investments into the fair value through profit or loss category.

Financial assets that are classified as loans and receivables include balances due from brokers and accounts receivable.

Financial liabilities that are measured at amortised cost include balances due to brokers and accounts payable.

**(ii) Recognition**

The Fund recognises financial assets and financial liabilities on the date it becomes a party to the contractual provisions of the instrument.

Financial assets are recognised using trade date accounting. From this date any gains or losses arising from changes in the fair value of the financial assets or financial liabilities are recorded.

**(iii) Measurement**

Financial instruments are measured initially at fair value (transaction price) plus, in the case of a financial asset or financial liability not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the financial asset or financial liability.

Transaction costs on financial assets and financial liabilities at fair value through profit or loss are expensed immediately, while on other financial instruments they are amortised.

Subsequent to initial recognition, all instruments classified at fair value through profit and loss are measured at fair value with changes in their fair value recognised in the profit or loss.



**Merchant Opportunities Fund**  
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**Notes to the financial statements (continued)**  
**For the year ended 30 June 2013**

**Note 3 Significant Accounting Policies (continued)**

Financial assets classified as loans and receivables are carried at amortised cost using the effective interest rate method, less impairment losses (see note 3(a)(v)), if any.

Financial liabilities, other than those at fair value through profit or loss, are measured at amortised cost using the effective interest rate.

Financial liabilities arising from the redeemable units issued by the Fund are carried at the redemption amount representing the investor's right to a residual interest in the Fund's assets, effectively fair value at reporting date.

**(iv) Fair value measurement principles**

The fair value of financial instruments is based on their quoted market prices at the balance sheet date without any deduction for estimated future selling costs. Financial assets are priced at current bid prices, while financial liabilities are priced at current asking prices.

If a quoted market price is not available on a recognised stock exchange or from a broker/dealer for non exchange traded financial instruments, the fair value of the instrument is estimated using valuation techniques, including use of recent arms length market transactions, reference to the current fair value of another instrument that is substantially the same, discounted cash flow techniques or any other valuation technique that provides a reliable estimate of prices obtained in actual market transactions.

Most of the unlisted investments were acquired as part of a capital raising process. As these are investments in seed, start-up or an early stage situation, these investments are valued based on purchase price, which is the price of recent investment activity. Following the relevant investment transaction date, the fair value of unlisted investments are assessed to determine whether changes in circumstances or events would imply a change in investment's fair value.

Investments in other unlisted managed investment schemes are recorded at the exit price or NTA as reported by managers of these schemes.

**(v) Impairment**

Financial assets that are stated at cost or amortised cost are reviewed at each balance sheet date to determine whether there is objective evidence of impairment.

If any such indication exists, impairment testing is carried out and an impairment loss is recognised in the statement of comprehensive income as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate.

**Merchant Opportunities Fund**  
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**Notes to the financial statements (continued)**  
**For the year ended 30 June 2013**

**Note 3 Significant Accounting Policies (continued)**

**(vi) Derecognition**

The Fund derecognises a financial asset when the contractual rights to the cash flows from the financial asset expire or it transfers the financial asset and the transfer qualifies for derecognition in accordance with AASB 139.

A financial liability is derecognised when the obligation specified in the contract is discharged, cancelled or expired.

**(b) Convertible loans**

Convertible loans are hybrid contracts measured at fair value through profit or loss as permitted under AASB 139.

The convertibility feature of the loan which meets the definition of an embedded derivative under AASB 139 is separated from the host contract and is measured at fair value through profit and loss.

**(c) Revenue**

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Fund and the revenue can be reliably measured. Specific revenues are recognised as follows:

*Dividend and distribution income*

Dividends and distributions from listed entities are recognised as income on the date the share or unit is quoted ex-dividend or ex-distribution.

In some cases the Fund may receive or choose to receive dividends or distributions in the form of additional shares or units rather than cash. In such cases the Fund recognises the dividend or distribution income for the amount of the cash dividend alternative with the corresponding debit treated as an additional investment.

*Interest income*

Income from interest bearing securities is recognised as the interest accrues using the effective interest rate method.

*Changes in the fair value of assets*

Gains or losses on financial assets at fair value through profit and loss are calculated as the difference between the fair value at sale, or at year end, and the fair value at the previous valuation point. This includes both realised and unrealised gains and losses.

**Merchant Opportunities Fund**  
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**Notes to the financial statements (continued)**  
**For the year ended 30 June 2013**

**Note 3 Significant Accounting Policies (continued)**

**(d) Expenses**

All expenses, including management fees and custodian fees, are recognised in the statement of comprehensive income on an accruals basis.

Included in other operating expenses are legal, advisory and other fees which are broken down in the statement of comprehensive income.

**(e) Cash and cash equivalents**

Cash and cash equivalents, comprise cash at bank and short term deposits with an original maturity of three months or less, are subject to an insignificant risk of changes in value and are held for the purpose of meeting short term cash commitments rather than for investment or other purposes.

**(f) Taxation**

Under the current legislation, the Fund is not subject to income tax provided the unitholders are entitled to the income of the Fund and the Fund fully distributes its taxable income (including assessable realised capital gains).

**(g) Distributions**

In accordance with the Fund's Constitution, the distributable income of the Fund is the amount determined by the Responsible Entity to be appropriate after reviewing the income of the Fund, the investment opportunities available and the market and any other matters that the Responsible Entity believes are relevant. The amounts the Responsible Entity determines in each financial year shall not be less than the net income (as defined in Section 95(1) of the Tax Act) of the Fund for the financial year (excluding any amount included in assessable income under section 160AQT or 6AC of the Tax Act).

Distributable income is calculated and distributed at the end of the financial year and at any other time that the Responsible Entity elects. Realised capital losses are not distributed to unitholders but are retained in the Fund to be offset against any future realised capital gains. If realised capital gains exceed realised capital losses the excess is distributed to unitholders.

**(h) Change in net assets attributable to unitholders**

The amount of the Fund's income for a financial year not distributed to unitholders as determined by the Responsible Entity in accordance with the Fund's Constitution is transferred to net assets attributable to unitholders. The amount transferred to net assets attributable to unitholders as determined by the Responsible Entity may include amounts of unrealised gains and losses in the fair value of investments, accrued income not yet assessable and expenses provided for or accrued but not yet deductible, net capital losses and tax free or tax deferred income.

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**Notes to the financial statements (continued)**  
**For the year ended 30 June 2013**

**Note 3 Significant Accounting Policies (continued)**

These items are included in the determination of distributable income in the period for which they are assessable for taxation purposes.

**(i) Unit prices**

Unit prices are determined in accordance with the Fund's Constitution and are calculated as the net portfolio value of the Fund less performance fees accrued and distributions paid divided by the number of units on issue.

**(j) Terms and conditions on units**

Each unit issued confers upon the unitholder an equal interest in the Fund, and is of equal value. A unit does not confer any interest in any particular asset or investment of the Fund. Unitholders have various rights under the Constitution and the Corporations Act 2001, including the right to:

- have their units redeemed;
- receive income distributions;
- attend and vote at meetings of unitholders; and
- participate in the termination and winding up of the Fund.

The rights, obligations and restrictions attached to each unitholder are identical in all respects.

**(k) Goods and services tax**

Expenses incurred by the Fund are recognised net of the amount of GST that can be recovered from the Australian Taxation Office (ATO). Amounts recognised as payables at balance date include the amount of GST payable.

Reduced input tax credits (RITC) recoverable by the Fund from the ATO are recognised as receivables in the statement of financial position. Cash flows are included in the statement of cash flows on a gross basis.

**(l) Significant accounting judgements, estimates and assumptions**

Except for the determination of fair values in the valuation of financial assets at fair value through profit and loss and recoverability of receivables (see note 3(c) (iii)), there are no other significant accounting judgements, estimates or assumptions made by management.

**(m) Redeemable units**

All redeemable units issued by the Fund provide the investors with the right to require redemption for cash and give rise to a financial liability. In accordance with the product disclosure documents the Fund is contractually obliged to redeem units at redemption price, which includes an allowance for transaction costs that would be incurred by the Fund on disposal of its assets required to fund redemptions.

**Merchant Opportunities Fund**  
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**Notes to the financial statements (continued)**  
**For the year ended 30 June 2013**

**Note 3 Significant Accounting Policies (continued)**

As a result of the transaction cost factor, there will be a difference between the carrying amount of the net assets of the Fund (excluding the unitholders funds classified as a financial liability) and the contractual amount payable to unitholders which is based on redemption price. The adjustments arising from the different unit pricing under Australian Accounting Standard's valuation principles are presented in the statement of financial position as part of the net assets attributable to unitholders.

**(n) Finance costs**

Distributions paid and payable on units are recognised in the statement of comprehensive income as financial costs and as a liability where not paid. Distributions paid are included in cash flows from financing activities in the statement of cash flows.

**(o) New standards and interpretations not yet adopted**

The following amendment to an accounting standard has been identified as those which may impact the Fund in the period of initial application. They are available for early adoption at 30 June 2013, but have not been applied in preparing this financial report:

- AASB 9 *Financial Instruments* includes requirements for the classification and measurement of financial assets resulting from the first part of Phase 1 of the project to replace AASB 139 *Financial Instruments: Recognition and Measurement*. AASB 9 will become mandatory for the Scheme's 30 June 2014 financial statements. Retrospective application is generally required, although there are exceptions. The Fund has not yet determined the potential effect of the standard.

AASB 9 deals with recognition, derecognition, classification and measurement of financial assets and financial liabilities. Its requirements represent a significant change from the existing requirements in AASB 139 in respect of financial assets. The standard contains two primary measurement categories for financial assets: at amortised cost and fair value. A financial asset would be measured at amortised cost if it is held within a business model whose objective is to hold assets in order to collect contractual cash flows, and the asset's contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest on the principal outstanding. All other financial assets would be measured at fair value. The standard eliminated the existing AASB 139 categories of held to maturity, available for sale and loans and receivables.

For an investment in an equity instrument that is not held for trading, AASB 9 permits an irrevocable election, on initial recognition, on an individual share-by-share basis, to present all fair value changes from the investment in other comprehensive income. No amount recognised in other comprehensive income would ever be reclassified to profit or loss. However, dividends on such investments are recognised in profit or loss, rather than other comprehensive income, unless they clearly represent a partial recovery of the cost of the investment. Investments in equity instruments in respect of which an entity does not elect to present fair value changes in other comprehensive income would be measured at fair value with change in fair value recognised in profit or loss.

**Merchant Opportunities Fund**  
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**Notes to the financial statements (continued)**  
**For the year ended 30 June 2013**

**Note 3 Significant Accounting Policies (continued)**

AASB 9 requires that the effects of changes in credit risk of liabilities designated as at fair value through profit and loss are presented in other comprehensive income unless such treatment would create or enlarge an accounting mismatch in profit or loss. Other requirements of AASB 9 relating to classification and measurement of financial liabilities are unchanged from AASB 139.

- AASB 10 *Consolidated Financial Statements* includes new requirements to determine whether or not entities that the Fund has an interest in needs to be consolidated. AASB 10 will become mandatory for the Fund's 30 June 2014 financial statements. Retrospective application is required. Based on the Responsible Entity's assessment of the Fund's current portfolio, this will not affect the preparation of the financial statements of the Fund. Reassessment will be made on a regular basis.
- AASB 11 *Joint Arrangements* includes new requirements for the accounting of interests in joint arrangements. AASB 11 will become mandatory for the Fund's 30 June 2014 financial statements. Retrospective application is required. The Fund has not yet determined the potential effect of the standard.
- AASB 12 *Disclosure of Interest in Other Entities* includes significant new disclosures for interests in subsidiaries, joint arrangements, associates and unconsolidated structured entities. AASB 12 will become mandatory for the Fund's 30 June 2014 financial statements. Retrospective application is required. The Fund has not yet determined the potential effect of the standard.
- AASB 13 *Fair Value Measurement* includes a definition of fair value and provides guidance on fair value measurement. AASB 13 will become mandatory for the Fund's 30 June 2014 financial statements. This standard is applied prospectively. The Fund has not yet determined the potential effect of the standard.

**Merchant Opportunities Fund**  
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**Notes to the financial statements (continued)**  
**For the year ended 30 June 2013**

	<b>2013</b>	<b>2012</b>
	<b>\$</b>	<b>\$</b>
<b>Note 4 Expenses</b>		
<b>(a) Responsible Entity and Investment Manager fees</b>		
Management fees	92,067	150,556
Total responsible entity fees	<u>92,067</u>	<u>150,556</u>
<b>(b) Auditor's remuneration</b>		
Audit services: KPMG		
- audit and review of the financial reports	48,763	33,257
- other regulatory audit services	11,130	8,480
	<u>59,893</u>	<u>42,197</u>
<b>Note 5 Distributions Paid and Payable</b>		
<b>(a) Distributions payable</b>		
- for period ended 30 June	-	260,392
Total distributions	<u>-</u>	<u>260,392</u>
<b>(b) Per unit distribution</b>		
- for period ended 30 June (cents per unit)	-	1.50
	<u>-</u>	<u>1.50</u>

**Merchant Opportunities Fund**  
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**Notes to the financial statements (continued)**  
**For the year ended 30 June 2013**

	<b>2013</b>	<b>2012</b>
	<b>\$</b>	<b>\$</b>
<b>Note 6 Financial assets and liabilities</b>		
The following table details the categories of financial assets and liabilities held by the Fund at reporting date:		
<b>Assets</b>		
<i>Classified as fair value through the profit and loss upon initial recognition</i>		
-Equity investments	8,410,268	10,427,664
-Managed investment schemes: related*	1,390,914	1,407,841
-Derivative financial instruments	50,000	500,000
<b>Total financial assets at fair value through the profit or loss</b>	<u>9,851,182</u>	<u>12,335,505</u>
<b>Cash and cash equivalents (Note 11a)</b>	<u>14,396</u>	<u>281,795</u>
<b>Loans and receivables</b>		
Dividends receivable	40,803	63,631
Interest receivable	340	22,849
Other receivable	18,699	56,885
GST receivable	2,885	3,885
<b>Total loans and receivables</b>	<u>62,727</u>	<u>147,250</u>
<b>Total assets</b>	<u>9,928,305</u>	<u>12,764,550</u>
<b>Liabilities</b>		
Financial liabilities measured at amortised cost	85,335	644,694
<b>Total liabilities</b>	<u>85,335</u>	<u>644,694</u>

\* Following the change in Responsible Entity in April 2013, the investment is no longer considered a related party at year-end.

Financial liabilities measured at amortised cost presented above represents accounts payable, accrued expenses and distributions payable as detailed in the statement of financial position.



**Merchant Opportunities Fund**  
**ARSN 111 456 387**  
**Notes to the financial statements (continued)**  
**For the year ended 30 June 2013**

**Note 7 Interest and dividend income**

The following table details the interest income earned by the Fund during the period:

	2013 \$	2012 \$
Interest income for financial assets carried at amortised cost:		
-cash and cash equivalents	2,865	100,052
-convertible loan	16,484	22,849
<b>Total interest income</b>	<b>19,349</b>	<b>122,902</b>

The following table details the dividend and distribution income earned by the Fund during the period:

	2013 \$	2012 \$
Dividend and distribution income from equity securities and units in listed and unlisted schemes classified as fair value through profit and loss	40,813	437,025
<b>Total dividend and distribution income</b>	<b>40,813</b>	<b>437,025</b>

**Note 8 Gains and losses from financial assets and liabilities**

The following table details the gains and losses from financial assets and liabilities at fair value through the profit and loss:

	2013 \$	2012 \$
Classified as fair value through the profit and loss:		
-Equity investments and listed managed investment scheme.	(2,232,416)	(2,198,956)
<b>Net gain(loss) from financial assets and liabilities classified as fair value through the profit and loss</b>	<b>(2,232,416)</b>	<b>(2,198,956)</b>

Gains and losses presented above exclude interest income, dividend income and distribution income.

The following table details the gains and losses from financial assets through the profit and loss for the year ended:

	2013 \$	2012 \$
Realised gain/(loss)	(951,919)	(1,159,656)
Unrealised gain/(loss)	(1,280,497)	(1,039,300)
<b>Net gain/(loss) from financial assets and liabilities classified as fair value through profit or loss</b>	<b>(2,232,416)</b>	<b>(2,198,956)</b>

**Merchant Opportunities Fund**  
**ARSN 111 456 387**  
**Notes to the financial statements (continued)**  
**For the year ended 30 June 2013**

	<b>2013</b>	<b>2012</b>
	\$	\$
<b>Note 9 Accrued expenses</b>		
Audit fees	31,600	27,385
Accounting Fees	35,000	25,000
	<u>66,600</u>	<u>52,385</u>

**Note 10 Net Assets Attributable to Unitholders**

**(a) Units on issue**

The Fund's units on issue are represented by fully paid ordinary units.

The Fund considers its capital to be Unitholder's Funds.

The objective of the Fund is to provide unitholders with above average returns over the medium to long term through capital growth. The Fund aims to achieve this through investing in private companies, companies in the pre listing phase and companies listed on ASX in line with the Responsible Entity's investment criteria, while maintaining sufficient liquidity to fund unitholder redemption facilities when these are operating.

The Fund does not have any externally imposed capital requirements.

Units are issued at the unit application price at the end of the month. The unit application price is calculated in accordance with the Fund's constitution.

It is anticipated that units can be redeemed at the end of each month, however from time to time the Fund may be illiquid – when such times arise the Investment Manager will seek permission to suspend the redemption facility until such time as liquidity emerges. The redemption price at which the units are redeemed is calculated at the end of the month in accordance with the Fund's constitution. To protect the interests of all unitholders, no more than 15% of total units on issue may be redeemed in any month, although this restriction can be waived by the Responsible Entity.

In conjunction with the 2011/12 change to the investment mandate, existing unitholders were provided with an opportunity to redeem units, if they did not desire to remain in the Fund. These redemption requests were met in full, and the Fund was frozen to further redemptions in August 2012 while a process of asset rebalancing was undertaken. A limited redemption facility was reinstated in September 2013, and the Fund is currently open to redemptions pending the adoption of the liquidity plan.

Each unitholder is entitled to attend and vote at any meeting convened by the Responsible Entity. Unitholders are entitled to one vote per unit held. Unitholders are entitled to receive all distributions declared and paid by the Fund. Upon winding up the holders are entitled to a return of capital based on the net asset value per share of the Fund.

**Merchant Opportunities Fund**  
**ARSN 111 456 387**  
**Notes to the financial statements (continued)**  
**For the year ended 30 June 2013**

**Note 10 Net Assets Attributable to Unitholders (continued)**

	<b>2013</b>	<b>2012</b>
	<b>Number</b>	<b>Number</b>
Units on issue as at beginning of reporting period	17,359,455	25,564,054
Units issued during the reporting period	1,230,236	691,031
Units redeemed or otherwise cancelled during reporting period	(787,704)	(8,895,630)
Units on issue as at the end of the reporting period	<u>17,801,987</u>	<u>17,359,455</u>

	<b>2013</b>	<b>2012</b>
	<b>\$</b>	<b>\$</b>
<b>(b) Movement in net assets attributable to unitholders</b>		
Net assets attributable to unitholders at beginning of reporting period	12,119,856	20,405,256
Change in net assets attributable to unitholders:		
Loss from operating activities	(2,485,810)	(1,940,597)
Distribution expense	-	(260,392)
Units issued during the reporting period	492,000	18,150
Units issued during the reporting period (distribution reinvestment)	245,820	538,022
Units redeemed or otherwise cancelled during the reporting period	(528,896)	(6,640,583)
Net assets attributable to unitholders at the end of reporting period	<u>9,842,970</u>	<u>12,119,856</u>

**Note 11 Cash and Cash Equivalents**

**(a) Cash and cash equivalents**

Cash balance comprises:

- Current deposits with banks	<u>14,396</u>	<u>281,795</u>
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**(b) Reconciliation of cash flows from operating activities**

Loss from operating activities	(2,485,810)	(1,940,597)
<i>Adjustments for:</i>		
Net changes in financial assets held at fair value through profit and loss	2,484,323	5,200,719
<i>Changes in operating assets and liabilities:</i>		
Decrease/(increase) in loans and receivables	84,523	(104,049)
(Decrease)/increase in accrued expenses	14,215	14,405
(Decrease)/increase in trade and other creditors	(313,233)	304,376
<b>Net cash flows (used in) / from operating activities</b>	<u>(215,982)</u>	<u>3,474,854</u>

**Merchant Opportunities Fund**  
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**Notes to the financial statements (continued)**  
**For the year ended 30 June 2013**

	2013	2012
	\$	\$
<b>Note 11 Cash and Cash Equivalents (continued)</b>		
<b>(c) Non-cash operating, financing and investing activities</b>		
Non-cash operating, financing and investing activities carried out during the year on normal commercial terms and conditions included:		
Reinvestment of dividend and distribution income	-	63,631
Reinvestment of unitholder's distributions (Note 10)	245,820	538,023
	<hr/>	<hr/>

**Note 12 Financial instruments and associated risk**

**Investment overview and strategy**

The Responsible Entity maintained its investment approach for this Fund up until 31 December 2011 which consisted of the following investment principles:

- The Fund will aim to hold a concentrated portfolio of between 10 and 40 companies.
- The Responsible Entity seeks companies to invest in that have strong, ethical trustworthy management.
- The Responsible Entity will invest in companies that it has identified as being undervalued by the market
- The Responsible Entity adopts a medium to long term investment horizon.
- Single investments can only represent more than 10% of the Fund's portfolio if approved by the Investment Committee.

The investment strategy is built around thorough fundamental financial analysis and regular contact with management of companies/managed investment schemes that the Responsible Entity proposes to invest in, and invests in. The objective is to understand the company/managed investment scheme well, to recognise the risk factors and to determine an appropriate valuation of the company/managed investment scheme.

Broadly, the Fund has endeavoured to have approximately 70% of the portfolio in "good value / good quality" small industrial companies, typically with a stable earnings history, strong balance sheet and with a market capitalisation between \$50 million and \$1 billion. The remaining 30% of the portfolio is invested in "special situations" – opportunities whereby the Responsible Entity seeks to become actively involved in unlocking the value in the investment.

As from 1 January 2012, the Responsible Entity determined to modify the investment mandate of this Fund to increase its focus on "special opportunities" and to also seek to increase the Funds exposure to small and emerging resource sector opportunities. The mandate was also widened to allow more active investment in unlisted securities. From 1 January 2012 until 12 April 2012 the portfolio was adjusted in line with the new Mandate.

**Merchant Opportunities Fund**  
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**Notes to the financial statements (continued)**  
**For the year ended 30 June 2013**

**Note 12 Financial instruments and associated risk (continued)**

On 12 April 2012 unitholders in the Fund approved the appointment of Merchant Funds Management Pty Ltd as the Investment Manager, with the name of the Fund changed to the Merchant Opportunities Fund (MOF).

The objectives of Merchant Funds Management Pty Ltd, the investment manager of the Fund as from 12 April 2012 are:

- To generate an absolute return greater than the prevailing Bank Bill Swap Rate (BBSW) plus a gross margin of 3%.
- To manage the Fund in a disciplined and focused manner with the aim of providing capital growth over the long term.
- To provide access to investment opportunities to which individual investors may not normally gain access.
- To protect capital during periods of extreme volatility.
- To create a Western Australian based absolute return Fund focused on Australian listed and unlisted equities.

The Guiding Principles of the Investment Manager are similar to those employed by the previous manager with the following exceptions:

- The Fund will hold between 10 and 30 separate investments.
- No single investment (apart from cash) can represent over 30% of the Fund's portfolio value unless approved by the Investment Committee.
- The Responsible Entity can from time to time invest in companies that are either; private and or pre-listing status.
- The Fund aims to protect capital in periods of extreme volatility through moving to cash or utilising hedging strategies as it sees fit.
- The Fund will seek and execute short term trading opportunities as appropriate and commensurate with the risk weightings of the Funds parameters.

Investments in assets are determined by the Fund Manager in consultation with the Investment Committee ("the Committee") and the board of the Responsible Entity ("Board"). The Investment Committee and the Board meet on a regular basis to discuss potential investments in the Fund, any changes to the weighting of the portfolio and to agree on the strategy going forward. Current market conditions are a focus of the Committee and the Board, with focus on the implications these conditions will have on the Fund. Where the Board and the Committee identify an area of risk the Fund will change its focus or strategy or change the weighting of the portfolio to minimise identified risks.

The Fund invests in securities in accordance with its investment strategy and the Fund Managers' investment criteria.

**Merchant Opportunities Fund**  
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**Notes to the financial statements (continued)**  
**For the year ended 30 June 2013**

**Note 12 Financial instruments and associated risk (continued)**

The impact of the financial risks to which the Fund is exposed are market risk, credit risk and liquidity risk. Each of these are discussed below. Disclosures in regard to these risks are prepared on the basis of the Fund's directly held investments and not on a look through basis.

**Market risk**

Market risk embodies the potential for loss and gains and, in the case of the Fund is limited to price risk on its investments and interest rate risk on its cash and cash equivalents. The Fund is not exposed to currency risk as it only invests in Australian currency denominated investments.

The Fund's investment strategy is, in simple terms, to purchase quality investments at a reasonable price. The Fund's market risk is managed on a daily basis by the Fund Manager and the Investment Manager. A financial model is maintained and updated daily to reflect current market conditions, analysis of the major investments of the Fund and the pricing of the investments of the Fund. Any risks identified by the Fund Manager are discussed with members of the Committee and the Board to determine appropriate action.

The Investment Manager regularly reviews the investments and holds monthly meetings. The Investment Manager is also in regular contact with the Board.

The Fund Manager maintains regular contact with the companies and managed investment schemes it invests in to better understand those entities and to assist the manager recognise any risk factors that the investment may be subject to.

**Interest rate risk**

The majority of the Fund's assets are non-interest bearing. All assets exposed to interest rate fluctuations are short term therefore limiting the exposure of the Fund to interest rate risk. Any excess cash and cash equivalents are invested in regular interest bearing accounts available on call to enable the Fund to act quickly on potential investment opportunities. The Fund does not have any interest bearing financial liabilities.

It is the intention of the Responsible Entity to invest the funds in equity assets not interest bearing assets.

***Interest rate sensitivity***

An increase of 50 basis points in interest rates as at the reporting date would have increased the net assets attributable to unitholders and profit from operating activities of the Fund by \$322 (2012: \$3,090). A decrease of 50 basis points would have had an equal but opposite effect.

**Merchant Opportunities Fund**  
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**Notes to the financial statements (continued)**  
**For the year ended 30 June 2013**

**Note 12 Financial instruments and associated risk (continued)**

**Other price risk**

Other price risk is the risk that value of the instrument will fluctuate as a result of changes in market prices (other than those arising from interest rate or currency risk), whether caused by factors specific to an individual investment, its issuer or all factors affecting all instruments traded in the market.

As a majority of the Fund's financial instruments are carried at fair value with fair value changes recognised in the statement of comprehensive income, all changes in market value of investments will directly affect the investment income of the Fund.

Price risk is managed by the Fund Manager by constructing a diversified portfolio of assets traded in differing sectors of the market.

The Fund is permitted to invest in securities quoted on ASX or unlisted companies, cash or interest in cash management trusts, debentures bonds and unsecured notes, derivative and short selling of securities, warrants and options and other financial products as permitted by the Responsible Entity's AFSL.

The following table details the sector breakdown

<b>Total investment assets by industry sector</b>	<b>2013</b>		<b>2012</b>	
	<b>\$</b>	<b>%</b>	<b>\$</b>	<b>%</b>
Consumer discretionary	20,000	0.20	-	-
Energy	1,901,253	19.30	3,575,092	28.98
Property	1,390,914	14.12	1,407,841	11.41
Health care	4,385,556	44.52	4,049,754	32.83
Industrials	492,370	5.00	1,354,539	10.98
Materials	727,500	7.38	1,313,279	10.65
Information Technology	933,589	9.48	635,000	5.15
	<b>9,851,182</b>	<b>100.00</b>	<b>12,335,505</b>	<b>100.00</b>

The following table details the breakdown of the investment assets held by the Fund:

	<b>30 June 2013</b>	<b>30 June 2012</b>
Listed equity investments	6,254,679	8,982,664
Unlisted equity investments and unlisted managed investment schemes	3,546,503	2,852,841
Convertible loan	50,000	500,000
<b>Total investment assets</b>	<b>9,851,182</b>	<b>12,335,505</b>

**Merchant Opportunities Fund**  
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**Notes to the financial statements (continued)**  
**For the year ended 30 June 2013**

**Note 12 Financial instruments and associated risk (continued)**

*Sensitivity analysis*

The objective of the Fund is to exceed the return of the S&P/ASX Small Ordinaries Accumulation Index over the medium to long term. A 5% increase in the market price of the Fund's listed investments at 30 June 2013 would have increased net assets attributable to unitholders and decreased loss from operating activities by \$312,734 (2012: \$449,133): an equal change in the opposite direction would have decreased net assets attributable to unitholders and increased loss from operating activities by an equal amount.

A 5% increase in the value of unlisted equity investments and convertible loans at 30 June 2013 would have increased net assets attributable to unitholders and decreased loss from operating activities by \$179,825 (2012: \$167,642). An equal change in the opposite direction would have decreased net assets attributable to unitholders and increased loss from operating activities by an equal amount.

**Credit risk**

Credit risk is the risk that counterparty to a financial instrument will fail to discharge an obligation or commitment that it has entered into with the Fund, resulting in financial loss to the Fund.

The carrying amounts of financial assets best represent the maximum credit risk exposure at balance sheet date.

At reporting date the Fund's financial assets exposed to credit risk amounted to the following:

	<b>30 June 2013</b>	<b>30 June 2012</b>
Cash and cash equivalents	14,396	281,795
Interest, dividends, distributions and other receivables	62,727	147,250
Convertible loan	50,000	500,000
<b>Total</b>	<b>127,123</b>	<b>929,045</b>

Credit risk arising on transactions with brokers relates to transactions awaiting settlement. The Fund uses a range of brokers when entering into equity transactions. As a result should one broker fail to settle transactions the Fund's exposure to this broker is diluted. The Fund uses only brokers that are known to the manager, have a good record in the industry and have a history and reputation for quality service and settling on equity transactions.

Distributions and dividends receivables are only recognised once declared. The credit risk the Fund is exposed to in respect to unsettled transactions and receivables is therefore considered low.



**Merchant Opportunities Fund**  
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**Notes to the financial statements (continued)**  
**For the year ended 30 June 2013**

**Note 12 Financial instruments and associated risk (continued)**

The convertible loan bears an interest rate of 8% per annum and is repayable on or before 31 January 2015. The Fund may request, in writing, that the Borrower repay the loan by converting the loan into shares at a discount of 20% to the volume weighted average price period as per the loan agreement.

All assets are held by the Fund's custodian, The Trust Company ("Custodian"). Bankruptcy or insolvency by the custodian may cause the Fund's right to securities held by the custodian to be delayed or limited. The Fund monitors the position of the Custodian in terms of its market participant stature on a quarterly basis and National Australia Bank ("Bank") with whom it places its cash with.

The credit risk associated with the custodian and the Bank is considered low as the Custodian is owned by a major financial institution. The Responsible Entity monitors the position of the Bank and the custodian through ASX releases and media commentary on a regular basis.

The carrying amounts of financial assets best represent maximum credit risk exposure at the balance sheet date.

**Liquidity risk**

Liquidity risk is the risk that the Fund will encounter difficulty in meeting obligations arising from its financial liabilities that are settled by delivering cash or another financial asset, or that such obligations will have to be settled in a manner disadvantageous to the Fund.

The Fund aims to provide a monthly redemption facility; however in times of illiquidity, the Fund will seek permission from the Responsible Entity to suspend redemptions to protect the value of the remaining unit holders.

Liquidity risk is managed on a daily basis by the fund manager in respect to trades awaiting settlement, monthly redemption requests and short term liabilities of the Fund. The portfolio of the Fund is updated to reflect purchases and sales of securities.

The Fund's listed securities are considered to be readily realisable as they are all listed on ASX.

The Fund's redemption policy allows for redemptions at the end of the month only, save for liquidity issues that arise from time to time referred to above.

**Merchant Opportunities Fund**  
**ARSN 111 456 387**  
**Notes to the financial statements (continued)**  
**For the year ended 30 June 2013**

**Note 12 Financial instruments and associated risk (continued)**

Set out below is the contractual maturity profile of the Fund's financial liabilities:

**30 June 2013**

	<b>Contractual cashflows</b>	<b>Less than 1 month</b>	<b>On call*</b>
Accrued expenses	66,600	66,600	-
Accounts payable	15,224	15,224	
Responsible Entity and Fund Manager fees payable	3,511	3,511	-
Net assets attributable to unitholders	9,842,970	-	9,842,970
<b>Total financial liabilities</b>	<b>9,928,305</b>	<b>85,335</b>	<b>9,842,970</b>

**30 June 2012**

	<b>Contractual cashflows</b>	<b>Less than 1 month</b>	<b>On call*</b>
Accrued expenses	52,385	52,385	-
Accounts payable	310,763	310,763	
Responsible Entity fees payable	21,154	21,154	-
Net assets attributable to unitholders	12,119,856	-	12,119,856
<b>Total financial liabilities</b>	<b>12,504,158</b>	<b>384,302</b>	<b>12,119,856</b>

\* To protect the interests of all unitholders, no more than 15% of total units on issue may be redeemed in any month, although this restriction can be waived by the Responsible Entity.

The table above does not include the distribution payable as this is substantially reinvested in units of the Fund, therefore not posing a liquidity risk.

**Operational risk**

Operational risk is the risk of direct or indirect loss arising from a wide variety of causes associated with the Fund's processes, personnel, technology and infrastructure, and from external factors other than credit, market and liquidity risks such as those arising from legal and regulatory requirements and generally accepted standards of corporate behaviour. Operational risks arise from all of the Fund's operations.

The objective of the Responsible Entity of the Fund is to manage operational risk so as to balance limiting of financial losses and damage to the Fund's reputation with overall cost effectiveness and to avoid control procedures that restrict initiative and creativity.

**Merchant Opportunities Fund**  
**ARSN 111 456 387**  
**Notes to the financial statements (continued)**  
**For the year ended 30 June 2013**

**Note 12 Financial instruments and associated risk (continued)**

The primary responsibility for the development and implementation of controls to address operational risk is assigned to the Responsible Entity. This responsibility is supported by the development of overall Fund standards for the management of operational risk in the following areas:

- requirements for appropriate segregation of duties, including the independent authorisation of transactions
- requirements for the reconciliation and monitoring of transactions.
- compliance with regulatory and other legal requirements
- documentation of controls and procedures
- requirements for the periodic assessment of operational risks faced, and the adequacy of controls and procedures to address the risks identified
- requirements for the reporting of operational losses and proposed remedial action development of contingency plans
- training and professional development
- ethical and business standards
- risk mitigation, including insurance where this is effective.

**Estimation of fair values**

The methods and assumptions used in estimating the fair values of financial instruments were disclosed in note 3(a)(iv) of the significant accounting policies.

**Listed investments and convertible loans**

At 30 June 2013, the carrying amounts of debt and equity investments which fair values were determined directly, in full or in part, by reference to published price quotations amounted to \$6,304,679 (2012: \$10,890,505).

**Merchant Opportunities Fund**  
**ARSN 111 456 387**  
**Notes to the financial statements (continued)**  
**For the year ended 30 June 2013**

**Note 12 Financial instruments and associated risk (continued)**

**Unlisted investments**

Details of unlisted investments and the valuation approach as at 30 June 2013 are set out below:

	<b>Industry Sector</b>	<b>Basis of valuation</b>	<b>Date of transaction</b>	<b>Fair value as at 30 June 2013</b>	Fair value as at 30 June 2012
Esplanade Property Fund	Property	Net Asset value as at 30 June 2013	N/A	<b>\$1,390,914</b>	\$1,407,841
Inhouse Group Ltd*	Information Technology	Price of MOF's most recent sales transaction	November 2012	<b>\$933,589</b>	\$635,000
Vesuvius Minerals Ltd*	Materials	Price of MOF's most recent investment	October 2012	<b>\$430,000</b>	\$280,000
Condor Energy Services Ltd*	Oil & Gas	Price of most recent investment in Condor (third-party transaction)	December 2012	<b>\$392,000</b>	\$280,000
Valiant Resources Ltd*	Materials	Price of MOF's most recent investment	April 2012	<b>\$250,000</b>	\$250,000
Pilbara Commodities*	Energy	Price of MOF's recent investment	June 2013	<b>\$150,000</b>	–
<b>Total</b>				<b>\$3,546,503</b>	\$2,852,841

Esplanade Property Fund (EPF) is an unlisted managed investment scheme. This investment represents 14% of the Fund's net assets as at 30 June 2013. On 2 July 2012, EPF acquired a 12.5% interest in Village National Holdings Limited ("Village National"). The investment in Village National represents 51.8% of EPF's Net Assets. The price paid by EPF as compared to Village National's net assets as at 30 June 2013 indicates an enterprise value significantly greater than its net asset position which reflects the expected growth potential of Village National's business. The growth anticipated is underpinned by the expectation that Village National will be able to obtain long-term offtake/lease agreements with mining companies which in turn is dependent upon there being an upturn in the mining sector/key resource projects commencing. In the absence of such agreements, the scale and timing of growth required for Village National to achieve the necessary earnings level is uncertain, having an impact as to the fair value of the investment. Due to the level of judgement involved in valuing EPF's underlying portfolio, the investment in EPF has been classified from Level 2 to Level 3 during the year.

\* The investments in seed and start-up venture capital investments represent 22% of the Fund's net assets. The fair value of these investments is determined with reference to the most recent transaction price which is typically the capital raising price or the most recent third party sale price by MOF. Subsequent to the latest transaction, the Responsible Entity has re-assessed the business activities of these entities to determine whether any significant changes in the circumstances or events would imply a change in the investment's fair value as at balance sheet date.

**Merchant Opportunities Fund**  
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**Notes to the financial statements (continued)**  
**For the year ended 30 June 2013**

**Note 12 Financial instruments and associated risk (continued)**

The directors of Capricorn Investment Partners Limited have determined that the most recent transaction price paid represents the best estimate of fair value as at 30 June 2013.

**Fair Value measurements recognised in the statement of financial position**

The table below analyses financial instruments carried at fair value, by valuation method. The different levels have been defined as follows:

- Level 1 fair value measurements are those instruments valued based on quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2 fair value measurements are those instruments valued based on inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).
- Level 3 fair value measurements are those instruments valued based on techniques using significant unobservable inputs. This category includes all instruments for which the valuation technique includes inputs not based on observable data and the unobservable inputs have a significant effect on the instrument's valuation. This category includes instruments that are valued based on quoted prices for similar instruments for which significant unobservable adjustments or assumptions are required to reflect differences between the instruments.

<b>30 June 2013</b>	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>	<b>Total</b>
Financial assets classified as fair value through profit and loss	6,254,679	50,000	3,546,503	9,851,182

<b>30 June 2012</b>	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>	<b>Total</b>
Financial assets classified as fair value through profit and loss	8,982,664	1,907,841	1,445,000	12,335,505

**Merchant Opportunities Fund**  
**ARSN 111 456 387**  
**Notes to the financial statements (continued)**  
**For the year ended 30 June 2013**

**Note 12 Financial instruments and associated risk (continued)**

**Reconciliation of level 3 fair value measurements of financial assets**

	<b>Fair value through profit or loss</b>	<b>Fair value through profit or loss</b>
	<b>\$</b>	<b>\$</b>
	<b>2013</b>	<b>2012</b>
Opening	1,445,000	-
Total gains or losses in profit or loss	423,196	-
Purchases	300,000	1,445,000
Sales	(12,607)	-
Transfers into Level 3	1,390,914	-
Transfers out of Level 3	-	-
Closing	3,546,503	1,445,000
Total gains or losses for the period included in profit or loss for assets held at the end of the reporting period:	404,349	-

**Note 13 Related Party Transactions**

**(a) Responsible Entity**

The Responsible Entity of Merchant Opportunities Fund is Capricorn Investment Partners Limited (ABN 26 095 998 771). Merchant Funds Management Pty Ltd (ABN 32 154 493 277) is the appointed investment manager of the Fund, and is responsible for the day to day management of the Fund.

**(b) Details of Directors and Other Key Management Personnel**

*(i) Directors*

*The directors of Capricorn Investment Partners Limited (the Responsible Entity) during the year were:*

Stephen John Moss	Chairman (Executive)
David McKay French	Director (Executive)
Michael John Cranny	Director (Non-Executive)

**Merchant Opportunities Fund**  
**ARSN 111 456 387**  
**Notes to the financial statements (continued)**  
**For the year ended 30 June 2013**

**Note 13 Related Party Transactions (continued)**

*The directors of Entrust Funds Management Limited (the former Responsible Entity) during the period of appointment were:*

Graeme Mark Yukich	Chairman (executive)
Andrew Christopher Fry	Director (executive)
Bradley William Gordon	Director (executive)
David John Franklyn	Director (executive)

*(ii) Other Key Management Personnel*

Neither Merchant Opportunities Fund, Entrust Funds Management Limited nor Capricorn Investment Partners Limited employ persons deemed to be key management personnel (KMP) of the Fund. The Responsible Entity who manages the activities of the Fund is considered to be the KMP. The directors do not receive any compensation directly from Merchant Opportunities Fund, and there are no agreements in place between the directors and the Fund.

**(c) Loans to Directors**

The Fund has not made, guaranteed or secured, directly or indirectly any loans to the directors or their personally related entities at any time during the period.

**(d) Investments**

Details of investments in the Fund held by directors, including their related entities are set out below:

**2013**

<b>Director/ Related Entity up to 4 April 2013</b>	<b>Note</b>	<b>Number of units held at balance date</b>	<b>% Interest held</b>	<b>Number of units acquired during year</b>	<b>Number of units disposed of during year</b>	<b>Distribution paid or payable  \$</b>
Davington Pty Ltd	(i)(ii)	N/A	0.18	666	-	-

**Merchant Opportunities Fund**  
**ARSN 111 456 387**  
**Notes to the financial statements (continued)**  
**For the year ended 30 June 2013**

**Note 13 Related Party Transactions (continued)**

**2012**

<b>Director/ Related Entity</b>	<b>Note</b>	<b>Number of units held at balance date</b>	<b>% Interest held</b>	<b>Number of units acquired during year</b>	<b>Number of units disposed of during year</b>	<b>Distribution paid or payable  \$</b>
David John Franklyn		-	-	12,083	401,789	-
Davington Pty Ltd	(i)	30,915	0.18	16,050	502,765	464
Bradley William Gordon Superannuation Fund	(iii)	-	-	552	18,366	-

(i) Graeme Yukich is a director and equity holder of Davington Pty Ltd, which holds the units in Merchant Opportunities Fund.

(ii) Entrust Funds Management Ltd ceased to be the Responsible Entity of the Fund on 5 April 2013, therefore this holding is not held by a director or related entity as at 30 June 2013.

(iii) Bradley Gordon is a member of the Bradley William Gordon Superannuation Fund, which holds the units in Merchant Opportunities Fund.

**(e) Fees**

The former Responsible Entity, Entrust Funds Management Limited, the new Responsible Entity, Capricorn Investment Partners Limited, and the Fund Manager, Merchant Funds Management Pty Ltd, received all management and performance fees that have been deducted from the Fund during the period. Total management and performance fees paid to the Responsible Entity and Fund Manager during the period were \$92,067 (2012: \$150,556). The total compliance and accounts preparation fees paid to the Responsible Entity during the period was \$12,688 (2012: \$26,250).

Expenses incurred by the Responsible Entity during the period and reimbursed by the Fund in accordance with the Fund's constitution was nil (2012: \$35).

Capricorn Investment Partners Limited provides investment services to Merchant Opportunities Fund, and outsources custodial and administrative functions.

Transactions between Merchant Opportunities Fund and Capricorn Investment Partners result from normal dealings with that company as the Fund's Responsible Entity. Capricorn Investment Partners Limited is an Australian Financial Services license holder.



**Merchant Opportunities Fund**  
**ARSN 111 456 387**  
**Notes to the financial statements (continued)**  
**For the year ended 30 June 2013**

**Note 13 Related Party Transactions (continued)**

**(f) Related party investments of the Fund**

Details of the Fund's investment in other registered Funds of which the former Responsible Entity, Entrust Funds Management Ltd, is also the Responsible Entity are set out below:

	Fair value of unit holdings		% Interest held		Distributions received or receivable from related parties		Number of units acquired during the year	Number of units acquired during the year
	2013	2012	2013	2012	2013	2012	2013	2012
	\$	\$	%	%	\$	\$		
Esplanade Property Fund	1,390,914	1,407,841	7.35	7.45	40,813	63,631	718,997	673,347

The Responsible Entity has redeemed 301,525 units of Esplanade Property Fund when redemptions were opened in April 2013 (2012: nil).

The principal activity of the Esplanade Property Fund is investment in domestic listed and unlisted property trusts.

**(g) Related party transactions**

All transactions with related parties are conducted on normal commercial terms and conditions. From time to time the Responsible Entity or their director-related entities may invest in or withdraw from the Trust. These investments or withdrawals are on the same terms and conditions as those entered into by other Trust investors and are trivial and domestic in nature.

**(h) Other transactions within the Fund**

Apart from those details disclosed in this note, no director of the Responsible Entity has entered into a material contract with the Fund since the end of the previous year and there were no material contracts involving directors' interests subsisting at year end.

**Note 14 Contingencies**

There are no contingent liabilities or contingent assets at 30 June 2013 and 30 June 2012.

**Note 15 Events subsequent to reporting date**

There have been no events subsequent to balance date which would have a material effect on the Fund's financial statements at 30 June 2013.

**Merchant Opportunities Fund**  
**ARSN 111 456 387**  
**Directors' Declaration**  
**For the year ended 30 June 2013**

In the opinion of the Directors of Capricorn Investment Partners Limited, the Responsible Entity of the Merchant Opportunities Fund, I state that:

- (a) the financial statements and notes that are set out on pages 10 to 40 are in accordance with the Corporations Act 2001, including:
  - (i) giving a true and fair view of the Fund's financial position as at 30 June 2013 and of its performance for the year ended on that date; and
  - (ii) complying with Accounting Standards in Australia (including the Australian Accounting Interpretations) and the Corporations Regulations 2001; and
- (b) the Directors draw attention to Note 1(a) of the financial report which contains a statement of compliance with International Financial Reporting Standards; and
- (c) there are reasonable grounds to believe that the Fund will be able to pay its debts as and when they become due and payable.

Signed in Accordance with a Resolution of the Directors of  
Capricorn Investment Partners Limited



David French  
Director

Perth  
27<sup>th</sup> September 2013



## **Independent auditor's report to the directors of Capricorn Investment Partners Limited**

We have audited the compliance plan of Merchant Opportunities Fund (the Scheme) which was established by Entrust Funds Management Limited who acted as Responsible Entity for the Scheme for the period from 1 July 2012 to 5 April 2013 at which time Capricorn Investment Partners Limited, replaced it as the Responsible Entity and is still acting in that capacity.

The compliance plan was approved by the directors of the responsible entity on 30 September 2010 and lodged with Australian Securities Investment Commission (ASIC) on 1 October 2010.

### *Directors' responsibility for the compliance plan*

The directors of the responsible entity are responsible for ensuring that the Scheme compliance plan meets the requirements of Section 601HA of the *Corporations Act 2001*, including that it sets out adequate measures that the responsible entity is to apply in operating the schemes to ensure compliance with the *Corporations Act 2001* and the schemes' constitution, and for complying with the compliance plan. These responsibilities are set out in Part 5C.2 of the *Corporations Act 2001*. The directors' assertions regarding the design and operation of the compliance plan have been acknowledged in the attached directors' declaration dated 27 September 2013.

### *Auditor's responsibility*

Our responsibility is to express an opinion on whether the responsible entity complied with the compliance plan during the period ended 30 June 2013 and the compliance plan continues to meet the requirements of Part 5C.4 of the *Corporations Act 2001* as at that date, in all material respects.

We conducted our audit in accordance with Standards on Assurance Engagements. These Standards on Assurance Engagements require that we comply with relevant ethical requirements relating to assurance engagements and plan and perform the engagement to obtain reasonable assurance that the responsible entity complied with the compliance plan and the plan met the requirements of the *Corporations Act 2001*. Our procedures included obtaining an understanding of the compliance plan and the measures which it contains and examining, on a test basis, evidence supporting the operation of these measures. These procedures have been undertaken to form an opinion whether, in all material respects, the responsible entity has complied with the compliance plan during the period ended 30 June 2013, and the compliance plan continues to meet the requirements of Part 5C.4 of the *Corporations Act 2001* as at that date.

### *Use of report*

This audit report has been prepared for Capricorn Investment Partners Limited as the responsible entity of the Scheme in accordance with section 601HG of the *Corporations Act 2001*. We disclaim any assumption of responsibility for any reliance on this report, or the compliance plan to which it relates to any person or users other than the directors of the responsible entity, or for any purpose other than that for which it was prepared.



*Inherent limitations*

Because of the inherent limitations of any compliance measures, as documented in the compliance plan, it is possible that fraud, error, or non-compliance with laws and regulations may occur and not be detected. An audit is not designed to detect all weaknesses in a compliance plan and the measures in the plan, as an audit is not performed continuously throughout the period and the procedures performed on the compliance plan and measures were undertaken on a test basis.

Any projection of the evaluation of the compliance plan to future periods is subject to the risk that the compliance measures in the plan may become inadequate because of changes in conditions or circumstances, or that the degree of compliance with them may deteriorate.

The audit opinion expressed in this report has been formed on the above basis.

*Auditor's opinion*

In our opinion, in all material respects:

- a) Entrust Funds Management Limited (for the period 1 July 2012 to 5 April 2013) and Capricorn Investment Partners Limited (for the period 5 April 2013 to 30 June 2013) have complied with the Scheme's compliance plan for the period ended 30 June 2013; and
- b) the compliance plan lodged with ASIC on 1 October 2010 continues to meet the requirements of Part 5C.4 of the *Corporations Act 2001* as at 30 June 2013.

  
KPMG

  
Grant Robison  
Partner

Perth

27 September 2013