

## K2 Asset Management

Please contact K2 Client Services

Telephone 61 3 9691 6191 Email [invest@k2am.com.au](mailto:invest@k2am.com.au)

Website [www.k2am.com](http://www.k2am.com)



## Additional Information to the Product Disclosure Statement 19 September 2011

### K2 Asian Absolute Return Fund

ARSN 106 882 384 / APIR KAM0100AU

### K2 Australian Absolute Return Fund

ARSN 106 882 302 / APIR KAM0101AU

### K2 Select International Absolute Return Fund

ARSN 112 222 465 / APIR ETL0046AU

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#### Contact Details

To request a free printed copy of this document or the PDS, or updated information about performance, unit prices, fund size or other matters contact K2 Asset Management Ltd at:

Level 32, 101 Collins Street,  
Melbourne, VIC, 3000

**Phone:** +61 3 9691 6191

**Email:** [invest@k2am.com](mailto:invest@k2am.com)

**Fax:** +61 3 9691 6170

**Website:** [www.k2am.com](http://www.k2am.com)

Issued by

**K2 Asset Management**

ABN 95 085 445 094 / AFSL 244 393



***Please note:*** The information in the document forms part of the Product Disclosure Statements (PDSs) for the K2 Asian Absolute Return Fund, K2 Australian Absolute Return Fund and K2 Select International Absolute Return Fund (the **Funds**), all dated 19 September 2011. You should read this document and the applicable PDS before making a decision to invest in the relevant Fund. Defined terms in this document have the same meaning as in the applicable PDS and references to '**the Fund**' or '**the PDS**' are references to the Fund or PDS in which you wish to invest.

The information provided here is general information only. It does not take into account the investment objectives, financial situation or needs of any particular investor. You should not base your decision to invest in the Fund solely on this information. You should consider the suitability of a Fund in view of your financial position, investment objectives and needs, and you may want to seek professional advice before making an investment decision. K2 and its respective employees, agents and officers do not guarantee the success, repayment of capital, rate of return on income or capital, or investment performance of the Fund. Past performance is not a guarantee of future performance. Units in the Fund are offered and issued by K2 on the terms and conditions described in the PDS and this document. You should read the PDS and this Additional Information because you will become bound by them if you become an investor in the Fund. It is your obligation to seek any advice on, and observe any legal restrictions on investment in the Fund which may apply to you.



# 01

## Acquisition and disposal of Units

### Applications

#### Initial application for investment

Investors must complete the application form and new investors must also complete the relevant client identification form before the application can be processed. This form is required to enable K2 to comply with the Anti-Money Laundering and Counter-Terrorism Financing Act 2006.

#### Application dates

Applications can be processed on any Business Day in Melbourne (**Valuation Day**) with units issued for that same day, provided the completed forms and cleared funds have been accepted by the unit registry by 2.00 pm Australian Eastern Standard Time (**Deadline**) on a Valuation Day,

**Note: you will need to be aware of the relevant banks' processing times to ensure the unit registry receives cleared funds by the Deadline.**

Subject to the Corporations Act 2001 Cth (**Corporations Act**), application money received after the Deadline will be held in the Fund's trust account, unless directed otherwise in writing by the applicant, and units will be issued on the following Valuation Day. Any interest earned on application money (less applicable withholding tax) paid in advance of a Valuation Day will be accrued to the Fund, and will not be credited in favour of the applicant.

K2 cannot issue units until it has *received, identified and accepted*:

- payment; and
- the application form (and client identification form for new investors), with all applicable sections filled out.

K2 reserves the right to refuse any application without giving a reason. If K2 refuses or is unable to process an application it will return the application money to the applicant who will not be entitled to any interest on that money. Any interest earned is credited for the benefit of the Fund.

If a cheque or other deposit is dishonoured, the corresponding units are deemed not to have been issued. K2 and the unit registry accept no responsibility for any loss caused as a result of non-receipt of any application sent by facsimile, post or other delivery methods.

Investors should note the 'Risks of investing shortly before a distribution period' in section 3 of this document, if applicable. Applications that are placed for a 30 June or 31 December Valuation Date are allocated units on that day, and will receive a distribution, if the Fund is paying one.

#### Privacy

When processing an application, K2 will be collecting personal information which it may need to provide to its service providers or to regulatory authorities as required by law. The information will be used primarily to action the application, identify each investor and administer and manage the investments in the Fund. K2's privacy policy is set out on its website at [www.k2am.com](http://www.k2am.com).

#### Terms for electronic communication

By providing an email address in the application form or in later correspondence with K2, you:

- acknowledge that you have nominated to receive any information on your investment in, or correspondence regarding, the Fund (**Investment Information**) electronically;
- agree not to receive Investment Information by post and agree for Investment Information to be sent to the most recent email address K2 has on the register for you, even if there is a fax number. If there is no email address, you agree to be sent Investment Information by post to the most recent address K2 has on the register for you;
- acknowledge that electronic communication may be intercepted, copied, adapted or imitated by third parties and may not always be safe, reliable or timely;
- accept all risks associated with receiving Investment Information electronically, including the risk that an email sent to you may be infected with viruses or corrupted in any other manner; and
- agree that K2 has no responsibility and is not liable for any loss arising in connection with the Investment Information being sent electronically, including if you do not receive this or there is a delay in you receiving the Investment Information,



or the fact that the email may be corrupted or infected with viruses.

All appointed authorised signatories that provide K2 or the unit registry with an email address or fax number are taken to agree to the above terms, where a reference to 'you' is taken to be a reference to 'the authorised signatory'. Please contact K2 if you do not want to be bound by these Terms for electronic communication.

### **Investing through an IDPS**

If you are investing through an IDPS, such as a master trust or wrap account, you may need to complete a separate application form and provide a cheque payable to the relevant IDPS operator. You may need to contact the relevant IDPS operator regarding its application cut-off times for pricing purposes.

Indirect investors investing through an IDPS do not acquire the rights of an investor in a Fund. The rights of indirect investors are set out in the IDPS guide or other offer document for the relevant IDPS. If you invest through an IDPS, your rights and liabilities will be governed by the terms and conditions of the IDPS disclosure document. Investors should carefully read the terms and conditions of that document before investing in any of the Funds.

IDPS investors will receive reporting directly from the IDPS operator, not from K2; and do not have the right to 'cool off' (as described in the PDS) in relation to an investment in the Funds.

### **Additional investments (for existing investors)**

Investors can add to their investment by either completing an application form from a current PDS or completing an 'additional investment form' available at [www.k2am.com](http://www.k2am.com). Before completing an additional investment form investors should ensure they have read the current PDS.

## **Disposal of Units**

### **Making a withdrawal**

An investor wishing to make a withdrawal must give written notice to be received by 2.00pm on the Valuation Day.

Withdrawal proceeds will be remitted by electronic transfer to the investor's designated account, after K2 receives completed documents. In normal circumstances, this will be within five Business Days after the relevant Valuation Day.

The minimum withdrawal is \$10,000 (unless otherwise permitted by K2) provided a minimum balance of \$20,000 remains in the Fund, otherwise only a complete withdrawal is permitted.

It is recommended that withdrawal requests are completed on the redemption form available at [www.k2am.com](http://www.k2am.com). You may also write to us and provide us with your withdrawal instruction, however failure to provide sufficient information to identify your investment may delay your redemption payment.

### **Transfer of units**

Investors wishing to transfer units to a different entity must complete a standard transfer form, available at [www.k2am.com](http://www.k2am.com) or by contacting K2. Both the seller and buyer must provide their executed instruction on the same transfer form. If the buyer is a new investor to K2, they are also required to complete an initial application form and client identification form.

A transfer of units from one entity to another may have tax implications and you should seek independent advice before proceeding.

### **Switching Investments**

You may switch all or part of your investment between K2 Funds by completing a "Switch form" available at [www.k2am.com](http://www.k2am.com) under "Forms".

A switch is processed as a withdrawal and an additional investment and accordingly the buy-sell spread applies.

Transferring units may give rise to tax consequences and it is recommended that you obtain tax advice before switching.

Remember that a minimum investment of \$20,000 is required to keep your investment in a Fund open.

### **Terms for fax instructions**

Instructions may be submitted by facsimile on +61 3 9473 2140. By lodging a faxed request the investor releases, discharges and agrees to indemnify K2 from and against all losses, liabilities, actions, proceedings, account claims and demands arising from the fax request.

The investor also agrees that any payment made in accordance with faxed instructions shall be a complete satisfaction of the obligations of K2, notwithstanding any fact or circumstances including that the payment was made without the investor's knowledge or authority. The investor agrees that if the payment is made in accordance with these conditions, the investor shall have no claim against K2 in relation to the payment.



### Restrictions on transfer and illiquidity of units

Units are generally redeemable at the request of the investor, however an investor's right to withdraw an investment from a Fund is limited by the circumstances set out in the PDS (including the requirement for notice before 2pm on the applicable Valuation Day) and the Corporations Act.

### Suspension of issue of units and withdrawal of funds

Under the Funds' constitutions, K2 may suspend the determination of the Net Asset Value (**NAV**) of a Fund and/or extend the time for paying redemption proceeds during a period:

- in which an exchange or market on which investments in a Fund are quoted is closed or suspended
- where, in the opinion of K2, it is not practicable to sell investments or where a disposal would be prejudicial to investors
- where, in the opinion of K2, the NAV cannot reasonably or fairly be ascertained
- in which a Fund is unable to repatriate funds to make payments on redemption or during which any transfer of funds cannot, in the opinion of K2, be effected at normal rates of exchange.

No units may be issued or withdrawn during such periods of suspension.

Where a Fund is not liquid (as defined in the Corporations Act) an investor does not have a right to withdraw from that Fund and can only withdraw where K2 makes a withdrawal offer to investors in accordance with the Corporations Act. K2 is not obliged to make such offers.

### Unit pricing (NAV per unit)

The calculation of unit prices is set out in the constitution for each Fund and is performed by the Fund Administrator each Valuation Day. Broadly, unit pricing is calculated by:

1. calculating the Gross Asset Value of the Fund as at the relevant Valuation Day
2. deducting any liabilities (including management fee)
3. deducting any accrued performance fee after the deduction of liabilities

4. dividing the resulting NAV by the number of units on issue, this amount being rounded to the nearest cent (0.5 of a cent will be rounded up).

## 02 Additional features and benefits of the Fund

### Income distributions

Fund income is distributed on a semi-annual basis shortly after 30 June and 31 December each year. An investor's entitlement to income is based on the number of units held in a Fund at that time. K2 may change the distribution times, but will not do so without first notifying investors.

Income amounts can vary between distribution periods, and in some periods there may be no distribution.

Distributions will be paid by the method nominated on your application form, by either:

- reinvesting the distribution into additional units; or
- paying cash into a nominated account.

To alter instructions regarding the payment of distributions, investors must advise in writing at least five Business Days prior to 30 June or 31 December, as applicable.

## 03 The significant risks of managed investment schemes

The Fund can invest in the asset classes permitted under its Constitution, and each class carries varying degrees of risk. Risks that should be considered when investing in the Fund include, but are not restricted to, the following.

- **Interest rate risk** – changes to interest rates may impact economic conditions and stock valuations.
- **Market risk** – changes in regulatory and economic policy, political events, technology, economic cycles, investor sentiment, environment and social



climate can all impact financial markets.

- **Equity specific risk** – companies in which the Funds invest can have specific factors, including change in management or major product recall, that can impact that company's stock valuation.
- **Liquidity risk** – securities may become illiquid and as a result it may be difficult to exit a position. K2 aims to mitigate liquidity risk by only investing in those markets that provide reasonable liquidity. K2 regularly conducts portfolio liquidity testing to assess the time frames required to exit current positions.
- **Currency risk** – currency risk occurs where the underlying assets of a Fund are denominated in currencies other than the Australian dollar. Changes in exchange rates will create gains or losses. K2 aims to reduce this risk through active currency management.
- **Short selling risk** – Short selling carries particular risks that traditional Long positions do not. With a Long position, the value of the asset cannot drop below zero, thereby placing a limit on the possible loss inherent in the asset. In a Short position, where the purchaser expects the asset to depreciate, there is a risk that the asset could appreciate. Short selling theoretically has unlimited risk of loss because there is no limit on the level to which a position may appreciate before the position is closed out. K2 mitigates this risk by restricting exposure to Short positions. Stop loss strategies are also employed to provide investment managers with instant notification when a position falls below a defined performance target. This enables investment managers to immediately execute a trade to minimise the loss on that position. It is a mechanism to minimise losses when the prices of Short positions are rising or alternatively when prices on Long positions are falling.
- **Derivative risk** – the Funds may use various derivative instruments, including futures, options, forward contracts and other derivatives, which may be volatile and speculative.
- **Leverage and borrowing risk** – The Funds may hold positions that have leveraged exposure to the underlying asset (i.e. where the financial instrument can be purchased by depositing only a percentage of the instrument's face value). Therefore, a relatively small price movement in a financial instrument's value may result in immediate and substantial gains or losses to the investor.

- **Counterparty and broker credit risk** – credit risk is the risk of loss caused by another party, including the prime broker or administrator, defaulting on their financial obligations. K2 seeks to mitigate these risks via various measures, including using a separate custodian to hold Fund assets, making them unavailable to creditors of the Prime Broker.

## More information about Counterparty Risk

### About the Prime Broker

Morgan Stanley & Co. International plc (the **Prime Broker**) and other Morgan Stanley companies provide prime brokerage services to the Fund such as clearing, settlement, stock borrowing and foreign exchange facilities. K2 also uses Morgan Stanley companies and other brokers and dealers to execute transactions for the Fund.

The Prime Broker also provides a custody service for all the Fund's investments held on the books of the Prime Broker as part of its prime brokerage function in accordance with the rules of the Financial Services Authority (**FSA**) of the United Kingdom by which it is regulated in the conduct of its investment business. The Prime Broker may appoint sub-custodians of such investments, including other Morgan Stanley companies,

### Identificaton and segregation of Fund assets

In accordance with FSA rules, the Prime Broker will identify, record and hold the Fund's investments held by it as custodian in such a manner that the identity and location of the investments can be identified at any time and that such investments are readily identifiable as belonging to a customer of the Prime Broker and are separately identifiable from the Prime Broker's own investments.

### Collateral and some other investments may not be segregated

However, investments which constitute collateral for the purposes of the FSA rules, as described below, may not be segregated from the Prime Broker's own investments and may be available to creditors of the Prime Broker or the Morgan Stanley companies. Furthermore, in the event that any of the Fund's investments are registered in the name of the Prime Broker where (due to the nature of the law or market practice of jurisdictions outside the United Kingdom) it is in the Fund's best interests to do so or it is not feasible to do otherwise, such investments will not be segregated from the Prime Broker's own investments



and in the event of the Prime Broker's default may not be as well protected.

#### **Protection of cash – client money rules**

The Prime Broker will treat money received from the Fund as client money (Client Money) in accordance with the terms of the FSA's Rules. The legal and regulatory regime applying to parties holding Client Money outside the EEA may be different to that of the UK and in the event of their default such money may be treated in a different manner from that which would apply if the money was held by such a party in an EEA state.

#### **Security over Fund assets**

As security for the payment and discharge of all liabilities of the Fund to the Prime Broker and the Morgan Stanley companies, the investments and cash held by the Prime Broker and each such Morgan Stanley Company will be charged by the Fund in their favour and will therefore constitute collateral for the purposes of the FSA rules. Investments and cash may also be deposited by the Fund with the Prime Broker and other members of the Morgan Stanley group of companies as margin and will also constitute collateral for the purposes of the FSA rules.

#### **Borrowing of Fund assets**

The Fund's investments may be borrowed, lent or otherwise used by the Prime Broker and the Morgan Stanley companies for their own purposes, whereupon such investments will become the property of the Prime Broker or the relevant Morgan Stanley company and the Fund will have a right against the Prime Broker or the relevant Morgan Stanley Company for the return of equivalent assets. The Fund will rank as an unsecured creditor in relation thereto and, in the event of the insolvency of the Prime Broker or the relevant Morgan Stanley company, the Fund may not be able to recover such equivalent assets in full. K2 and the Prime Broker have agreed to certain limitations on the borrowing and use of Fund assets.

#### **Liability and indemnity of the Prime Broker**

Neither the Prime Broker nor any Morgan Stanley company will be liable for any loss to the Fund resulting from any act or omission in relation to the services provided under the terms of the Agreement unless such loss results directly from the negligence, wilful default or fraud of the Prime Broker or any Morgan Stanley company. The Prime Broker will not be liable for the solvency, acts or omissions of any sub-custodians or other third party by whom or in whose control any of the Fund's investments or cash may be held. The Prime Broker and the Morgan Stanley companies accept the same level of responsibility for nominee companies controlled by them as for their own acts. The Fund has

agreed to indemnify the Prime Broker and the Morgan Stanley companies against any loss suffered by, and any claims made against, them arising out of the Agreement, save where such loss or claims result primarily from the negligence, wilful default or fraud of the indemnified person.

#### **About the Custodian**

Morgan Stanley Private Bank, National Association (the **Custodian**), a U.S. national banking association, regulated by the Officer of the Comptroller of the Currency, and the Federal Deposit Insurance Corporation will provide custody services to the Fund. These include the maintenance of cash and securities accounts, safe custody of assets, income collection, corporate actions and voting rights processing (other than certain voluntary corporate actions), and certain reporting services.

#### **Sub-custodians**

The Custodian may appoint any person to act as a sub-custodian or a depository bank of the Fund's investments and cash, provided, that with respect to each appointment of a sub-custodian or depository bank, the Custodian: (i) exercises reasonable skill, care and diligence in the selection of such sub-custodian or depository bank; (ii) satisfies itself as to the ongoing suitability of the sub-custodian or depository bank to provide sub-custodial or depository services, as the case may be, to the Custodian; (iii) maintains an appropriate level of supervision over the sub-custodian or depository bank; (iv) makes appropriate enquiries periodically to confirm that the obligations of the sub-custodian or depository bank continue to be competently discharged; and (v) does not appoint any entity in the Morgan Stanley group of companies to act as either of a sub-custodian or a depository bank in respect of such investments and cash.

#### **Movement and segregation of Fund assets**

The Custodian is authorised to transfer certain of the Fund's investments to the Fund's prime brokerage account with the Prime Broker in the case that either: (i) K2 instructs the Prime Broker to transfer or sell to a third party certain assets held partially or wholly in its account(s) at the Custodian; and/or (ii) the Custodian has received notification of certain voluntary corporate actions in respect of any of the investments held by the Custodian on behalf of the Fund.

The Custodian will identify, record and hold the Fund's investments held by it as custodian in such a manner that the identity and location of the investments can be identified at any time and that such investments are readily identifiable as belonging to a customer of the



Custodian and are separately identifiable from the Custodian's own investments.

The Custodian may pool the Fund's assets held by it with assets held for its other clients provided that the Custodian's books and records will reflect the ownership of such securities for each customer, including the Fund.

#### **No borrowing of Fund assets held by Custodian**

The Custodian is not permitted to borrow, lend, charge, rehypothecate, dispose of or otherwise use for its benefit any investment held in custody on behalf of the Fund.

#### **Custody of cash**

The Custodian is required to hold any cash received from the Fund in a custodial cash account at a depository bank and such custodial cash account shall contain only cash held for customers of the Custodian. The Custodian is required to request each depository bank to maintain the custodial cash account on such depository bank's records in the name of Custodian as agent for the Custodian's customers. With respect to United States dollars held in a custodial cash account established at a depository bank whose deposits are insured by the US Federal Deposit Insurance Corporation, the Custodian will maintain records of beneficial ownership of cash to establish the Fund's interest in such custodial cash account.

The Custodian and the Fund have acknowledged in the custody agreement that cash held in a custodial cash account shall constitute a 'special' deposit and shall not constitute a general deposit with the Custodian creating a debtor-creditor relationship between the Fund and the Custodian. While the Custodian is an 'insured depository institution', as defined in the Federal Deposit Insurance Act, as amended (**FDIA**) and certain cash deposits maintained at the Custodian are insured by the FDIC to the extent permitted by applicable law, as noted above, the Custodian holds the Fund's custodial cash accounts at depository banks and the availability of deposit insurance, if any, would depend on the amount of cash deposits held in custodial accounts as well as on the status of that institution as an insured depository institution. Any assets held in custody in the Fund's securities accounts at the Custodian are not insured by the U.S. Treasury, the Federal Reserve, the FDIC, the Securities Investor Protection Corporation or any other government, government agency or self-regulatory organization, in the event of an insolvency of the Custodian or otherwise.

#### **Security over Fund assets**

The Fund has granted a security interest, general lien and right of set off over the assets of the Fund held by

the Custodian as security for the discharge of any monies, debts and obligations of the Fund to the Custodian.

#### **Liability and indemnity of the Custodian**

Neither the Custodian nor any other Morgan Stanley entity will be liable to the Fund for loss, liability, claim, damage, tax or expense (including legal fees and expenses) (**Loss**) resulting from any act or omission in relation to the custody services provided except in the event of the Custodian's gross negligence or willful misconduct. Neither the Custodian nor any Morgan Stanley entity will be liable to the Fund for any special, indirect, punitive, incidental or consequential damages of any nature whatsoever arising from any act or omission of any Morgan Stanley entity, sub-custodian or depository bank, whether or not the possibility of such damage was disclosed to, or could have been reasonably foreseen by, the Custodian or any Morgan Stanley entity, sub-custodian or depository bank.

The Fund has agreed to indemnify the Custodian and any Morgan Stanley entity against any Loss suffered or incurred by the Custodian or any Morgan Stanley entity in connection with the Fund's assets held by the Custodian or the performance of the services provided to the Fund by the Custodian or any Morgan Stanley entity provided that neither the Custodian nor any Morgan Stanley entity will be indemnified against any Loss to the extent that such Loss is a direct result of the gross negligence or willful misconduct of the Custodian.

The Prime Broker and Custodian are service providers to the Fund and are not responsible for the preparation of this document or the activities of the Fund and therefore accept no responsibility for any information contained in this document. The Prime Broker and Custodian do not participate in the investment decision-making process.

K2 may remove the Fund's Prime Broker; Custodian; Administrator (State Street Australia Limited) or Unit Registry (Computershare Fund Services) and appoint a replacement at any time without notice to investors.

#### **Liability and indemnity of the Responsible Entity**

K2 is indemnified out of the Funds against all liabilities and expenses incurred by it in properly performing any of its duties, exercising any of its powers, or omitting to act in relation to the Funds, or attempting to do so. Subject to the Corporations Act, provided K2 acts in good faith and without negligence, it is not liable to investors for losses in relation to the Funds (except, in certain circumstances, where the it can be indemnified from the Fund).



## 04 Additional explanation of fees and expenses

### Buy/Sell spread

A buy/sell spread of +/-0.4% is charged on applications and redemptions to cover the transaction costs of buying and selling the underlying investments. It ensures other investors are not disadvantaged by brokerage and transaction costs associated with providing daily liquidity.

### Investment management fee

The investment management fee of 1.5375% (including GST and RITC) per annum of the Gross Asset Value of the Fund is paid to K2 for managing each of the Funds' investments. It is paid to K2 out of the assets of each Fund in accordance with its constitution.

### Estimated expense recoveries

K2 is entitled to be reimbursed for certain expenses incurred in managing the Funds. These expenses include the fees payable to the Administrator, Unit Registry, Prime Broker and Custodian, and other expenses relating to the compliance, investment management, management and administration of the Fund.

There are other expenses that include tax and operating costs, such as audit, legal and tax consulting fees, which are also recoverable out of the assets of the Funds. K2 is entitled to be reimbursed for the full amount of these expenses. K2 has the right to recover all proper and reasonable expenses from the Funds, and the estimated figure may increase or decrease accordingly.

### Estimated responsible entity fee

A responsible entity fee is charged by K2 to cover direct and indirect costs which relate to K2 acting as the responsible entity of the Funds, such as the maintenance of a compliance committee. The amount is reviewed bi-annually by K2, but cannot exceed 0.07% of the Gross Asset Value of each Fund.

### Performance fee expense

A performance fee expense may be payable, depending on the performance return of each Fund, and is payable out of the assets of each Fund. The performance fee is calculated as follows.

1. The NAV per unit is calculated for each of the Funds.

2. Where the NAV exceeds the High Water Mark, the performance fee is calculated at 20.5% (inclusive of GST, less RITC) of the amount by which the respective NAV exceeds the High Water Mark.
3. In the case of the K2 Asian Absolute Return Fund and K2 Australian Absolute Return Fund, a performance fee will only apply when the Fund's performance exceeds net 6% performance return above the High Water Mark. When this hurdle is achieved the performance fee is applicable on the total performance above the High Water Mark.

The 6% hurdle can be changed by K2 on 90 days' notice to investors, although K2 does not anticipate this to change over the life of the current PDS.

The **High Water Mark** is determined by:

- a) where a performance fee is paid or payable in respect of the immediately preceding half financial year, the highest NAV per unit from which a performance fee has been last deducted in the immediately preceding half financial year; or
- b) where a performance fee is not payable in respect of the immediately preceding half financial year, the higher of:
  - I. the NAV per unit as at the end of the immediately preceding half financial year, and
  - II. either the relevant NAV on the date of your initial subscription in the first half financial year of investment or the last NAV from which a performance fee has been paid, if any.

The performance fee is accrued daily and withdrawals during a financial year will attract a pro-rata performance fee with the actual return being annualised (calculated as at the Business Day for which the relevant units are redeemed). For all investors who have not redeemed during the year, the performance fee, when applicable, is calculated as at 30 June and 31 December and paid annually in July and January.

### Performance fees explained

Performance fees reward investment managers for exceeding specified performance hurdles. In addition to meeting the specified performance hurdles, if applicable, the investment manager must exceed a High Water Mark before a performance fee can apply.



A High Water Mark is a NAV price above which the investment manager is eligible to charge a performance fee, subject to meeting a performance hurdle (if applicable). If the current NAV falls below the High Water Mark, K2 must reach the High Water Mark before receiving a performance fee on additional performance.

**Example:** if a starting balance \$50,000 investment fell to \$45,000, K2 would not be entitled to a performance fee until the balance exceeds \$50,000 (the High Water Mark) again. For the K2 Asian and K2 Australian Absolute Return Funds the balance is required to exceed the High Water Mark and net 6% performance hurdle above \$50,000 for a performance fee to apply.

**Performance fee example – K2 Asian Absolute Return Fund**

The table below presents a range of scenarios for an investor in the K2 Asian Absolute Return Fund in terms of when and what performance fees might be payable.

**Other fees and expenses**

**Commissions payable to financial advisers**

The Funds do not pay commissions to any person.

**Transaction and other costs**

All Government taxes such as GST will be deducted from the Funds as appropriate. Reduced Input Tax Credits (RITC) will also be claimed by the Funds where applicable. GST and RITC do not apply to international assets held by the Funds. As such, the proportion of GST and RITC charged to each Fund will vary. The Funds may incur transaction costs such as brokerage, settlement costs (including custody costs), clearing costs and stamp duty. These costs are an additional cost and will reduce the NAV of each respective Fund.

Fund Performance	Performance Condition	Performance Fee Outcome
-1%	Below the High Water Mark	No performance fee payable
3%	Above the High Water Below the 6% hurdle Mark	No performance fee payable
6%	Above the High Water Mark Equal to the 6% hurdle	No performance fee payable – the performance of the Fund must exceed the High Water Mark and the 6% hurdle to incur a performance fee expense  (Note that the K2 Select International Fund does not have a 6% hurdle)
10%	Above the High Water Mark Exceeds the 6% hurdle requirement	If the Fund obtains a 10% return, therefore exceeding the 6% hurdle and meeting the performance fee requirements, based on a \$50,000 investment the investor will be charged \$1,025  (Performance fee of 20.50% per annum applied to performance above the High Water Mark)
20%	Above the High Water Mark Exceeds the 6% hurdle requirement	If the Fund obtains a 20% return, therefore exceeding the 6% hurdle and meeting the performance fee requirements, based on a \$50,000 investment the investor will be charged \$2,050  (Performance fee of 20.50% per annum applied to performance above the High Water Mark)



## 05 Taxation of registered managed investment schemes

The following information is a tax summary based on tax laws current at the date of this document. The purpose of this information is to provide a general outline of the Australian tax implications for Australian resident investors who hold an interest in the Funds on capital account. This general summary is not intended to be authoritative or a complete statement of the applicable laws. Prospective investors are advised to seek independent professional advice relevant to their own particular circumstances before investing in the Funds.

### Taxation of the Funds

The Funds are registered within Australia for tax purposes, with income determined for each Fund annually.

The Funds have made the MIT capital account election. Consequently, all gains and losses from disposal of qualifying assets (for example shares in a company or units in a unit trust) are treated as being on capital account for tax purposes. This election is irrevocable.

On the basis that investors are presently entitled to the net income of each Fund (including net taxable capital gains), pursuant to the existing income tax legislation, the Funds should not be subject to Australian income tax. In the case where a Fund makes a loss, for tax purposes the Fund cannot distribute the loss to investors. However, subject to that Fund meeting certain conditions, the Fund may be able to take into account the losses in subsequent years.

Due to the possibility of investors moving into and out of each Fund at different points in time, there is a risk that taxation liabilities in respect of gains that have benefited past investors may have to be met by subsequent investors.

From 1 July 2010, the Taxation of Financial Arrangements (TOFA) provisions applied mandatorily to certain taxpayers in respect of qualifying financial arrangements. Broadly, the TOFA regime impacts the timing and recognition of gains and losses on qualifying financial arrangements. The Funds have not made any elections to apply elective methodologies under TOFA.

### Taxation of resident investors

Generally, an investor's entitlement to the net income of a Fund for a financial year forms part of the investor's assessable income for that year. This includes distributions that investors have elected to have reinvested into additional units in the Funds.

### Risks of investing shortly before a distribution

A distribution of income generally forms part of an investor's assessable income, and investors will be liable to pay tax on that income. At the time of distribution, the value of each unit will be reduced by the distribution amount.

Distribution of income is not based on the amount of time investors have held units in the Fund, but rather the number of units an investor holds at the distribution date (31 December and 30 June).

Investors purchasing units on or shortly before a distribution date will receive the full distribution entitlement for the number of units they hold at the distribution date. Such distributions (depending on the investor's tax circumstances) will be likely to create a tax liability for the investor.

Distributions from the Funds to investors may include capital gains realised by the Fund. Investors that are individuals or superannuation funds may be entitled to a capital gains discount where the capital gain has arisen from an investment held continuously by the Fund for at least 12 months. Companies are not entitled to the discount.

### Imputation credits and franked dividends

Income distributions from the Funds may include an entitlement to franked dividends. Generally, investors should include the franked dividends and the franking credits (imputation credits) they receive in their assessable income. Certain additional requirements, including the 45-day holding period rule may need to be satisfied in order to obtain franking credits in relation to dividends. The investor's particular circumstances (and those of the applicable Fund) will be relevant to determine whether the investor is entitled to any franking credits in respect of their share of the franked dividends.

### Foreign income

The Funds may derive foreign sourced income that is subject to tax overseas. Investors should include their share of both the foreign income and the amount of the foreign tax credits in their assessable income. Investors may be entitled to foreign tax credits that may be used to offset the Australian tax payable on the foreign source income.



### **Foreign investment funds (FIF) and Foreign accumulation funds (FAF)**

The former FIF regime has been abolished with effect from 1 July 2010. It is anticipated that the FIF regime will be replaced by the FAF regime. Based on Exposure Draft legislation released by the Government on 17 February 2011, it is expected that the new regime will seek to tax foreign investments which do not annually distribute income from certain investments. On this basis, the FAF rules are unlikely to apply to the Funds.

### **Tax free distributions and tax deferred distributions**

Distributions of non-assessable amounts are generally not subject to tax. Examples of non-assessable amounts include distributions comprising amounts attributable to deductions for capital allowances. Although the receipt of non-assessable amounts is generally not subject to tax, the receipt of certain non-assessable amounts may have capital gains tax consequences. Broadly, the receipt of certain non-assessable amounts may reduce the cost base of the investor's investment in a Fund. The impact of the reduction to the cost base may result in either an increased capital gain or a reduced capital loss on the subsequent disposal of the investment in a Fund.

### **Disposal of units by investors**

Any taxable capital gain arising from the disposal of an investment in any of the Funds may form part of the investor's assessable income. Investors that are individuals, trusts, and complying superannuation funds may be eligible for the discount capital gain concession if their investment has been held for 12 months or more, and the relevant Fund – and the investor – satisfies certain other requirements.

Any capital losses arising from the disposal of the investment may be used to offset other capital gains the investor may have derived.

## **06 Information for New Zealand investors**

- (a) This offer to New Zealand investors is a regulated offer made under Australian and New Zealand law. In Australia, this is Chapter 8 of the Corporations Act 2001 and Regulations. In New Zealand, this is Part 5 of the Securities Act 1978 and the Securities (Mutual Recognition of Securities Offerings-Australia) Regulations 2008.
- (b) This offer and the content of the offer document are principally governed by Australian rather than New Zealand law. In the main, the Corporations Act 2001 and Regulations (Australia) set out how the offer must be made.
- (c) There are differences in how securities are regulated under Australian law. For example, the disclosure of fees for collective investment schemes is different under the Australian regime.
- (d) The rights, remedies, and compensation arrangements available to New Zealand investors in Australian securities may differ from the rights, remedies, and compensation arrangements for New Zealand securities.
- (e) Both the Australian and New Zealand securities regulators have enforcement responsibilities in relation to this offer. If you need to make a complaint about this offer, please contact the Securities Commission, Wellington, New Zealand. The Australian and New Zealand regulators will work together to settle your complaint.
- (f) The taxation treatment of Australian securities is not the same as for New Zealand securities.
- (g) If you are uncertain about whether this investment is appropriate for you, you should seek the advice of an appropriately qualified financial adviser.
- (h) The offer may involve a currency exchange risk. The currency for the securities is not New Zealand dollars. The value of the securities will go up or down according to changes in the exchange rate between that currency and New Zealand dollars. These changes may be significant.
- (i) If you expect the securities to pay any amounts in a currency that is not New Zealand dollars, you may incur significant fees in having the funds credited to a bank account in New Zealand in New Zealand dollars.
- (j) The dispute resolution process described in this offer document is only available in Australia and is not available in New Zealand.