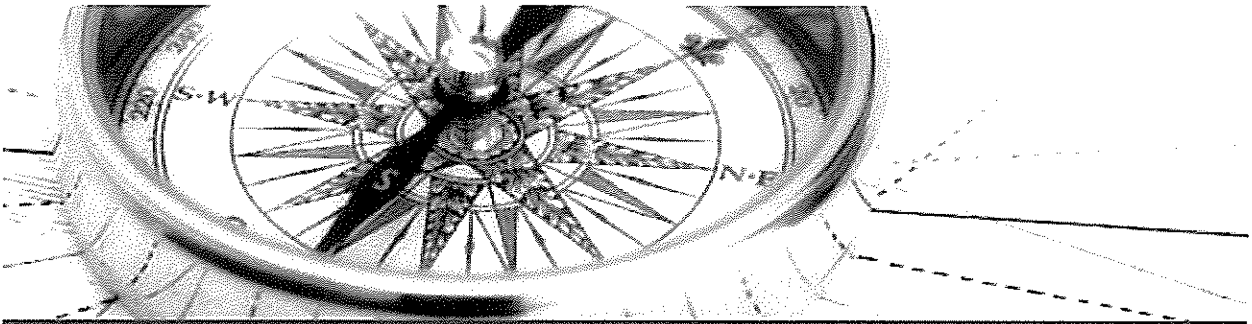
Independent Adviser's Report



New Dawn Energy Limited

Prepared Pursuant to Rule 22 of the New Zealand Takeovers Code in Relation to a Full Takeover Offer for L&M Energy Limited

October 2012

Purpose of the Report

- This report is not a report on the merits of the offer.
- This report has been obtained by the offeror.
- The purpose of this report is solely to compare the consideration and terms offered for the different classes of securities, and to certify as to the fairness and reasonableness of that consideration and terms as between the different classes.
- A separate independent adviser's report on the merits of the offer, commissioned by the directors of L&M Energy Limited, must accompany L&M Energy Limited's target company statement.
- The offer should be read in conjunction with this report and the separate independent adviser's report on the merits of the offer.

Statement of Independence

Northington Partners Limited confirms that it:

- Has no conflict of interest that could affect its ability to provide an unbiased report; and
- Has no direct or indirect pecuniary or other interest in the proposed transaction considered in this report, including any success or contingency fee or remuneration, other than to receive the cash fee for providing this report.

Northington Partners Limited has satisfied the Takeovers Panel, on the basis of the material provided to the Panel, that it is independent under the Takeovers Code for the purposes of preparing this report.

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Abbreviations and Definitions

A$	Australian dollars
ASX	Australian Stock Exchange
Code	The Takeovers Code
Consideration Options	Options issued by LME As part of the consideration agreed in December 2009 to be paid by LME to acquire all the shares in L&M Coal Seam Gas Holdings Limited
ESOP	Employee Share Option Plan
ESOP Options	Options issued by LME under the terms of its ESOP
Exercise Price	The exercise price for a particular Tranche of Options
LME or Company	L&M Energy Limited
New Dawn	New Dawn Energy Limited
Northington Partners	Northington Partners Limited
NZ$	New Zealand dollars
NZSX	New Zealand Stock Exchange
Offer	The full takeover offer that New Dawn intends to make for all of the voting and non-voting securities on issue in LME
Option Offer Price	The cash payment offered by New Dawn for each Tranche of Option
Options	The 71,865,000 options issued by LME and currently outstanding either as ESOP Options or Consideration Options
Ordinary Shares	The 754,405,518 ordinary shares of LME on issue and which are tradable on the Australian and New Zealand Stock Exchanges
Share Offer Price	A cash payment of A$0.06 per Ordinary Share of LME offered by New Dawn
Tranche	Each, or any of, the various tranches of Options issued by LME, as the context requires

1.0 Introduction and Summary of Our Assessment

1.1 Introduction

New Dawn Energy Limited ("**New Dawn**"), a company associated with Geoff Loudon, intends to issue a Takeover Notice to L&M Energy Limited ("**LME**" or "**Company**") on or about 22 October 2012 indicating its intention to make a full takeover offer ("**Offer**") for all the equity securities on issue in LME.

Under New Zealand company law, LME has two categories of equity securities. As at 22 October 2012, those categories comprised:

- 754,405,518 issued ordinary shares ("**Ordinary Shares**") which are traded on both the Australian and New Zealand Stock Exchanges; and
- 71,865,000 options ("**Options**") which (as summarised in Table 1 below) have been issued:
  - In 12 tranches (each a "**Tranche**") pursuant to an employee share option plan ("**ESOP**") for key executives of the Company; and
  - As part of the consideration agreed in December 2009 to be paid by LME to acquire all the shares in L&M Coal Seam Gas Holdings Limited ("**Consideration Options**").

The Ordinary Shares are voting securities and the Options are non-voting securities. Each Tranche of the ESOP Options and the Consideration Options constitutes a separate class of non-voting securities for the purposes of the Takeovers Code ("**Code**").

Table 1: Summary of Options as at 22 October 2012

Scheme	Tranche	Expiry Date	Options Outstanding	Options Vested	Exercise Price
ESOP	1	30/10/2012	220,000	220,000	A$0.20
	2	15/04/2013	1,875,000	1,875,000	A$0.20
	3	5/11/2013	220,000	165,000	A$0.125
	4	27/04/2014	1,875,000	1,406,250	A$0.10
	5	12/11/2014	120,000	60,000	A$0.11
	6	17/03/2015	280,000	140,000	A$0.14
	7	28/04/2015	3,175,000	1,587,500	A$0.14
	8	10/11/2015	2,750,000	687,500	A$0.12
	9	2/05/2016	11,250,00	2,812,500	A$0.12
	10	7/11/2016	2,750,000	0	A$0.12
	11	28/02/2017	2,750,000	0	A$0.07
	12	28/06/2017	11,250,000	0	A$0.12
Total ESOP			38,515,000	8,953,750	
Consideration Options	E	26/02/2015	33,350,000	27,050,000	NZ$0.0001
Total			71,865,000	36,003,750	

Source: LME

Key terms and conditions of the Offer are as follows:

- **Offer Price for Ordinary Shares:** A cash payment of A$0.06 per Ordinary Share ("**Share Offer Price**");
- **Offer Price for Options:** The cash payment offered per Option varies across each Tranche of Options remaining on issue and as between the vested and non-vested Consideration Options, as set out in Table 2 below ("**Option Offer Price**").

Table 2: Offer Price for Options

Scheme	Tranche	Option Offer Price (A$)
ESOP	1	0.0000
	2	0.0004
	3	0.0059
	4	0.0115
	5	0.0135
	6	0.0126
	7	0.0127
	8	0.0168
	9	0.0178
	10	0.0196
	11	0.0255
	12	0.0202
Consideration Options - Vested	E	0.0599
Consideration Options – Non-vested	E	0.0554

Source: New Dawn Takeover Notice

- **Minimum Acceptance Condition:** The Offer is conditional upon New Dawn receiving acceptances that would confer on it 90% or more of the voting rights in LME.
- **Other Conditions:** The Offer is also conditional on certain regulatory approvals in New Zealand, as well as a number of other matters that are standard for an offer of this type.

Rule 8(4) of the Code requires that if non-voting securities are included in a full offer, the consideration and terms offered for non-voting securities must be fair and reasonable in comparison with the consideration and terms offered for voting securities and as between classes of non-voting securities. In this particular case, the Code therefore requires that:

- The consideration and terms offered for the Options must be fair and reasonable compared to the consideration and terms offered for the Ordinary Shares; and
- The consideration and terms offered for each Tranche of Options must be fair and reasonable as between all of the Tranches.

With the approval of LME, New Dawn has obtained access to information in relation to the ESOP and the Consideration Options. This report has been prepared based on information provided to us by New Dawn (or its advisers) and LME.

1.2 Summary of Our Assessment

A Rule 22 report is not required to consider the merits of the Offer for the Ordinary Shares, and we offer no opinion on whether the Share Offer Price of A$0.06 is fair and reasonable. Rather, our role is to determine whether the Option Offer Price (offered for each Tranche of Options) is fair and reasonable in comparison to the amount offered for the Ordinary Shares and as between each Tranche.

Our assessment is based on the following framework:

- The total consideration of A$0.06 per share for the Ordinary Shares provides the benchmark for our assessment. Although we make no attempt to determine whether the Share Offer Price is itself fair and reasonable, the Share Offer Price is the starting point from which we determine the relative fairness of the Offer for each Tranche of Options.
- That is, we need to determine the underlying fair value of the Options issued under each Tranche, assuming an initial fair value for the Ordinary Shares of A$0.06. Our assessment also takes into account the current rules that govern the ESOP Options and the Consideration Options, with particular emphasis on the rules that are relevant in the event of a successful takeover offer for LME.
- The assessment then rests on a comparison of the consideration offered for the Options in each Tranche to the underlying fair value of the Options.

Our estimate of the current fair value range of the Options in each Tranche is set out in Table 3 below.

Table 3: Estimated Fair Value Range for Options

Scheme	Tranche	Options Outstanding	Low Value per Option (A$)	High Value per Option (A$)	Mid-Point Value per Option (A$)	Total Tranche Value (A$)[1]
ESOP	1	220,000	0.0000	0.0000	0.0000	0
	2	1,875,000	0.0001	0.0007	0.0004	728
	3	220,000	0.0041	0.0077	0.0059	1,296
	4	1,875,000	0.0091	0.0138	0.0115	21,484
	5	120,000	0.0108	0.0162	0.0135	1,619
	6	280,000	0.0097	0.0155	0.0126	3,521
	7	3,175,000	0.0098	0.0156	0.0127	40,424
	8	2,750,000	0.0137	0.0199	0.0168	46,194
	9	11,250,00	0.0148	0.0209	0.0178	200,468
	10	2,750,000	0.0165	0.0228	0.0196	54,030
	11	2,750,000	0.0229	0.0282	0.0255	70,253
	12	11,250,000	0.0172	0.0232	0.0202	227,112
Total ESOP		**38,515,000**				**667,129**
Consideration Options - Vested	E	27,050,000	0.0599	0.0599	0.0599	1,620,994
Consideration Options – Non-vested	E	6,300,000	0.0554	0.0554	0.0554	349,218
Total Consideration Options		**33,350,000**				**1,970,211**

1. Calculated as Options Outstanding x Mid-Point Value per Option (subject to rounding).

Source: Northington Partners Analysis

The Option Offer Prices (as set out in Table 2) have been set equal to our assessed mid-point value for each Tranche of Options (as set out in Table 3). As such, we believe that the holders of the Options should realise the same value for the Options from either accepting the Offer or retaining the Options and pursuing the best strategy available under the relevant rules governing the Options. On this basis, we conclude that the Option Offer Price for each Tranche of Options is fair compared to the Share Offer Price.

We also note that:

- Both the holders of the Ordinary Shares and the Options will be paid cash if they are capable of accepting and accept the Offer, and the Offer to each group is effectively conditional on the same set of general conditions. On this basis, we conclude that the terms of the Offer for the Ordinary Shares and each Tranche of the Options are equivalent.
- The Option Offer Price for each Tranche has been determined using the same general valuation framework, with adjustments principally to account for differences in the expiry dates for each Tranche.

We therefore certify that in our opinion the consideration and terms offered for non-voting securities (being the Options) is fair and reasonable in comparison with the terms offered for the voting securities (being the Ordinary Shares). We also conclude that the terms offered for each Tranche of Options are fair and reasonable as between all of the Tranches.

2.0 Scope of this Report

2.1 Background

New Dawn intends to issue a Takeover Notice to LME on or about 22 October 2012 indicating its intention to make a full takeover offer for all of the equity securities on issue in LME.

Under New Zealand company law, LME has two categories of equity securities. As at 22 October 2012 there were 754,405,518 Ordinary Shares on issue (which can be traded on both the Australian and New Zealand Stock Exchanges), and 71,865,000 Options that comprised those issued under the terms of the Company's ESOP and the Consideration Options. The Ordinary Shares are considered voting securities and the Options are considered non-voting securities for the purposes of the Code.

The ESOP Options were issued to key Company executives (and one non-employee consulting contractor) in 12 Tranches. When issued, the Option holder had the right to convert each Option into one Ordinary Share upon payment of an exercise price ("**Exercise Price**"). The Exercise Prices for the ESOP Options range from A$0.07 to A$0.20. Each Tranche of ESOP Options has a different expiry date and therefore represents a separate class of non-voting securities.

The Consideration Options were issued following a transaction in December 2009 pursuant to which LME agreed to acquire all the shares in L&M Coal Gas Holdings Limited. The vast majority of the Consideration Options vested immediately upon issue, with 12,600,000 set to vest on a deferred basis ("**Deferred Vesting Consideration Options**"). The Exercise Price in respect of all the Consideration Options is NZ$0.0001.

Further details of the terms and conditions of both the ESOP Options and the Consideration Options are included in Section 3.2.

2.2 Requirements of Takeovers Code

LME is a publicly listed company on the ASX and NZSX and is a "Code Company" as defined by Rule 3 of the Code. The takeover process initiated by New Dawn must therefore comply with the provisions set out in the Code relating to the Offer procedure.

Pursuant to Rule 8(2) of the Code, a full offer must include offers in respect of all the securities in each class of equity securities of the target company (other than those that are already held by the offeror). Furthermore, Rule 8(4) of the Code requires that if non-voting securities are included in a full offer, the consideration and terms offered for non-voting securities must be fair and reasonable in comparison with the consideration and terms offered for voting securities and as between classes of non-voting securities. In this particular case, the Code therefore requires that:

- The consideration and terms offered for the Options must be fair and reasonable compared to the consideration and terms offered for the Ordinary Shares; and
- The consideration and terms offered for each Tranche of Options must be fair and reasonable as between all of the Tranches.

For the purposes of the Code, LME's Ordinary Shares are regarded as one class of equity security and each Tranche of the Options is regarded as a separate class of equity security given the different features of each Tranche. New Dawn as offeror must obtain a report pursuant to Rule 22 of the Code from an independent adviser which certifies that, in the adviser's opinion, the offer complies with Rule 8(4).

This report has been prepared to meet the requirements of Rule 22 of the Code. The appointment of Northington Partners Limited ("**Northington Partners**") to prepare the Rule 22 report was approved by the Takeovers Panel on 2 October 2012.

2.3 Assessment Approach

Rule 22 of the Code requires that the independent adviser's report certifies that the consideration and terms are fair and reasonable in comparison with the consideration and terms offered for voting securities and as between the classes of non-voting securities. The exact meaning of the words "*fair*" and "*reasonable*" is not prescribed in the Code and there is no well accepted, authoritative New Zealand reference that clearly establishes what should be considered for an assessment of this nature.

Statutory requirements within the Australian market are defined in somewhat more detail. The Australian Securities and Investments Commission has issued a policy statement regarding "Independent Expert Reports to Shareholders", which sets out some fundamental requirements for a report that is completed in similar circumstances to those relating to this Offer.

According to the policy statement, an offer is "fair" if the value of the consideration to be paid under the offer is equal to or greater than the value of the securities that are subject to the offer. An offer is deemed to be "reasonable" if it is fair. An offer may also be reasonable if it is unfair but where other significant factors mean that the shareholders should accept the offer in the absence of any higher bid before the close of the offer.

We believe that these definitions provide a useful starting point for assessing the fairness and reasonableness of the consideration offered for each class of equity securities under the Offer. Fairness is determined largely from the results of a comparative valuation exercise, while the reasonableness of the Offer is related to a general assessment of a range of other non-price terms that may be relevant in this case.

For this particular assessment, we have adopted the following framework to determine whether the consideration offered for each Tranche of Options is fair and reasonable in comparison to the offer price per share for the Ordinary Shares, and as between the Tranches of Options:

- Comparison of the gross consideration offered for all of the voting and non-voting securities is examined on a before investor tax basis.
- The Share Offer Price of A$0.06 provides the benchmark for our assessment in relation to the Options. Although we make no attempt to determine whether this Share Offer Price is itself fair and reasonable, the Share Offer Price is the starting point from which we determine the relative fairness of the Offer for each class (i.e. Tranche) of Options.
- That is, we need to determine the underlying fair value of each Tranche of Options, assuming an initial fair value for the Ordinary Shares of A$0.06. Our assessment also takes into account the current rules that govern the ESOP Options and Consideration Options.
- The assessment then rests on a comparison of the net consideration offered for each Tranche of Options to the underlying fair value of each Tranche of Options.

We believe that the assessment of the Offer terms relating to the Ordinary Shares in comparison to the Offer terms relating to each Tranche of Options is inconsequential in this case. Both the holders of the Ordinary Shares and the holders of the Options will receive cash consideration if they are capable of accepting and accept the Offer, and the Offer to each group of stakeholders is effectively contingent on the same set of conditions. On this basis, we conclude that the terms of the Offer are equivalent as between the voting and non-voting securities.

Our overall assessment therefore concentrates on a comparison of the consideration that will be offered for each class of security, based on an examination of the following factors:

- The consideration offered for the Ordinary Shares and each Tranche of Options;
- The differential between the Exercise Price for each Tranche of Options and the Offer price for the Ordinary Shares;
- The current rights of the holders of the Options, specifically with regard to transferability and the circumstances and timing of the conversion into Ordinary Shares; and
- The circumstances under which an Option holder's rights to the Options are relinquished.

We again note that we have not attempted to assess the underlying value of the Ordinary Shares, but have used the Share Offer Price as the benchmark for our assessment of the relativities between the offers for the different classes of securities.

2.4 Primary Sources of Information

The sources of information that we have relied on in preparing this report are set out in Appendix I.

2.5 Limitations and Reliance on Information

This report is subject to all of the limitations and restrictions set out in Section 5.0. In particular, in preparing this report, Northington Partners has relied on information supplied by New Dawn (or its advisers) and LME and has assumed the honesty and accuracy of this information. Northington Partners accepts no responsibility for inaccurate information supplied by New Dawn or LME, or for any failure by New Dawn or LME to provide relevant information.

Our assessment is reliant on a number of key assumptions that have been outlined in this report. Should any of these assumptions not be accurate, then the valuation assessment and our conclusions could be materially affected.

Subject to this limitation, we have obtained all of the information that we consider is necessary for preparing the report.

3.0 L&M Energy Equity Securities

3.1 Background to Offer Participants

New Dawn is an entity associated with Geoff Loudon, who is Chairman of LME and a substantial security holder in the Company, with a shareholding of approximately 28%. Mr Loudon is an international resource professional experienced in exploration, development, production and finance in Australasia, Asia, the Americas and Europe. He moved to New Zealand permanently in April 2010 from London, UK.

LME is a Wellington-based oil and gas exploration company, listed on the ASX and NZSX. LME's exploration strategy focuses on exploring for conventional oil and gas within proven hydrocarbon producing basins while maintaining upside potential through a portfolio of unconventional plays.

3.2 Key Terms of LME Equity Securities

3.2.1 Ordinary Shares

There are currently 754,405,518 Ordinary Shares on issue in LME. Each Ordinary Share confers:

- The right on a poll at a meeting of shareholders to one vote on each resolution;
- The right to an equal share in dividends authorised by the Board; and
- The right to an equal share in the distribution of the surplus assets of the Company.

3.2.2 Options

The Options issued by LME comprise those issued under the terms of the ESOP and the Consideration Options. Since their issue, a number of the ESOP Options have been cancelled under the rules of the ESOP, and some of the Consideration Options have been exercised. As summarised in Table 4 below, a total of 71,865,000 Options remain outstanding as at 22 October 2012.

Table 4: Summary of Options as at 22 October 2012

Scheme	Tranche	Expiry Date	Options Outstanding	Options Vested	Exercise Price
ESOP	1	30/10/2012	220,000	220,000	A$0.20
	2	15/04/2013	1,875,000	1,875,000	A$0.20
	3	5/11/2013	220,000	165,000	A$0.125
	4	27/04/2014	1,875,000	1,406,250	A$0.10
	5	12/11/2014	120,000	60,000	A$0.11
	6	17/03/2015	280,000	140,000	A$0.14
	7	28/04/2015	3,175,000	1,587,500	A$0.14
	8	10/11/2015	2,750,000	687,500	A$0.12
	9	2/05/2016	11,250,00	2,812,500	A$0.12
	10	7/11/2016	2,750,000	0	A$0.12
	11	28/02/2017	2,750,000	0	A$0.07
	12	28/06/2017	11,250,000	0	A$0.12
Total ESOP			**38,515,000**	**8,953,750**	
Consideration Options	E	26/02/2015	33,350,000	27,050,000	NZ$0.0001
Total			**71,865,000**	**36,003,750**	

Source: LME

3.2.3 Summary of the Material Terms of the Options

The terms and conditions of the Options are substantially similar except for the Exercise Price and the vesting terms for the vast majority of the Consideration Options (which vested immediately upon their issue). A summary of the material terms of the Options are set out in Table 5 below.

Table 5: Summary of Material Terms of the Options

Material Term	Commentary
Exercise Price	ESOP Options: range from A$0.07 to A$0.20. Consideration Options: NZ$0.0001.
Option Life and Vesting Period	All of the Options have been issued with a 5 year life from the date of issue. For the ESOP Options and 12,600,000 Deferred Vesting Consideration Options, the Options vest at a rate of 25% over the first four years of their life. 6,300,000 of the Deferred Vesting Consideration Options have vested and 20,750,000 of the outstanding Consideration Options vested immediately upon their issue.
Payment Terms	No consideration has been paid for the Options.
Exercise Requirements	A notice of exercise must be in a prescribed form (or otherwise in a form approved by the Company's Board) and be accompanied by payment of the relevant Exercise Price.
Transferability	The ESOP Options are not able to be transferred to other parties (other than by transmission on death of the Option holder or with the written approval of the Board). Consideration Options that have vested can be transferred to other parties to whom securities in the Company may be issued without the issue of a disclosure document, prospectus or similar document required under either Australian or New Zealand law.
Dividend	The Options attract no dividend rights.
Voting	The Options carry no voting rights.
Variations of Capital	In the event of a variation to the Company's capital (e.g. bonus issues, rights issues, returns of capital), provision is made (as the case may be) for either an adjustment to the number of Ordinary Shares issued for each Option upon exercise or an adjustment to the Exercise Price.

Expiry and Forfeiture	▪ All Options expire at the end of the period five years after their issue date.
	▪ For the ESOP Options and the Deferred Vesting Consideration Options:
	  ▪ Any non-vested Options lapse in the event that the Option holder ceases to be employed by the Company; and
	  ▪ Options that have vested at the time the Option holder ceases to be employed by the Company must be exercised within a prescribed period following the termination of employment or otherwise lapse.
	▪ Consideration Options which vested immediately upon issue can be exercised at any time prior to the end of their five year life, with no requirement for the Option holder to maintain employment with the Company.

Source: Northington Partners Analysis

3.2.4 Option Holder Rights upon a Takeover Offer

Pursuant to the terms and conditions of the relevant Options, in the event that the Offer becomes unconditional:

- The vesting date for any ESOP Options that have not vested is brought forward to the date on which the Offer becomes unconditional. In effect, all ESOP options will become fully vested if the Offer becomes unconditional. Although there is a general restriction on the ability to transfer

ESOP Options, such a transfer may be made with the written agreement of the Company's Board. We would expect all the ESOP Option holders to be granted permission by the Board to transfer the Options (which is a condition of the Offer), thereby allowing them to accept the Offer.

- The holders of the Consideration Options that vested immediately upon their issue will be capable of accepting the Offer – none of these Options have expired or are close to expiry and there is no specific restriction on transfer.
- To the extent that Deferred Vesting Consideration Options have vested (6,300,000 such Options are in this category), the holders of these vested Options will also be capable of accepting the Offer – again, none of these options have expired or are close to expiry and no specific restriction on transfer exists.
- To the extent that Deferred Vesting Consideration Options have not vested (6,300,000 such Options are in this category), the position is less certain. Although a specific provision exists in the event of a takeover for the immediate vesting of the non-vested portion of these Options if the Option holder's employment is terminated (other than by the Option holder), there is no mention of what happens if the Option holder's employment is not terminated. Based on advice we have received from legal counsel to both the Company and New Dawn, the "preferred" interpretation and conclusion from a review of the relevant provisions is as follows:
  - It is a condition to the vesting of these Options that the Option holder is employed by the Company;
  - Although vested Options can be transferred, it is implicit that non-vested Options cannot be transferred. Non-vested Options are expressly not included in the power of transfer that applies to vested Options;
  - The non-vested Options are treated as being personal to the employee holder. This conclusion is consistent with the employment condition for vesting of the Options (i.e. a transferee of the non-vested Options could not meet this condition);
  - There is no provision for the Company's Board to amend the terms of the Options so as to allow for the non-vested portion of the Options to vest upon a takeover offer; and
  - Accordingly, although the Offer will extend to the holders of the non-vested portion of the Deferred Vesting Consideration Options, the holders of these non-vested Options will not be capable of accepting the Offer.

4.0 Valuation of the Options

4.1 Introduction to the Valuation Framework

Each of the Options on issue effectively provides the Option holder with the right to purchase an Ordinary Share at some time in the future at a fixed price. Because the Option holder is not obligated to eventually make the purchase unless it is in their best interest to do so, the Options can be viewed as a variant of a standard call option[1]. An Option holder will rationally only choose to convert Options of a particular Tranche into Ordinary Shares if the market price of the Ordinary Shares exceeds the Exercise Price of that Tranche. If the market price is lower than the Exercise Price at the expiry of the relevant exercise period, the Option holder will obviously choose to let the Options expire by taking no further action.

Because the rights attached to the Options will only have value in the future if the LME Ordinary Share price exceeds the Exercise Price before the relevant expiry date, current value is related to an assessment of the likelihood that the Ordinary Share price will exceed the relevant Exercise Price before the expiry date of a particular Tranche. There are a number of mathematical models with which to determine the probability that the Options will have a positive payoff in the future, and which 'translate' that probability into an Option value today. We use some standard models as the basis for our assessment, on the assumption that the underlying LME shares will continue to trade on either the ASX or NZSX for the remaining life of the Options.

Unfortunately, although the analogy between the rights attached to the Options and a standard call option is reasonably strong, the terms and conditions of the Options have some features that are commonly attached to more complex employee share option schemes. These features include the following:

- The rights attached to the ESOP Options and the non-vested portion of the Deferred Vesting Consideration Options are not able to be traded; and
- Generally, the rights attached to the ESOP Options and the non-vested portion of the Deferred Vesting Consideration Options lapse if the Option holder ceases to be employed by LME.

Option features of this type are more difficult to value than standard equity options for a number of reasons, and mean that the well known Black-Scholes valuation formula is inappropriate. The Black-Scholes model was derived for simple European-style[2] options on a non-dividend paying share, assuming that the option instrument trades in a liquid market and has a relatively short time to maturity (6 – 9 months). Because most of these conditions do not hold for the rights attached to the Options, values derived from the Black-Scholes model are likely to be inaccurate and, in this case, will overstate the underlying fair value.

From a valuation perspective, the key complications relate to the fact that a significant portion of the Options are non-tradeable and are effectively cancelled if the Option holder leaves the Company prior to the relevant expiry date of the Options. This type of option is therefore often exercised earlier than is optimal for standard options, thereby reducing the payoff that could have been received had the option been retained for the full term. Expected dividend payments during the life of the option also reduce the value because of the corresponding decrease in the value of the underlying share.

[1] A call option provides the holder with the right, but not the obligation, to purchase an asset at a fixed price either during, or at the termination of, a specified future period.

[2] European-style options can only be exercised on the expiration date, while American-style options can be exercised at any time prior to maturity. The rights attached to the Options are American-style, but only to the extent that they have vested.

Although there are a range of alternative models available that attempt to incorporate the impact of the features of employee share options, implementation is difficult because all alternative models require an extra set of parameters. Unfortunately, appropriate values for the additional parameters cannot be directly observed and there is usually no useful data that can be used to estimate the values.

The usual approach to deal with these issues is to use a standard option pricing model to estimate some benchmark values, initially ignoring the value impacts of the Option features. Appropriate value discounts to reflect factors such as non-tradability and the potential for forfeiture can then be derived from available empirical studies.

4.2 Assessed Valuation Range

Table 6 presents the most important parameters for the benchmark valuation model, along with the selected values.

Table 6: Key Parameters for Benchmark Valuation Model

Parameter	Discussion	Chosen Value
Initial Share Value	Set equal to the Share Offer Price of A$0.06.	A$0.06
Exercise Prices	ESOP Options: range from A$0.07 to A$0.20. Consideration Options: NZ$0.0001.	Actual Exercise Price by Tranche
Volatility	This parameter determines the likelihood that the Ordinary Share price will exceed the Exercise Price of the relevant Tranche of Options prior to their expiry date. The higher the volatility, the greater the probability that the Option will finish in-the-money, and the greater the current Option value. This parameter cannot be directly observed, and we have based our range on the recent market volatility of LME share prices. The raw LME volatility estimates have also been benchmarked against a broad range of estimates for listed Australian companies operating in the same sector as LME. Given LME's very limited trading volume and low share price, validation against a broader sample is important to ensure that the LME estimates are not overly sensitive to the selected data sample.	70% - 90%
Expected Dividends	No dividends have been paid by LME over recent years. Without any indication to the contrary, we assume that future dividends (for valuation purposes) are set to zero.	Nil
Expiry Dates and Exercise Feature	The ESOP Options and the Deferred Vesting Consideration Options have a maturity structure analogous to what is known as a "partial window" option, in that the rights attached to each allotment can only be exercised during a "window" over the full term of the Option scheme. For example, for the ESOP Options under Tranche 11, the first 25% of these Options do not vest (and cannot therefore be exercised) until 7 November 2012, and can then be exercised at any time until the expiry date for that Tranche, being 7 November 2016. However, because it can be shown that it is not optimal to force the early exercise of an Option on a non-dividend paying share, an accurate representation of the maturity structure of this Option scheme will have no impact on the estimated benchmark value of the Options. We can therefore assume that the Options are only exercisable at the relevant expiry date for each Tranche.	Equal to the Expiry Date for each Tranche

Source: Northington Partners Analysis

Given the assumptions made in relation to the effective exercise date and future dividend stream, the theoretical values for the Options can in this case be appropriately determined using the standard Black-Scholes model. These starting values, prior to any allowance for factors such as lack of marketability and the inability to transfer the rights attached to the Options, are set out in Table 7. Prior to making the appropriate adjustments, the presented values represent an absolute upper limit for the actual fair value of each Tranche of Options.

Table 7: Upper Limit for Value of Options

Class	Tranche	Benchmark Value Per Option (A$) Low (Volatility 70%)	High (Volatility 90%)
ESOP	1	0.0000	0.0000
	2	0.0001	0.0008
	3	0.0051	0.0096
	4	0.0116	0.0175
	5	0.0137	0.0206
	6	0.0123	0.0197
	7	0.0129	0.0205
	8	0.0180	0.0261
	9	0.0203	0.0288
	10	0.0227	0.0315
	11	0.0316	0.0388
	12	0.0254	0.0344
Consideration Options - Vested	E	0.0599	0.0599
Consideration Options – Non-Vested	E	0.0599	0.0599

Source: Northington Partners Analysis

Market evidence in relation to valuation discounts for the employee option features of the Options is relatively limited. While there are a number of model adjustments that can be implemented to estimate the impact of vesting requirements, forfeiture provisions, and non-transferability, it is usually not possible to test the validity of the additional assumptions needed to parameterise the models simply because traded prices for this type of option are not available.

Because most of these factors will usually lead the Option holders to exercise their rights to take up the Ordinary Shares earlier than appears to be optimal, the simplest adjustment to the standard pricing model involves a reduction in the assumed time to maturity. A reduction in the assumed life of the Option leads to a decrease in the assessed current value of the Option. While this approach is intuitively appealing, there is again no market data from which to determine what the most appropriate reduction in the option term may be in any particular case.

The appropriate valuation discount to apply to the theoretical model prices therefore remains largely a matter of judgement. Although market rules of thumb suggest discounts between 20% and 50% from the values derived from the most appropriate variant of the Black-Scholes model, our analysis suggests that the appropriate discount in this case should be in the range of 20% to 40%, with a higher discount rate generally applied to vesting dates for a particular Tranche that are later in time. The resulting mid-point of the value range for each Tranche (based on an averaging of the differing values for each vesting date within a Tranche) is presented in Table 8 below.

Table 8: Estimated Fair Value Range for Options

Scheme	Tranche	Options Outstanding	Low Value per Option (A$)	High Value per Option (A$)	Mid-Point Value per Option (A$)	Total Tranche Value (A$)[1]
ESOP	1	220,000	0.0000	0.0000	0.0000	0
	2	1,875,000	0.0001	0.0007	0.0004	728
	3	220,000	0.0041	0.0077	0.0059	1,296
	4	1,875,000	0.0091	0.0138	0.0115	21,484
	5	120,000	0.0108	0.0162	0.0135	1,619
	6	280,000	0.0097	0.0155	0.0126	3,521
	7	3,175,000	0.0098	0.0156	0.0127	40,424
	8	2,750,000	0.0137	0.0199	0.0168	46,194
	9	11,250,00	0.0148	0.0209	0.0178	200,468
	10	2,750,000	0.0165	0.0228	0.0196	54,030
	11	2,750,000	0.0229	0.0282	0.0255	70,253
	12	11,250,000	0.0172	0.0232	0.0202	227,112
Total ESOP		**38,515,000**				**667,129**
Consideration Options - Vested	E	27,050,000	0.0599	0.0599	0.0599	1,620,994
Consideration Options – Non-vested	E	6,300,000	0.0554	0.0554	0.0554	349,218
Total Consideration Options		**33,350,000**				**1,970,211**

1. Calculated as Options Outstanding x Mid Point Value Per Option. Note subject to rounding.

Source: Northington Partners Analysis

5.0 Qualifications, Declarations and Consents

5.1 Declarations

This report is dated 22 October 2012 and has been prepared by Northington Partners at the request of New Dawn to fulfil the reporting requirements pursuant to Rule 22 of the Code. This report, or any part of it, should not be reproduced or used for any other purpose. Northington Partners specifically disclaims any obligation or liability to any party whatsoever in the event that this report is supplied or applied for any purpose other than that for which it is intended.

Prior drafts of this report were provided to New Dawn for review and discussion. Although minor factual changes to the report were made after the release of the first draft, there were no changes to our methodology, analysis, or conclusions.

This report is provided for the benefit of all of the security holders of LME that are subject to the Offer, and Northington Partners consents to the distribution of this report to those people. The engagement terms did not contain any term which materially restricted the scope of our work.

5.2 Qualifications

Northington Partners provides an independent corporate advisory service to companies operating throughout New Zealand. The company specialises in mergers and acquisitions, capital raising support, expert opinions, financial instrument valuations, and business and share valuations. Northington Partners is retained by a mix of publicly listed companies, substantial privately held companies, and state owned enterprises.

The individuals responsible for preparing this report are Greg Anderson B.Com, M.Com (Hons), Ph.D and Steven Grant B.Com, LLB (Hons). Each individual has a wealth of experience in providing independent advice to clients relating to the value of business assets and equity instruments, as well as the choice of appropriate financial structures and governance issues. Greg Anderson also has a high level of expertise and extensive experience in valuing complex financial instruments including options, swaps, and hybrid debt and equity securities.

Northington Partners has been responsible for the preparation of numerous Independent Reports in relation to takeovers, mergers, and a range of other transactions subject to the Code and NZX Listing Rules.

5.3 Independence

Northington Partners has not been previously engaged on any matter by New Dawn or LME or (to the best of our knowledge) by any other party to the proposed transaction. None of the Directors or employees of Northington Partners have any other relationship with any of the Directors or substantial security holders of the parties involved in the proposed Offer.

The preparation of this Rule 22 report will be Northington Partners' only involvement in relation to the proposed transaction. Northington Partners will be paid a fixed fee for its services which is in no way contingent on the outcome of our analysis or the content of our report.

Northington Partners does not have any conflict of interest that could affect its ability to provide an unbiased report.

5.4 Disclaimer and Restrictions on the Scope of Our Work

In preparing this report, Northington Partners has relied on information provided by New Dawn and LME. Northington Partners has not performed anything in the nature of an audit of that information, and does not express any opinion on the reliability, accuracy, or completeness of the information provided to us and upon which we have relied.

Northington Partners has used the provided information on the basis that it is true and accurate in material respects and not misleading by reason of omission or otherwise. Accordingly, neither Northington Partners nor its Directors, employees or agents, accept any responsibility or liability for any such information being inaccurate, incomplete, unreliable or not soundly based or for any errors in the analysis, statements and opinions provided in this report resulting directly or indirectly from any such circumstances or from any assumptions upon which this report is based proving unjustified.

We reserve the right, but will be under no obligation, to review or amend our report if any additional information which was in existence on the date of this report was not brought to our attention, or subsequently comes to light.

5.5 Indemnity

New Dawn has agreed to indemnify Northington Partners (to the maximum extent permitted by law) for all claims, proceedings, damages, losses (including consequential losses), fines, penalties, costs, charges and expenses (including legal fees and disbursements) suffered or incurred by Northington Partners in relation to the preparation of this report; except to the extent resulting from any act or omission of Northington Partners finally determined by a New Zealand Court of competent jurisdiction to constitute negligence or bad faith by Northington Partners.

New Dawn has also agreed to promptly fund Northington Partners for its reasonable costs and expenses (including legal fees and expenses) in dealing with such claims or proceedings upon presentation by Northington Partners of the relevant invoices.

Northington Partners Limited

Greg Anderson
Managing Director
www.northington.co.nz

Appendix I: Sources of Information Used in This Report

Other than the information sources referenced directly in the body of the report, this assessment is also reliant on the following sources of information:

- Copies of the agreements in relation to the Consideration Options that vested immediately upon their issue;
- Copies of the agreements in relation to the Deferred Vesting Consideration Options;
- The Plan rules for the Company's ESOP;
- L&M Energy Limited Annual Report for 2011;
- Various emails from Bell Gully as legal adviser to New Dawn, including details on the number of Options currently on issue, as well as the number that have vested and those that have not yet vested; and
- A copy of the draft Takeover Notice, with the latest version provided on 22 October 2012.

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