

The Impact of the Australian equivalents to International Financial Reporting Standards on Managed Investment Schemes AASB 124 'Related Party Disclosures'

Outline

For the majority of managed investment schemes, the 30 June 2006 financial report will be their first full set of financial statements compliant with Australian Equivalents to International Financial Reporting Standards (A-IFRS).

In December 2005, a revised AASB 124 'Related Party Disclosures' was issued by the Australian Accounting Standards Board which is applicable to annual reporting periods ending on or after 31 December 2005. The revised AASB 124 supersedes AASB 1046 'Director and Executive Disclosures by Disclosing Entities' (including AASB 1046A 'Amendments to Accounting Standard AASB 1046') and AASB 124 issued in July 2004.

For managed investment schemes, AASB 124 ('the standard') has caused considerable debate as the standard is silent as to how managed investment schemes should apply the disclosure requirements and there have been a number of possible alternatives debated by the industry sector and their advisors.

We explore below the issues and challenges facing Responsible Entities of managed investment schemes and propose our view of the required AASB 124 disclosures for managed investment schemes.

AASB 124

The standard is purely a disclosure standard as measurement rules are specified in other Australian Accounting Standards.

The standard introduces the concept of Key Management Personnel ('KMP') for whom compensation must be disclosed within the financial statements.

The standard applies to all entities that are reporting entities and those which prepare general purpose financial reports including all for-profit and not-for-profit, non-corporate entities. Certain additional detailed requirements only apply to those entities that are disclosing entities. As the standard provides no guidance on the impact on managed investment schemes, there is a need to apply judgement as to whether such disclosing entities have KMP that are compensated directly or indirectly by the entity based on the facts in each circumstance. There are varying interpretations of the standard, and opinions may change. This newsletter provides the current Deloitte view with regard to the particular circumstances of Managed Investment Schemes and KMP; it does not discuss the other related party transactions that are required to be disclosed by the standard.

Definitions

Some key definitions within the standard are set out below:

Key Management Personnel ('KMP'):

'those persons having authority and responsibility for planning, directing and controlling the activities of the entity, directly or indirectly, including any director (whether executive or otherwise) of that entity.'

Control: 'the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.'

Compensation: 'includes all employee benefits (as defined in AASB 119 Employee Benefits) including employee benefits to which AASB 2 Share-based Payment applies. Employee benefits are all forms of consideration paid, payable or provided by the entity, or on behalf of the entity, in exchange for services rendered to the entity. It also includes such consideration paid on behalf of a parent of the entity in respect of the entity.'

Compensation includes:

(a) **short-term employee benefits**, such as wages, salaries and social security contributions, paid annual leave and paid sick leave, profit-sharing and bonuses (if payable within twelve months of the end of the period) and non-monetary benefits (such as medical care, housing, cars and free or subsidised goods or services) for current employees

(b) **post-employment benefits** such as pensions, other retirement benefits, post-employment life insurance and post-employment medical care

(c) **other long-term employee benefits**, including long-service leave or sabbatical leave, jubilee or other long-service benefits, long-term disability benefits and, if they are not payable wholly within twelve months

after the end of the period, profit-sharing, bonuses and deferred compensation

(d) **termination benefits**

(e) **share-based payment.**

Key Management Personnel for Managed Investment Schemes

Managed investment schemes rarely have employees of their own and therefore the identification of KMP has the potential to be quite complex as it is a matter of judgement. The standard requires the substance of the relationships to be considered and not just the legal form. For a managed investment scheme the natural starting point for determining who the key management personnel may be is the Responsible Entity of the scheme.

The questions which require consideration are as follows:

1. What is required to be disclosed where KMP exist?

A managed investment scheme must disclose key management personnel compensation in total and for each of the following categories:

- (a) short-term employee benefits
- (b) post-employment benefits
- (c) other long-term benefits
- (d) termination benefits
- (e) share-based payment.

In addition, more detailed requirements are necessary for certain registered schemes as the Standard requires more extensive disclosure for each disclosing entity that is required to prepare financial reports in accordance with Part 2M.3 of the Corporations Act (registered schemes with more than 100

investors fall within this definition).

For such disclosing entities, for each KMP the following is also required:

- (a) the name of the person
- (b) the position held
- (c) where the period of responsibility is less than the reporting period, the date or dates identifying the period of responsibility.

If any of the following changes occur in the period after the reporting date and prior to the date when the financial report is authorised for issue, the name, position and date for each person involved shall be disclosed for:

- (a) each change in the chief executive officer and directors of the entity
- (b) the retirement of any key management person (other than a director or chief executive officer).

For each KMP, the components of each of the compensation categories must also be disclosed.

2. Can the Responsible Entity of the scheme be considered to be KMP as a corporate entity?

In our view, the Responsible Entity of the scheme cannot be considered to be a KMP as a corporate entity. In our view, the KMP must be individuals.

3. Do the directors of the Responsible Entity qualify as KMP of the scheme? If so, what amount should be disclosed as compensation?

The Responsible Entity has the authority and responsibility for planning, directing and controlling the activities of the managed investment scheme, then it follows that the directors of the Responsible Entity have that authority and responsibility as they are the decision makers, not the corporate entity

itself. Therefore they do qualify as KMP of the scheme.

The compensation paid to the directors of the Responsible Entity by the Responsible Entity is in part for services rendered to the managed investment scheme. In effect the Responsible Entity is compensating the KMP of the managed investment scheme on behalf of the managed investment scheme. In the majority of the cases, the compensation of the KMP is not paid directly by the scheme, nor is it generally paid by the Responsible Entity (or a related party) and directly reimbursed by the scheme. Generally the only fee incurred by the scheme payable to the Responsible Entity is the management fee and the management fee agreement may or may not prescribe whether this includes an element of compensation cost.

In our view, for consistency purposes, we believe the compensation to be disclosed in the financial report of the scheme should be the portion of the directors' compensation which can be attributed to the services they provide to the managed investment scheme, irrespective of which entity has paid that compensation. This is an area that is open to interpretation and will require clarity from the standard setters to ensure differences of opinion are eliminated.

4. Should you go further than just the directors of the Responsible Entity when considering who qualifies as KMP?

The KMP of a managed investment scheme should be considered in relation to the services rendered to and the operations of the managed investment scheme and therefore may extend to executives of the Responsible Entity and executives and directors of related companies but will not necessarily include all the executives

considered as KMP of the Responsible Entity. Similarly, there may be personnel at the Responsible Entity who are not considered KMP of the Responsible Entity but may be considered KMP of the scheme. The determination of who is KMP of the managed investment scheme is a judgement decision based on the facts of each scheme. However, where the Responsible Entity outsources any activities to a third party we believe key personnel of the outsourced entity are unlikely to be KMP.

5. Can an apportionment method be used to calculate compensation to be disclosed?

The Responsible Entity should determine the compensation to be disclosed as the portion of the compensation which can be attributed to the services provided by the KMP to the managed investment scheme. This is not inconsistent with the approach adopted in 2005 under the superseded AASB 1046.

6. Are comparatives required?

Comparative information is required for KMP if they would have been identified as a key management person in the prior period. Additionally there may be changes in compensation calculations as a result of changes in definitions and reference back to AASB 119 and AASB 2 for measurement principles. For example share based payments calculated and disclosed under the old AASB 1046 may not comply with the new AASB 2 requirements.

7. Where the senior management are not employed by or compensated by the Responsible Entity or scheme, does this mean they can be excluded from the definition of KMP?

The standard requires disclosure of all forms of consideration paid, payable or provided by an entity, or on behalf of the entity, in exchange for services rendered

to the entity. As a result the question of who makes the compensation payment and/or employs the staff, is in our view irrelevant in determining who are the KMP of any entity, including managed investment schemes.

Details of disclosure required for registered managed investment schemes that are disclosing entities

If you require illustrative disclosure, please refer to the Deloitte Illustrative Managed Investment Scheme Financial Report for the financial year ended 30 June 2006, at www.deloitte.com.au.

What should you do now?

Identify the KMP for your managed investment schemes.

Determine and document the type and method of calculation of the compensation and any apportionment of compensation.

Seek advice if you are unsure which personnel should be included in KMP and which should not, in your circumstances.

Regularly liaise with industry bodies such as IFSA and your advisors, as the accounting standards continue to be changed/enhanced.

New IASB Exposure Draft on Financial Instruments Puttable at Fair Value

On June 22nd, the IASB issued an Exposure Draft that proposes changes to the accounting for certain types of financial instruments that have characteristics similar to ordinary shares but are currently classified as financial liabilities. The AASB has followed with a similar A-IFRS Exposure Draft.

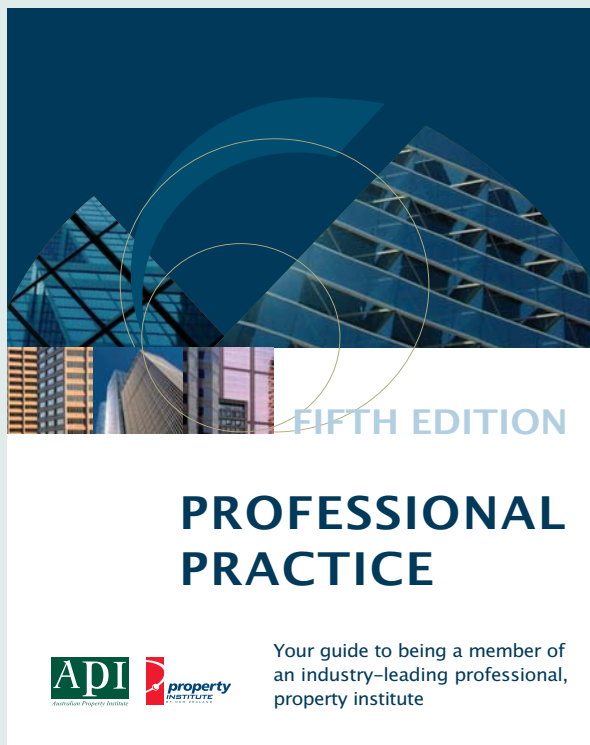
As noted in previous editions of this publication, AASB 132 currently requires unitholder funds in unlisted managed investment schemes to be classified in the balance sheet as a liability rather than equity because of the unitholders' right to redeem (or 'put') their units for cash.

Under the proposed amendments, units in unlisted managed investment schemes may be able to be classified as equity despite this 'put' feature i.e. the balance sheet presentation may return to the one in existence prior to financial years beginning on or after 1 January 2005. Care will need to be taken to ensure that the rights attaching to a scheme's units meet the specific requirements of the proposed new standard.

The IASB Exposure Draft has a comment period ending on 23 October 2006, and the Standard revisions should be issued thereafter subject to any comments arising. The AASB Exposure Draft has a comment period ending 22 September 2006.

Source: Deloitte and Minter Ellison Lawyers, "The Impact of the Australian equivalents to International Financial Reporting Standards on Managed Investment Schemes" July 2006. Published with permission of Deloitte and Minter Ellison Lawyers.

API/ PINZ Professional Practice 5th Edition



PROFESSIONAL PRACTICE 5th EDITION is the second Professional Practice jointly published by the Australian Property Institute (API) and the Property Institute of New Zealand (PINZ).

This fifth edition of Professional Practice represents the second stage toward the harmonisation of valuation and real property standards within Australia and New Zealand and reflects the continued move towards IVS. This edition of Professional Practice includes all the IVSC Applications, Standards and Guidance Notes, which have been drawn from IVS 2005. Interposed within the IVSC material is additional information to assist members in meeting local valuation and real property reporting requirements.

Hardcopies of API/ PINZ Professional Practice 5th edition are available for purchase from API National Office. Please visit the API National website at www.api.org.au to download an order form or please call API National Office on (02) 6282 2411.



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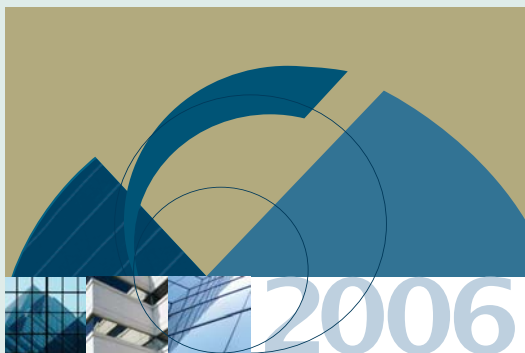
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For more information, go to www.avscopyerty.net.au, or signal your interest and provide details by email to avs@avscopyerty.net.au.



2006 RMM External Module

Members should be advised that the Australian Property Institute in association with Phillips Fox Lawyers are currently in the process of developing an external module of the RMM 2006 course. This course is scheduled to be available for members in September and will be available via API National Office. Further details including a registration form will be posted shortly on the API National Office website www.api.org.au or by contacting API National Office on 02 6282 2411.

Retail leasing perils in NSW

You are a landlord of a retail shop in nsw and your tenant's lease recently expired. The tenant is holding over and you negotiate a new short term lease with the tenant, since you plan to soon redevelop the premises. You give the tenant a letter with your proposed terms, adding the usual qualification that the parties will not be bound until a formal lease is executed. You invoice the tenant for the same rent as that payable under the expired lease. The tenant writes back accepting your terms. Guess what: you may have just entered into a five year lease with the tenant.

These were the circumstances in the May 2006 decision of the administrative decisions tribunal in *Helou & Ors v Bong Bong Pty Limited & Anor* [2006] NSW ADT128. In *Helou*, the tribunal followed two single judge decisions of the NSW Supreme Court, both by Hodgson CJ, and subsequent decisions of the tribunal, which considered Section 8 of the NSW Retail Leases Act (the Act).

Section 8 provides that a retail lease is entered into when a person enters into possession of the shop as lessee under the lease, or begins to pay rent as lessee under the lease, or when both parties execute the lease, whichever happens first.

In *Whiteway House (No.100) Pty Limited v Abrocoona Pty Ltd* [1998] NSWSC 521, Hodgson CJ found that under Section 8, a retail lease is entered into when the tenant enters into possession, or begins to pay rent, pursuant to a "consensus" as to the terms of the lease. The precise meaning of this "consensus" concept is far from certain, although it is clearly something short of an agreement enforceable under the general law. In a case before the

tribunal, *Randi Wixs Pty Limited v Pokana Pty Limited (No. 2)* [2003] NSW ADT 4, the tenant was a sitting tenant, pursuant to a holding over under a previous retail lease. The tribunal commented that if there was a "consensus" as to terms, there could be a notional "entry into possession" by a sitting tenant, even though there was no actual break in possession. However, in *Randi Wixs*, the tenant had commenced paying the higher rent in any event, so the test in Section 8 was satisfied, quite apart from the question of whether the tenant had entered into possession.

In *Helou*, the tribunal went one step further again. Not only was there no actual entry into possession (the tenant being a sitting tenant), there was no increase in the rent being paid. Nonetheless, the tribunal applied the comments in *Randi Wixs* and found there was a sufficient consensus as to terms so that a notional "entry into possession" arose, which satisfied the test in Section 8. This was despite the parties having qualified their negotiations as being subject to execution of formal lease documentation.

Helou illustrates that the qualifications commonly used while negotiating leases (e.g. "subject to board approval", "subject to lease execution") are likely to be ineffective when negotiating a retail lease with a sitting tenant. A particularly nasty sting for landlords is that although the "consensus" may have been for a term of less than 5 years, the lease actually entered into by the operation of Section 8 will be for a 5 year term, unless a Section 16(3) certificate is given by the tenant.

Apart from *Helou*, another anger for landlords lurks in the recent amendments to the Act. Formerly, if parties entered into a lease for a term of less than 6 months, where the tenant could not unilaterally renew or extend the lease, the lease was

not subject to the Act. The new section 6a provides that, under such leases commencing after 1 January 2006, if the tenant is in possession, or is entitled to be in possession, for a continuous period exceeding 12 months, then the act automatically applies to the lease from the day after that 12 month period expires. The tenant may then elect that the lease term be extended to five years.

The Helou case and the recent amendments to the act are a potential minefield for retail landlords. Landlords should obtain advice on how they can avoid or minimise the dangers involved.

Authors: David Ireland, Senior Associate and Colin Windeyer, Partner, Henry Davis York Lawyers.

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Lease market rent reviews – a new opening for tenants

The recent NSW Supreme Court decision in *Callaghan v Merivale CBD Pty Ltd* [2005] NSW SC 985 raised an intriguing possible ground for a tenant to attack its landlord's market rent review.

The case concerned a disputed market rent review under a lease of the Wynyard Hotel in Clarence Street, Sydney.

Clause 6(b) of the lease provided as follows:

At any time but not earlier than 120 days prior to each date specified in Item 7(b) ... or at any time thereafter the Lessor may by notice in writing to the Lessee fix the annual rent (subject as herein provided)

at an amount which in the opinion of the Lessor is the market rent of the Premises.

The lease then went on to give the lessee a right to object within 14 days and to provide for expert determination of the new rent in the event of such an objection.

The landlord served a notice on the tenant nominating the new "market" rent. The tenant, after the expiry of the allowed period of 14 days, purported to object to the new figure. The landlord challenged this objection, saying it was ineffective, as out of time. The tenant ended up paying the increased amount set by the landlord for a period of approximately 2 and half years, before bringing proceedings against the landlord, claiming that the landlord's nomination of the new "market" rent itself had been invalid, as not having occurred within the time allowed under the lease. In all the circumstances of the case, the tenant succeeded and was able to recover the overpaid rent. However, the most interesting part of the case was what the judge said about the way in which the landlord had purported to set the new rent.

Although it was not necessary for the purposes of the case (as the tenant won on other grounds), the judge said as follows:

In the circumstances, I need not examine in detail the plaintiff's alternative argument that the defendant did not comply with Clause 6(b) because it did not by its notice "fix the annual rent ... at an amount which in the opinion of the lessor [was] the market rent of the Premises as at [the] review date." No doubt a clause committing such a power to one party to a contract requires the power to be exercised genuinely and in good faith. In the present case, the amount inserted in the lessor's notice was decided by [one of the directors of the landlord] ... I am satisfied upon a consideration of the whole of his evidence and having regard to other evidence ... that the [director of the landlord] made no

serious attempt to assess the market rent of the leased premises as at the review date, but chose a figure upon which he had determined long before as being the amount he wanted. ... However, it is unnecessary to pursue the point.

The case highlights a possible ground for attack by a tenant of a landlord's market rent determination, which might be particularly useful where the tenant had missed its opportunity to object in time to the rent set by the landlord. As occurred in this case, it could conceivably allow the rent to be challenged years after it was "set", and despite subsequent payment of the new rent by the tenant.

Author: Colin Windeyer Partner, Henry Davis York Lawyers.
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23rd Pan Pacific Congress - San Francisco 2006

The Pan Pacific Congress of Appraisers, which will be held from September 16 - 19 in San Francisco, is just around the corner.

This is a wonderful opportunity to broaden your knowledge through an exchange of information and ideas with your industry peers from all around the world. Your registration provides admission to a variety of relevant educational sessions and presentations focused on topics such as:

- Technology in real estate investment, appraisal and consulting
- Cooperation between real estate professionals and other professions
- Financial harmonisation across borders
- International valuation standards

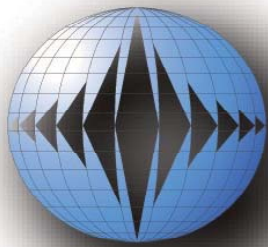
Your registration includes your choice of several unique technical tours that will offer a valuer's view of Silicon Valley, AT & T Ballpark, San Francisco's hospitality industry and the California wine country, among others.

And you won't want to miss the special opening reception at the Asian Art Museum, one of the largest museums in the Western world devoted exclusively to Asian art. This reception as well as a Friendship Banquet and traditional closing ceremonies are also included in your registration package.

For more information on the 23rd Pan Pacific Congress and to obtain a registration form please visit www.appraisalinstitute.org/conf/ppc.asp or contact Gianna Mavros at gmarvros@appraisalinstitute.org or phone 312-335-4100.

I look forward to seeing you in San Francisco!

Richard Powers, MAI, SRA
President, Appraisal Institute



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1st WAVO VALUATION CONGRESS

Congress Theme: Valuation in the Globalised Economy

27 to 29 November 2006, Meritus Mandarin, SINGAPORE

The World Association of Valuation Organisations (WAVO) will be hosting its first world congress in Singapore on 27 to 29 November 2006. This is an invaluable opportunity for valuers from various parts of the world to meet, exchange views and discuss issues of common interest. All practising valuers from both private and public sectors as well as valuation lecturers are welcome. We would like to extend an invitation to you to attend this congress as a participant, presenter or as chairperson of a session.

Highlights of this Congress

- All valuers are invited to participate in conducting an investment analysis of the integrated resort sites in Singapore. Singapore's government has recently decided to award two sites for the development of two large integrated resorts with casinos which attracted great interest from resort developers all over the world. A top prize of US\$3000 will be awarded to the Best Investment Analysis Report submitted as recommended by a panel of international assessors.
- A Best Research Paper presented at the congress will be awarded a prize of US\$1500. A research paper is one which is prepared based on a survey, literature review or an enunciation of new principles including any paper written with a strong academic rigour.
- A Best Practice Paper presented at the congress will be awarded a prize of US\$1500. A practice paper is one which is very much focused on practice issues.
- A session on valuation practices in various WAVO members' countries will be discussed.

The suggested topics are:

- **Specialist valuations** of air rights, cemeteries & crematoria, golf courses, hospitals, leaseholds, public colleges, subterranean rights, theme parks and water beds.
- International Valuation Standards, Valuation under IAS - International Accounting Standards, business valuations, plant and machinery valuations, training and education of valuers, professional ethics, professional liability and other related topics.

All submissions will be reviewed by a panel of international assessors. Authors are to submit an abstract and a brief CV by 15 August 2006. All submitted papers will be eligible for the best paper awards which will be determined by a panel of assessors. Selected papers will be published in the WAVO Journal of Valuation, an international refereed publication.

Registration fees - Delegates SGD\$700 and accompanying person SGD\$300

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