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15 November 2005

The Chairman
PO Box 204
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Melbourne Vic 8007

MACQUARIE
BANK

Dear Mr. Boymal

ED143 - Director and Executive Disclosures by Disclosing Entities

We are pleased to be able to provide our comments on the Australian Accounting Standards Board (AASB) exposure draft, ED 143 *Director and Executive Disclosures by Disclosing Entities: Removal of AASB 1046 and Addition to AASB 124*.

In submitting this response, we recognise the importance of the AASB's role and the standard setting process in Australia. We are also supportive of enhanced disclosures in financial statements where it produces relevant and reliable information for users to make informed decisions.

If we are to achieve the goal of one set of high quality global accounting standards, it is necessary that International Financial Reporting Standards (IFRS) be introduced into Australian Law with the same requirements. We are concerned that the AASB's approach of removing AASB 1046 and incorporating the requirements into AASB 124 will introduce inconsistencies with the underlying International Standard, IAS 24, because the Australian Standard will contain disclosures that are additional to those applying IFRS in foreign jurisdictions. We consider a better approach would be for the Corporations Law to solely govern the disclosure of individual remuneration, to remove paragraph Aus1.12 of AASB 124, and to relocate other disclosures in AASB 1046 to AASB 124. While this approach could lead to differences (of defined terms and individuals included) in determining aggregate vs. individual remuneration disclosures, we consider political influences will always play a role in the area of individual disclosures and therefore the AASB should avoid complicating the matter. Our suggestion will also ensure IFRS compliance. Our comments on the specific matters below are provided on the basis that the AASB perseveres with its approach in ED 143.

We consider that the AASB has proposed an inappropriate interpretation of IFRS in the case of managed schemes. In the most common scenario there is no link between the management fee paid by the scheme and the remuneration given to an individual (ie employee/director of the responsible entity). Consequently, we consider that the Objective of ED 143 (and Basis for Conclusions to the underlying international standard, IAS 24) is not met, the definition of compensation is not met, and the individuals are not KMP of the scheme. We disagree that disclosure of remuneration given to these individuals is required for compliance with AASB 124 and IAS 24.

From our research of disclosure requirements of some foreign jurisdictions (eg. USA and UK), we have learned that there are no comparable disclosures required by managed schemes of compensation given to individuals (employee/director) of the responsible entity. We have also researched disclosure practices of managed schemes in some European and Asian jurisdictions where IFRS is currently being applied, and have been unable to find any managed schemes that are making comparable disclosures of compensation. Further, we note that in the UK, the Association of Investment Trust Companies released a Statement of Recommended Practise *Financial Statements of Investment Trust Companies* on 24 June 2005 to bring it in line with IAS 24 – it does not mention any change in practice, which we understand currently is to not apply the interpretation being proposed by ED 143 (ie. no disclosure would be made in the UK). Consequently, Australian reporting in this area will be more specific as compared to other jurisdictions (including those also applying IFRS), which will put Australian entities at a competitive disadvantage. The proposed compensation disclosures related to managed schemes are not in the best interests of the Australian economy.

Specific Matters for Comment as requested:

Our comments follow on those specific matters that the AASB has requested comment:

1. Proposal to remove parent relief from AASB 124

We support removal of the current parent entity relief provided in AASB 124. We also support reliance on the definition of KMP for determining those persons affected. Both of these changes are necessary for IFRS compliance.

We are, however, concerned that without specifying a maximum number of KMP to be disclosed under individual compensation disclosures (ie proposed paragraphs AUS25.1 – AUS25.7.3), then the disclosures could become overly burdensome and add to what are already extensive disclosures. In particular, we are also concerned that since individual remuneration disclosures are not required under IFRS, these disclosures could put Australian entities at a competitive disadvantage for retaining and attracting talented individuals as compared to foreign jurisdictions where such disclosures are not required.

2. Scope of AASB 124

We support the expansion of the scope of AASB 124, because IFRS applies to all profit-oriented entities (Preface to IFRS, paragraph 9).

In addition, as the AASB is responsible for setting sector-neutral accounting standards, we see no conceptual reason for why the scope should not be further expanded to not-for-profit entities.

3. Amalgamation of AASB 1046 with AASB 124

Interpretations are a necessary part of applying accounting standards. So, when definitions or disclosure requirements are changed, there is a possibility that disclosures will develop differently from those anticipated initially.

Overall, we do not anticipate the quality or quantity of disclosures to become less as a result of amalgamating AASB 1046 with AASB 124.

Appendix 1 (paragraph A3) to ED 143 proposes disclosure of compensation allocated on appropriate basis to each MIS for which the "entity" is responsible. An individual that may be a KMP for a MIS may not also be a KMP of the responsible entity. Consistent with relying on the definition of KMP, we consider the emphasis should be based on an allocation of compensation across the entities for which the "KMP", not the "entity", is responsible.

4. Specified director, executive and specified executive

We support replacing the definitions of specified director, executive and specified executive with key management personnel. We consider that this is necessary for IFRS compliance.

As noted above under question 1, we are concerned that there is no specified maximum number of KMP to be disclosed under individual compensation, and concerned the individual remuneration disclosures could put Australian entities at a competitive disadvantage as compared to foreign jurisdictions.

As noted below under question 13, we consider that some reporting entities do not have any natural persons that are KMP but instead a responsible entity is fulfilling the role of the KMP.

5. Subtotals for compensation and loans for directors and non-director KMP

We support deleting the requirement to disclose subtotals for compensation and loans for directors and non-director KMP, as it focuses on the total cost to the reporting entity and simplifies disclosures.

6. Former KMP

We support deleting the requirement to separately disclose transactions with former KMP. However, we are concerned that some may consider this question in the context of no disclosure at all. That is, no disclosure of transactions / compensation paid after a KMP falls outside of the definition of KMP but is being transacted in respect of their previous role as KMP. We consider such items would still be caught by the disclosures required by AUS25.2.2, and therefore clarification may be needed.

7. Prescribed Benefits

We support the deletion of separate disclosure for prescribed benefits in each of the five categories of compensation.

8. Entities that have to disclose details of KMP

While we don't disagree with the proposed descriptive disclosures (eg name of person and position held), we are concerned that this area of disclosure is already subject to unnecessary and overly complicated disclosures, which gives the information less relevance.

9. Incorporation of section 300A(1)(ba) into AASB 124 paragraph Aus25.3

We support incorporating section 300A(1)(ba) of the Corporations Act into AASB 124 as it is helpful to preparers to have all the requirements located in one reference document, and ensures consistent use of terminology and definitions.

10. Should "other transactions" disclosures in paragraphs Aus25.5.3 to Aus25.7 be by individual director when the disclosures in paragraph 18 are disaggregated into "key management personnel of the entity or its parent" and "other related parties"?

We do not support this difference in disclosure. Working with the principle established by AASB 124.18 – to disclose transactions separately for each of KMP and other related parties – we consider that the disclosures required by Aus25.5.3 to Aus25.7 should be merely a further disaggregation of this information. We are concerned that the AASB's approach will cause confusion, because users tend to attempt reconciling any differences between aggregate and individual disclosures.

11. No Appendices to final revised AASB 124

We do not fully support the AASB's proposal to delete all Appendices to ED 143. We consider Appendix 1 is useful, however we consider the guidance to be incorrect and therefore should be changed to explain why disclosures are not required. We also consider Appendix 5 clarifies the AASB's intentions on a number of issues that are helpful to preparers, and therefore it should remain in the final standard. While we consider the other appendices (Appendices 2, 3 and 4) provide useful illustrations, we agree that they are unnecessary for an understanding of the proposals in ED 143, and therefore they could be removed.

12. Transitional provisions

Due to the difference in definitions between specified directors & specified executives as used in AASB 1046 and the KMP as used in ED 143, there could be practical difficulties in obtaining the information for the comparative year if the individuals included in each of the defined terms differ.

For example, there could be circumstances where an individual is a KMP under ED 143 but was not a specified executive under AASB 1046 (because the definition of specified executive relies on employment by the entity whereas the definition of KMP does not rely on employment). If the responsible entity of a MIS were replaced, then the new responsible entity would need to obtain the relevant information from the previous responsible entity. The previous responsible entity cannot be compelled to meet any requests from the current responsible entity, and by law, they may consider the provision of such information to be a breach of privacy and not provide the information.

We recommend including transitional provisions in the final standard when disclosure is impracticable, as defined in AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors*.

13. Application to managed schemes (including MIS)

We consider it necessary to understand the commercial and contractual relationships before one can appropriately interpret IFRS.

Where a MIS pays a management fee to its responsible entity (which in turn either pays its employees/directors or pays another entity that provides services to the responsible entity), in the most common scenario there is no link between the management fee paid by the MIS and the remuneration given to an individual (ie employee/director of the responsible entity).

- Management fee structures are influenced by one variable – market forces. Generally, they may consist of entry and / or exit fees based on the value of assets managed, and ongoing management fees based on the market capitalisation and / or performance of the MIS (eg annual unit price increases above a specified benchmark, or underlying assets achieving a specified rate of return). The investors of the MIS always approve the fee structures. In some cases, a management fee is not paid by the MIS (eg when the benchmark is not met, or the manager waives the fee for a variety of reasons) or the amount paid may be insufficient for the responsible entity to earn a profit for providing services to that fund (eg when the benchmark is marginally met).

- The remuneration given to an individual is solely determined in either an employment contract with the employing entity or a contract for the director position of the entity (entity being either the responsible entity or the entity that provides services to the responsible entity) – a MIS has no ability to influence the amount or basis for remunerating such an individual.

Hence, the two amounts are independently determined, the management fee charged to a MIS is not determined based on the remuneration given to an individual, and each is separately approved by different stakeholders.

Does disclosure meet the Objective of ED 143 (and the Basis for Conclusions to the underlying international standard, IAS 24)?

Before we provide our comments on the specific matters requested in ED 143, we think it is necessary to assess whether disclosure of the remuneration paid to an individual in the scenario described above meets the Objective of ED 143 (and the Basis for Conclusions to the underlying international standard, IAS 24).

The Objective of ED 143 is to *ensure that an entity's financial report contains the disclosures necessary to draw attention to the possibility that its financial position and profit or loss may have been affected* [underline added for emphasis] *by the existence of related parties and by transactions and outstanding balances with such parties*. Further, the Basis for Conclusions (paragraph BC7) to the underlying international standard, IAS 24, notes that a reason for requiring disclosure of KMP compensation is for *...users of financial statements to make a better assessment of the impact of such compensation on the entity's financial position and profit or loss*.

In the scenario described above, there is absolutely no possibility for the MIS' financial position and profit or loss to be affected by the remuneration paid to an individual, because the remuneration paid has no bearing on the costs incurred by the MIS and therefore the investor's financial return. As stated in the rubric to ED 143, all paragraphs (which include the Objective paragraph) have equal authority. Consequently, it is clear in the scenario described that any disclosure of an individual's remuneration would be contrary to the Objective of ED 143.

We have also researched disclosure practices of managed schemes in some European and Asian jurisdictions where IFRS is being applied. We have been unable to find any managed schemes that are making comparable disclosures of compensation. Further, we note that in the UK, the Association of Investment Trust Companies released a Statement of Recommended Practise *Financial Statements of Investment Trust Companies* on 24 June 2005 to bring it in line with IAS 24 – disclosure of individual remuneration is not specifically mentioned. Consequently, ED 143 proposes disclosure for Australian managed schemes that is beyond that provided by managed schemes in other jurisdictions applying IFRS.

We have previously provided the AASB a letter on 6 September 2005 commenting on the Board's discussions thus far (refer Appendix). We have not attempted to reiterate those previous comments in this submission, but continue to support them.

When a MIS pays a management fee to its responsible entity, does the MIS indirectly provide the compensation of the KMP for managing the MIS ?

The definition of compensation in AASB 124 relies on whether benefits are paid, payable or provided by the MIS, <u>or on behalf of the MIS</u>, in exchange for services rendered.

As described in the most common scenario above, there is no link between the management fee paid by the MIS and the remuneration given to an individual. The two amounts are <u>independently determined</u>, the <u>management fee charged to a MIS is not determined based on the remuneration given to an individual</u>, and <u>each is separately approved by different stakeholders</u>. Consequently, we disagree with the AASB's proposal that an MIS indirectly provides the compensation (ie the responsible entity does not pay on behalf of the MIS). We consider that in such circumstances the remuneration given to an individual does not meet the definition of compensation, and therefore should not be subject to KMP compensation disclosures. Our comments below indicate that in this circumstance we consider the management fee paid by the MIS to the responsible entity should be disclosed.

We would agree with the AASB's proposal in a scenario where the remuneration paid to an individual is linked to the management fee paid by the MIS, such as when a responsible entity charges a management fee based on remuneration paid plus a margin.

Should KMP of a MIS that is a disclosing entity be subject to the same disclosure regime as all other disclosing entities, or should they make fewer disclosures?

We consider the disclosure regime of a MIS should not be expanded to cover Aus 25.1 – Aus 25.7.3. Our reason is based on the concern outlined in question 15 below – the proposal could put Australian entities at a competitive disadvantage for retaining and attracting talented individuals as compared to foreign jurisdictions where such disclosures are not required.

In addition, if the AASB's reason for proposing a MIS that is a disclosing entity be required to make the disclosures proposed in Aus25.1 – Aus 25.7.3 is based on a premise that a MIS has little if any distinction from other listed entities, we consider the AASB has selectively chosen the entities to be included and not completely applied its own reason. Had the AASB followed its conceptual argument completely, then we fail to understand why it did not expand the proposals in Aus 25.1 – Aus 25.7.3 to apply to all reporting entities. If the AASB were to have proposed such a scope expansion, we would still not have supported the proposal on the basis that it would put Australian entities in an anti-competitive position.

Are the KMP of a MIS among the individuals paid by the responsible entity (or by another entity that provides services to the responsible entity)?

While accounting standard setters cannot possibly contemplate all scenarios at the time of deliberating proposals for a new/revised standard (and therefore we operate in a realm of principles-based standards), we consider that it is possible for some entities to not have any KMP.

In the most common scenario described above where there is no link, we consider the AASB's interpretation for determining the KMP of a MIS to be incorrect. We consider two alternative views are appropriate interpretations – either that the MIS has no KMP (in which case, no disclosures would be given) or that the responsible entity undertakes the activities of a KMP. Under our second suggestion, the management fee paid by the MIS to the responsible entity would be considered the compensation that should be disclosed. Under this suggestion, we would also recommend disclosure that the amounts paid to individuals (employee/director) of the responsible entity are not paid by, or on behalf of, the MIS – as this is consistent with the approach already taken by disclosure of audit fees that are not paid by the MIS.

Other issues

In relation to the question of application of AASB 124 to managed schemes, we wish to raise the following additional points:

- the AASB is proposing that aggregate compensation disclosures be provided by all managed schemes (eg trusts) included in the scope of ED 143 (in addition to individual compensation disclosures for all disclosing entities) in respect of its KMP, when those entities pay a services fee to another entity (eg trustee company). Overall, we agree that any entity (including a trust) that falls within the scope of ED 143 should be subject to its proposals. However, consistent with our earlier comments provided in this question 13, where the scenario is such that there is no link between the management fee paid by the trust and the remuneration given to an individual (ie employee/director of the trustee company), we disagree that disclosure of aggregate remuneration given to individuals is required for compliance with AASB 124 and IAS 24. In this circumstance, the Objective of ED 143 is not met, the definition of compensation is not met, and the individuals are not KMP of the trust.

- The AASB suggests in Appendix 1 to ED 143 that the governance requirements of a MIS are the same as a public company, and that disclosing compensation is important for identifying the cost of governance of the MIS. We consider it important for the AASB to understand that a MIS has different governance obligations, as considered in their compliance plans and compliance committees. As noted above, a MIS (or its investors) has no ability whatsoever to influence the amount or basis for remunerating an individual who is an employee or director of the responsible entity.

- Appendix 1 (paragraph A3) to ED 143 suggests that remuneration paid to individuals that manage a number of MIS' should be allocated across all the relevant funds. We consider that there could be circumstances where practically it would be difficult to determine an appropriate allocation basis. However, we consider that to comply with the definition of compensation (ie. '…in exchange for services rendered to the entity'), it is necessary to always allocate.

- we understand that there may be legal issues regarding privacy of information where an entity that provides services to a responsible entity is requested to provide information about the remuneration given to its individuals. We can also foresee potential difficulties when third parties jointly own a responsible entity, and one of the venturers refuses a request to provide such information. The AASB should consider providing guidance in these situations, for example by providing relief when gathering the information is considered impracticable, because the Australian legal framework may provide unique difficulties compared to others internationally.

14. Other disclosure requirements

We do not propose adding any other disclosure requirements.

15. Proposals in the best interest of the Australian economy

The proposed individual compensation disclosures related to managed schemes are not in the best interests of the Australian economy.

We consider Australian equivalents of IFRS should not go beyond the requirements of IFRS. We are concerned that the proposals to disclose individual compensation for entities other than those included in section 300A of the Corporations Act (ie other than listed companies) could put Australian entities at a competitive disadvantage for retaining and attracting talented individuals as compared to foreign jurisdictions where such disclosures are not required. As noted at the beginning of this submission, we are concerned that the AASB's approach will introduce inconsistencies with the underlying international standard, IAS 24, because the Australian Standard will contain disclosures that are additional to those applying IFRS in foreign jurisdictions. We consider a better approach would be for the Corporations Law to solely govern the disclosure of individual remuneration, to remove paragraph Aus1.12 of AASB 124, and to relocate other disclosures in AASB 1046 to AASB 124. Our suggestion will also ensure IFRS compliance.

From our research of disclosure requirements of some foreign jurisdictions (eg. USA and UK), we have learned that there are no comparable disclosures required by managed schemes of compensation given to individuals (employee/director) of the responsible entity. As noted above, we have also researched disclosure practices of managed schemes in some European and Asian jurisdictions where IFRS is being applied, and have been unable to find any managed schemes that are making comparable disclosures of compensation. Consequently, Australian reporting in this area will be more specific as compared to other jurisdictions (including those also applying IFRS), which will put Australian entities at a competitive disadvantage.

If you wish to discuss any of these matters further, please do not hesitate to contact Stuart Dyson (02) 8232.8670.

Yours sincerely,

Greg Ward
Chief Financial Officer

Appendix

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6 September 2005

Mr David Boymal
Chairman
Australian Accounting Standards Board
PO Box 204
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MACQUARIE BANK

Dear David

Exposure Draft to revise AASB 1046 *Director & Executive Disclosures by Disclosing Entities* - application to an MIS

We understand that the Australian Accounting Standards Board (AASB) is expected to issue an exposure draft in the near future proposing changes to the current AASB 1046 *Director & Executive Disclosures by Disclosing Entities*. As communicated in its media release of 21 June 2004, the AASB's current interpretation is that AASB 1046 applies to all those registered managed investment schemes (MIS) that are classified as disclosing entities by the *Corporations Act 2001*. This interpretation is expected to be confirmed in the exposure draft.

We disagree with the AASB's intention of proposing continued application of AASB 1046 to an MIS that is a disclosing entity. We strongly support the letter of 13 July 2004 that was previously sent to the AASB by the Investments and Financial Services Association (IFSA). In particular, we consider the disclosure for an MIS is not relevant and does not meet the AASB's purpose of providing information as to the cost of corporate governance of an MIS for the following reasons (as previously enunciated by IFSA):

- the cost to the MIS is the management fees charged by the responsible entity (RE), and these are already fully disclosed. Remuneration paid to directors or executives of the RE is a cost of the RE. Unitholders do not have the scope or authority to influence the remuneration paid by the RE. This view can also be inferred from the Regulation Impact Statement accompanying the AASB's original exposure draft, ED 106 *Director,* *Executive and Related Party Disclosures* (ED 106), which states that if no action were taken, one of the most likely negatives consequences is a misallocation of resources in the area of remuneration of directors and senior management that is likely to increase since shareholders will not be provided with sufficient relevant and reliable information to make an adequate assessment of existing and proposed remuneration when required to vote on these matters.

- Directors and executives of an RE are often employed by a parent entity in a larger financial services organisation. It is this parent entity that has the authority over the quantum and structure of the remuneration packages. External director fees for externally managed schemes are compensated directly by the RE. Unitholders have no ability to influence this compensation.

- Directors and executives remuneration is not related directly to an individual MIS. In many cases an RE has responsibility for many MIS and the same entity may also manage private mandates on behalf of wholesale investors. Remuneration does not change proportionally to the number of MIS. Further, some RE's earn a performance fee where the scheme outperforms benchmarks set. Accordingly, disclosure of total compensation (or a proportion based on some measure) is misleading, as there is no direct relationship between remuneration packages and the underlying MIS size or performance.

Further, we are concerned that including an MIS that is a disclosing entity within the scope of AASB 1046 is going beyond the government's expectation originally arising from changing the Corporations Act. As stated in the Preface and the Regulation Impact Statement to the AASB's original exposure draft, ED 106, the initiation of this AASB project was motivated by the then recent and proposed amendments to the Corporations Act, particularly: (a) the introduction of section 300A in July 1998 by the Company Law Review Act 1998; and (b) the revisions relating to regulated related party transactions proposed in the Corporate Law Economic Reform Program Bill 1998 (subsequently enacted in CLERP Act 1999).

The CLERP had, as one of its aims, the goal of removing accounting rules from the Law and locating them in Accounting Standards. As S300A only ever applied to listed companies, the expectation would have been for the AASB to simply relocate the accounting rules for these affected entities (ie only listed companies). This expected intention would have also been supported by the Regulation Impact Statement accompanying ED106, which states:

- that the AASB decided to divide the project into two phases and that the first phase was to primarily address the need to increase the quality of disclosures by *listed companies* about those responsible for their governance; and

- that the Parliamentary Joint Standing Committee on Corporations and Securities (PJSC) noted the evidence on the disparity of compliance with section 300A, and reached the conclusion that the lack of apparent compliance with section 300A was not due to an unwillingness of companies to comply with the Law but to the fact that the Law is unclear because of the drafting of section 300A.

We note that the AASB is required to give consideration to its functions and powers under Section 227 of the Australian Securities and Investments Commission Act 2001. In particular:

- the functions of the AASB include advancing and promoting the main objects of Part 12 [S.227(1)(e)], which include facilitating:
    - the development of accounting standards that require the provision of financial information that: … (iii) is relevant to assessing performance, financial position, financing and investment; and (iv) is relevant and reliable… [S.224(a)]; and
    - the Australian economy by: …(ii) enabling Australian entities to compete effectively overseas [S.224(b)]
- in carrying out its functions, the AASB must consider the interests of Australian corporations which raise or propose to raise capital in major international financial centres [S.227(2)].

As stated in the Preface and the Regulation Impact Statement to the original exposure draft, ED 106, the disclosures required by the then current Accounting Standard AASB 1017 *Related Party Disclosures* in respect of directors were significantly less than those required in the major capital markets overseas, in terms of the number of individuals and the level of detail. Consequently, ED 106 proposed to reduce this deficiency by incorporating the best features of overseas reporting adapted to accord with requirements in the *Corporations Act 2001*. In doing this, the AASB considered the requirements of the then current international standards (IAS 24 *Related Party Disclosures* and IAS 19 *Employee Benefits*) were considered as well as the disclosure requirements in major capital markets, including the USA and the UK.

We are currently undertaking to review director and executives disclosure requirements in other jurisdictions. At the moment, we are not aware of any other major jurisdiction that requires listed managed funds to disclose remuneration of the directors and executives of their RE's, as is currently required (and expected to be confirmed in the exposure draft) in Australia by MIS that are disclosing entities.

We consider that such disclosures could adversely affect the Australian industry's ability to attract and retain talented fund managers for MIS that are disclosing entities from approach by other fund managers overseas.

We consider it important for the AASB to consider these concerns prior to publishing any proposals for AASB 1046. If you wish to discuss any of these matters further, please do not hesitate to contact myself or Mary Nicholson (02.8232.7935).

Yours sincerely,

Stuart Dyson
Group Financial Controller