

Important notice for managed fund investors

May 2017

31 May 2017

This notice outlines changes which take effect from 1 July 2017, including:

- changes to the management fees that we charge you – both up and down
- changes to how we disclose our fees and costs to you
- changes to some risk levels and a fund name, and
- our proposed election of the new Attribution Managed Investment Trust regime.

These changes are a little technical, so if you have any questions please call us on 1800 021 227 or email investors@australianethical.com.au.

This Important Notice relates to the following managed investment schemes operated by Australian Ethical Investment Limited:

- Australian Ethical Advocacy Fund (ARSN 140 444 211)
- Australian Ethical Emerging Companies Fund (ARSN 606 254 157)
- Australian Ethical Fixed Interest Fund (ARSN 166 048 184)
- Australian Ethical Cash Fund (ARSN 089 919 120)*
- Australian Ethical Balanced Fund (ARSN 089 919 255)
- Australian Ethical Australian Shares Fund (ARSN 089 919 175)
- Australian Ethical Diversified Shares Fund (ARSN 089 919 166)
- Australian Ethical International Shares Fund (ARSN 124 861 338)

* The Australian Ethical Cash Fund will be known as Australian Ethical Income Fund from 1 July 2017

Review of our management fees for some wholesale managed funds

We've conducted a review of all our management costs to ensure they continue to accurately reflect the costs of managing your investments, including the indirect costs incurred by the Funds.

From 1 July 2017, we'll reduce the management fees for some of our portfolios, including the **Cash Fund (wholesale)**, **Fixed Interest Fund (wholesale)** and **International Shares Fund (wholesale)**, while the management fees for our **Australian Shares Fund (wholesale)** will increase from 0.95% to 1.10% p.a. (including GST).

If you're invested in these funds, you can find out more about these changes in the summary of fees and costs set out below.

There have been no changes to the management fees for our retail funds.

Changes to how we disclose our fees and costs to you

New fees and costs disclosure requirements mean we'll now disclose the fees and costs differently in our Product Disclosure Statements (PDS), which will be available on 1 July 2017. This includes the format for how we disclose the indirect costs (charges from specialised external asset managers), which form part of our management costs, and also estimates of what those indirect costs will be.

As you can see in the table below, the indirect costs for each fund are expected to be nil, except for the **Balanced Fund**.

In the future, these costs may vary. We'll provide an update on the indirect costs as the information from those external asset managers becomes available.

Summary of new fees and costs disclosure

The tables below show a summary of fees and costs (including any increase or decrease in fees and costs) before and after 1 July 2017:

Retail funds

Fund name	Before 1 July 2017		Fee or cost from 1 July 2017		
	Mgmt Costs % p.a.	Total* % p.a.	Mgmt Fees % p.a.	Estimated Indirect Costs % p.a.	Total Mgmt Costs* % p.a.

Advocacy Fund	2.20	2.20	2.20	0.00	2.20
Australian Shares Fund	2.50	2.50	2.50	0.00	2.50
Balanced Fund	2.50	2.50	2.42	0.08	2.50
Cash Fund	1.00	1.00	1.00	0.00	1.00
Diversified Shares Fund	2.20	2.20	2.20	0.00	2.20
Emerging Companies Fund	2.20 [#]	2.20	2.20 [#]	0.00	2.20
Fixed Interest Fund	1.50	1.50	1.50	0.00	1.50
International Shares Fund	2.20	2.20	2.20	0.00	2.20

- Additional fees and costs, such as transaction and operating costs, may apply. These costs are not new costs, but are simply being disclosed differently. Refer to the relevant Fund PDS and Additional Information Booklet for further information about fees and costs.
- A performance fee may apply. Refer to the Emerging Companies PDS for more information.

Note: The above fees and costs are inclusive of any GST.

Wholesale funds

(Shading indicates a change in management fees)

Fund name	Before 1 July 2017		Fee or cost from 1 July 2017		
	Mgmt Costs % p.a.	Total* % p.a.	Mgmt Fees % p.a.	Estimated Indirect Costs % p.a.	Total Mgmt Costs* % p.a.
Advocacy Fund (Wholesale)	0.95	0.95	0.95	0.00	0.95
Australian Shares Fund (Wholesale)	0.95	0.95	1.10	0.00	1.10
Cash Fund (Wholesale)	0.50	0.50	0.35	0.00	0.35
Diversified Shares Fund (Wholesale)	0.95	0.95	0.95	0.00	0.95
Emerging Companies Fund (Wholesale)	1.20 [#]	1.20	1.20 [#]	0.00	1.20
Fixed Interest Fund (Wholesale)	0.65	0.65	0.45	0.00	0.45
International Shares Fund (Wholesale)	1.35	1.35	0.85	0.00	0.85

- Additional fees and costs, such as transaction and operating costs, may apply. These costs are not new costs, but are simply being disclosed differently. Refer to the relevant Fund PDS and Additional Information Booklet for further information about fees and costs.
- A performance fee may apply. Refer to the Emerging Companies PDS for more information.

Note: The above fees and costs are inclusive of any GST

Changes to some risk levels and a fund name

The risk levels for the **Australian Shares Fund** and the **Emerging Companies Fund** will change from High to Very High. We've modelled these funds to incorporate updated expected risk and return assumptions, which has resulted in a slight increase in the expected negative annual returns over the projected 20-year timeframe.

We're also changing the name of the **Cash Fund** to the **Income Fund** from 1 July 2017, to better reflect its objective, which is to generate an income stream consistent with prevailing short-term interest rates. Following a review of our expected risk and return assumptions, we've changed the risk level of the fund from a Low to a Very Low likelihood of negative annual returns over the projected 20-year timeframe.

Again, take a look at the new PDSs from 1 July 2017, which will reflect these changed risk levels and new fund name.

AMIT provides greater tax certainty

Finally, on 27 April 2017 we published our intention to operate under the new Attribution Managed Investment Trust regime (AMIT). We intend to make

an election for each of the Funds to operate as an AMIT under the AMIT regime from 1 July 2017.

AMIT will give us greater certainty on the tax status of each fund and provide flexibility when we distribute taxable income to investors. There's more detail about AMIT at the end of this notice.

And that's it!

There's a lot of information here, but the bottom line is, there's nothing that you need to do apart from make sure you're aware of and understand these changes. Of course if you'd like to talk through these changes with us you can call us on **1800 021 227** or email investors@australianethical.com.au.

Notice

Australian Ethical managed fund constitutions have been amended so we can adopt the Attribution Managed Investment Trust regime

Australian Ethical Investment Limited ACN 003 188 930 (AEIL) is the responsible entity of the following registered managed investment schemes (collectively, the Funds):

1. Australian Ethical Advocacy Fund (ARSN 140 444 211)
2. Australian Ethical Emerging Companies Fund (ARSN 606 254 157)
3. Australian Ethical Fixed Interest Fund (ARSN 166 048 184)
4. Australian Ethical Cash Fund (ARSN 089 919 120)
5. Australian Ethical Balanced Fund (ARSN 089 919 255)
6. Australian Ethical Australian Shares Fund (ARSN 089 919 175)
7. Australian Ethical Diversified Shares Fund (ARSN 089 919 166)
8. Australian Ethical International Shares Fund (ARSN 124 861 338)

Background

Each Fund is eligible to be an attribution managed investment trust (AMIT) within the meaning of sections 995-1(1) and 276-10 of the Income Tax Assessment Act 1997 (Cth) and relevant accompanying legislative provisions (AMIT regime). AEIL intends to make an election for each of the Funds to operate as an AMIT under the AMIT regime from the financial year commencing 1 July 2017.

A notice informing investors of the proposed modification to each Fund's constitutions was posted on the AEIL website from 27 April 2017 until 5 May 2017 in accordance with section 601GCA(3) of the Corporations Act 2001 as modified by ASIC Corporations (Attribution Managed Investment Trusts) Instrument 2016/489.

AEIL has not received any requests to call and arrange to hold a meeting of Fund investors relating to that notice. As such, we're letting you know that under section 601GCB of the Corporations Act 2001 as modified by ASIC Corporations (Attribution Managed Investment Trusts) Instrument 2016/489, we've now modified the Constitution of each Fund so they can each operate as an AMIT under the AMIT regime (modifications). The modifications will apply from the time AEIL makes an election to adopt the AMIT regime for the relevant Fund, and will continue to have effect for as long as the Fund remains an AMIT.

Why we decided to modify for AMIT

AEIL decided to adopt the AMIT regime and make the modifications for each Fund based on the best interest of investors.

The main reason is because the AMIT regime provides greater flexibility when distributing taxable income. The key feature of the AMIT regime is the ability for the Funds to 'flow through' taxable income to investors on an 'attribution basis' (which is to be determined by AEIL on a fair and reasonable basis) and for that taxable income to retain its character for tax purposes as it flows through the Fund.

The modifications have amended the Constitution of each Fund to:

- give AEIL the power to make an irrevocable election for each Fund to operate as an AMIT; and
- insert provisions AEIL considers necessary for, or incidental to, each Fund being able to be operated as an AMIT.

There may be the following effects to investors from operating each of the Funds as an AMIT under the AMIT regime:

- certainty as to the tax status of a Fund and its entitlements to certain tax concessions, including a deemed 'fixed trust' status for tax purposes. Prior to the introduction of the AMIT regime, managed investment trusts such as the Funds relied on certain 'administrative concessions' allowed by the ATO. These concessions have been codified in the AMIT regime and that means any managed investment trusts that aren't part of the AMIT regime would have significant uncertainty for whether the administrative concessions would continue to apply;
- certainty in attributing and determining, on a fair and reasonable basis (in accordance with the AMIT regime, the Constitution and as disclosed in any current offer document for each Fund), the amount and character of taxable income of each investor in a Fund;
- ability to distribute or otherwise pass through taxable income to investors while retaining 'quantum and character' of the income for tax purposes;
- flexibility for reconciling under-estimations or over-estimations of net income for a Fund, including through adjustments to investor entitlements, to trust income in the year of discovery (i.e. carrying these amounts forward), rather than amending previously lodged investor tax returns (as is currently the case); and
- ability to reduce the potential for double taxation of investors' distributions where there are disparities between the amount distributed to investors and the taxable income of the Fund attributed to investors. This may be achieved under the AMIT regime by allowing for cost base adjustments to be made where the distribution to the investor is greater or less than the taxable income attributed to that investor.

We've made these modifications to the Constitutions to take advantage of these benefits.

AEIL has decided to maintain a consistent approach to the allocation of income and expenses and retain its current distribution methodology. A copy of the modified Constitutions are available at australianethical.com.au/shareholders/corporate-governance/ or you can call Australian Ethical Investment on 1800 021 227.

This information is general information only and is not intended to provide you with financial advice or take into account your individual investment

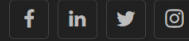
objectives, financial situation or needs. You should consider, with an accredited financial adviser, whether the information is suitable for your circumstances. To the extent permitted by law, no liability is accepted for any loss or damage as a result of any reliance on this information. You should consider the Product Disclosure Statement (PDS) for the relevant Fund before you make an investment decision. A copy of the PDS or updated information can be obtained by calling us on 1800 021 227 or visiting our website www.australianethical.com.au/managed-funds-pds.

No company in the Australian Ethical Group* guarantees the performance of any fund or the return of an investor's capital. The information contained in this document is believed to be accurate at the time of compilation.

Issued by Australian Ethical Investment Ltd (ABN 47 003 188 930, AFSL 229949)

*Australian Ethical Group means Australian Ethical Limited ACN 003 188 930 and its subsidiaries.

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You should consider seeking advice from an authorised financial adviser before making an investment decision. Past performance is not a reliable indicator of future performance.

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