

annual report

futurefund





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Letter of transmittal



27 September 2010

Senator the Hon. Penny Wong
Minister for Finance and Deregulation
Parliament House
Canberra ACT 2600

Dear Minister

As the Minister with nominated responsibility for the Future Fund, Building Australia Fund, Education Investment Fund and Health and Hospitals Fund, I have pleasure in presenting to you the Annual Report of the Future Fund Board of Guardians and the Future Fund Management Agency for the year ending 30 June 2010 for presentation to the Parliament.

The report has been prepared in accordance with section 81 of the *Future Fund Act 2006* (the Act). Subsection 81(3) of the Act requires you to cause a copy of the report to be tabled in each House of Parliament within 15 sitting days of that House after receiving the report.

Subsection 81(4) of the Act requires you, as soon as practicable after receiving the report, to give a copy to the Communications Minister, the Education Minister, the Energy Minister, the Health Minister, the Infrastructure Minister, the Research Minister and the Water Minister.

The report has also been prepared in accordance with the Requirements for Annual Reports for Departments, Executive Agencies and FMA Act bodies for 2009/10 as approved by the Joint Committee of Public Accounts and Audit under sub-section 63(2) and 70(2) of the *Public Service Act 1999*.

Yours sincerely

A handwritten signature in blue ink, appearing to read "David Murray".

David Murray AO
Chair
Future Fund Board of Guardians

About the Funds

The Future Fund Board of Guardians (the Board) supported by the Future Fund Management Agency (the Agency), has responsibility for investing the assets of the Future Fund and three Nation-building Funds – the Building Australia Fund, the Education Investment Fund and the Health and Hospitals Fund.

Our mission

We are a funds management business focused on delivering high, risk-adjusted returns over the long term on contributions to special purpose public funds. Operating independently from the Government, we will tailor the management of each Fund to its unique mandate while delivering efficiency through common infrastructure.

Future Fund

The Future Fund is a financial asset fund established by the *Future Fund Act 2006*, its purpose is to meet unfunded superannuation liabilities that will become payable during a period when an ageing population is likely to place significant pressure on Commonwealth finances.

Withdrawals from the Future Fund to pay superannuation benefits may only occur once the superannuation liability is fully offset or from 1 July 2020, whichever is the earlier. In addition, expenses associated with the investment and administration of the Future Fund may be drawn from the Future Fund throughout its existence.

The Investment Mandate for the Future Fund is to achieve an average annual return of at least the Consumer Price Index (CPI) plus 4.5% to 5.5% per annum over the long term with an acceptable but not excessive level of risk.

Nation-building Funds

The Nation-building Funds (the Building Australia Fund, the Education Investment Fund and the Health and Hospitals Fund) are financial asset funds established on 1 January 2009. The Nation-building Funds were created to provide financing resources to meet the Australian Government's commitment to Australia's future through investment in critical areas of infrastructure such as transport, communications, energy, water, education, research and health.

The Board of Guardians is responsible for growing the assets of the Nation-building Funds in line with Investment Mandates from the responsible Ministers, but has no role in determining or advising on payments from the Funds.

Payments from the Nation-building Funds are determined by Government. The *Nation-building Funds Act 2008* provides that relevant Portfolio Ministers must not make a recommendation in relation to a payment from the respective Fund for an identified project unless the advisory board for that Fund has advised that the project satisfies the relevant criteria.

The Appropriations Bills provide Parliament with a mechanism by which it may review the maximum amounts that can be paid from the Nation-building Funds each year.

Investment Mandates for the three Nation-building Funds were issued to the Board on 14 July 2009 and set a benchmark return of the Australian three month bank bill swap rate +0.3% per annum calculated on a rolling 12 month basis while minimising the probability of capital losses over a 12 month horizon.

Future Fund

Asset allocation 30 June 2010

Category & Asset Class	A\$m	Percentage of Fund (ex Telstra)
Equities		39.7
Australian equities	7,465	11.8
Developed markets equities	13,778	21.8
Developing markets equities	1,986	3.1
Private equity	1,895	3.0
Tangibles		9.5
Property	3,125	5.0
Infrastructure & Timberland	2,865	4.5
Debt		21.9
Debt securities	13,822	21.9
Alternative assets		15.6
Alternative assets	9,871	15.6
Cash		13.1
Cash	8,266	13.1
Total (ex Telstra)	63,074	100.0
Telstra holding	4,272	
Total Future Fund assets	67,346	



Data does not sum due to rounding

Asset allocation 30 June 2009

Category & Asset Class	A\$m	Percentage of Fund (ex Telstra)
Equities		27.2
Australian equities	4,494	8.3
Developed markets equities	7,273	13.4
Developing markets equities	1,728	3.2
Private equity	1,240	2.3
Tangibles		3.6
Property	757	1.4
Infrastructure & Timberland	1,178	2.2
Debt		23.1
Debt securities	12,489	23.1
Alternative assets		5.0
Alternative assets	2,694	5.0
Cash		41.1
Cash	22,262	41.1
Total (ex Telstra)	54,115	100.0
Telstra holding	6,925	
Total Future Fund assets	61,040	



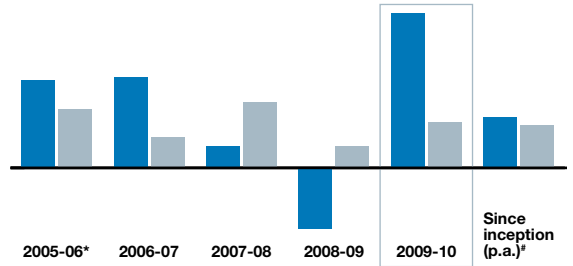
Nominal return and CPI

Year	Nominal return %	CPI %
2005-06*	6.0	4.0
2006-07	6.2	2.1
2007-08	1.5	4.5
2008-09	-4.2	1.5
2009-10	10.6	3.1
Since inception (p.a.)*	3.5	2.9

■ Nominal return ■ CPI

* Represents annualised return for the period from initial contribution on 5 May to 30 June 2006 only.

5 May 2006.



Operating result

	\$m
Total income/(loss)	6,660.4
Total expenditure	339.9
Operating result – inc Telstra	6,320.5
Operating result – ex Telstra	5,917.9

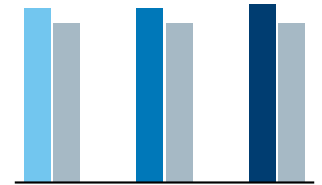
Nation-building Funds

Nation-building Fund performance 2009/10

Fund	Balance at 30 June 2010 A\$	Actual Return %	Benchmark %
Building Australia Fund	9,763	4.6	4.2
Education Investment Fund	5,516	4.6	4.2
Health and Hospitals Fund	4,736	4.7	4.2

■ Benchmark

The Nation-building Funds were invested in combinations of short and medium-term debt instruments in line with the investment mandates.



Report from the Chair

At the end of the financial year, the Future Fund held assets totalling \$67.35 billion comprising portfolio investments of \$63.07 billion and 1.35 billion shares in Telstra Corporation Limited (Telstra) valued at \$4.27 billion.

No cash or financial asset contributions were received into the Future Fund from Government during the financial year.

The operating result for the Future Fund was \$6,320.5 million comprising \$402.6 million from the holding in Telstra and \$5,917.9 million from the broader portfolio.

This produces a return for the Future Fund (ex Telstra) of 10.6%, while the Telstra holding generated a return of 6.7%.

No new contributions to the Nation-building Funds were received during the year. Withdrawals during the year from the Building Australia Fund, Education Investment Fund and Health and Hospitals Fund were \$740 million, \$1.25 billion and \$270 million respectively. Taking withdrawals and earnings into account, at year end the Building Australia Fund was valued at \$9.76 billion, the Education Investment Fund was valued at \$5.52 billion and the Health and Hospitals Fund was valued at \$4.74 billion.

The assets of the Nation-building Funds were invested in accordance with the Investment Mandates issued by the responsible Ministers on 14 July 2009 which sets a target return of the Australian bank bill swap rate plus 0.3% over rolling 12 month periods. The Board is required to minimise the probability of capital loss over a 12 month horizon.

The Building Australia Fund and Education Investment Fund achieved returns of 4.6% for the year, while the Health and Hospitals Fund returned 4.7%, beating the benchmark by 40 basis points and 50 basis points respectively.



Developments

On 20 August 2009 the Board disposed of 684.4 million Telstra shares through an underwritten sale to institutional investors. As a result the Board now holds 1.35 billion shares in Telstra or 10.9% of the company.

Following the sale the Board placed its shares under voluntary lock up for 180 days. This lock up period expired in February 2010 and the Board intends to reduce its holding in Telstra further over the medium term to a level consistent with its long-term mandate and strategy.

In May 2010 the Future Fund hosted a meeting of the International Forum of Sovereign Wealth Funds in Sydney. The meeting provided an opportunity for participants to exchange views on issues of common interest and to facilitate understanding of the Santiago Principles which establish a framework for governance, accountability and transparency for Sovereign Wealth Funds.

The principles and practices detailed by the Santiago Principles are fully implemented by the Future Fund. A review of how they are applied has been completed and is provided as an appendix to this report.

Governance

The governance arrangements for the Board and Agency and for the operation of the public asset funds have provided a sound framework since they came into effect in May 2006. These arrangements, detailed in the Governance section of this report, provide for the independence and accountability of the Board which is critical to the performance of the Funds and the achievement of the investment objectives.

Staff of the Agency are currently employed under the *Public Service Act 1999* (Public Service Act). However, the Agency's role in supporting an independent Board which invests public assets in financial markets is unique in the Australian Public Service.

While the Public Service Act arrangements are suitable for a department involved in policy advice or service delivery, they are less helpful given the Agency's market orientation and very specific purpose.

In November 2008 the then Minister for Finance and Deregulation announced his intention to remove Agency staff from coverage by the Public Service Act once an appropriate alternative employment framework is established. This will enhance the Agency's ability to align fully to the Board's mandated objective while in no way reducing accountability.

The Minister also announced plans to provide an exemption under the *Freedom of Information Act 1982* in respect of acquiring, realising or managing investments of the Board. This will provide greater certainty in protecting sensitive information the release of which could reduce investment returns or limit the range of investments the Board can access.

Alongside these developments in the statutory governance framework, the Board has initiated a review of governance practices and arrangements within the organisation, including a comparison of key governance elements to those of other leading global funds. This reflects the obligation on the Board to have regard to international best practice for institutional investment and the Board's own view that good governance protects and creates investment value.

The outcome of this review will help the Board ensure the organisation's time, resources and skills are optimally applied to the achievement of the Investment Mandate. Ultimately this will contribute to the achievement of performance goals and other key targets over the medium term.

During the year the Board brought the exercise of its voting rights in Australian companies inside the organisation, rather than delegating this power to external managers as was previously the case. The organisation now also applies greater oversight to the exercise of voting rights outside Australia by its investment managers. These initiatives are based on the view that appropriately exercising voting rights can improve governance and that improved governance results in higher returns to investors.

In relation to the Future Fund's holding in Telstra the Minister for Finance and Deregulation confirmed that the Government would not direct the Board in relation to its Telstra shareholding, including in respect of any shareholder vote on structural separation of the company, nor discuss with the Board its intentions in relation to the exercise of voting rights.

An overview of how voting rights in Australia and overseas were exercised is included in the Governance section of this report.

On 18 December 2009 John Paterson's term of appointment to the Board of Guardians expired. Mr Paterson made an outstanding contribution to the organisation bringing particular knowledge of markets and governance and expertise in the proper and effective conduct of transactions.

The Honourable Peter Costello was welcomed to the Board on the departure of Mr Paterson. Mr Costello brings a unique perspective on governance, international finance and macroeconomic conditions to the organisation.

People and Remuneration

The Board is focused on ensuring that an appropriately skilled and aligned management team is in place to provide it with support and advice and to manage the portfolio. The Agency has continued to grow in line with operational needs and the growing sophistication of the portfolio.

Following the initial phase in the Agency's development, work on talent management and development is now being undertaken with a view to sustaining performance and supporting the succession planning process across the organisation.

The Governance section of this report provides details of the approach to remuneration for the Agency including the arrangements for performance related payments.

Following a freeze on remuneration for all senior staff and the vast majority of other staff in 2009/10, remuneration was benchmarked against similar roles in the financial services sector at start of the 2010/11 year. This indicated that the remuneration for a significant number of employees was below the market median for their role and remuneration was adjusted accordingly. For the balance of the employees the average increase approved by the Board was 4.6%. This matches inflation and compares with increases of around 6% in the public sector over the two year period.

Outlook

The Investment Mandate for the Future Fund sets a target benchmark return of at least CPI +4.5 to 5.5% per annum over the long term with acceptable but not excessive risk. The Board defines the reference to 'long term' in the Investment Mandate in terms of rolling 10 year periods, using rolling five year periods to assess progress towards the target benchmark.

While the Future Fund delivered strong returns in the 2009/10 year, returns over previous years have been modest. The annualised return since the Fund received its first contribution four years ago is 3.5% per annum. The return since investments first began to be moved from cash in June 2007 is 2.5% per annum.

Returns since inception are below the long-term target, reflecting both the expectation in the mandate that returns would be lower in the initial period of investment and the market turmoil from late 2007 in which many investors made significant losses.

As set out in the Investment Report, the target asset allocation has been designed to be robust to a number of economic scenarios reflecting the structural issues weighing on markets throughout much of the world as well as the potential for growth from emerging economies.

The Board is confident that the investment strategy and the dynamic approach to building and adjusting the portfolio appropriately position the Fund to achieve its mandate.

Returns on the assets of the Nation-building Funds have exceeded the benchmark return established at the start of the year. The Board expects to continue to achieve the benchmark while minimising the probability of capital loss and ensuring that there is adequate liquidity to allow withdrawals from the Funds.

Acknowledgements

I acknowledge and thank my colleagues on the Board of Guardians whose expertise and capabilities have been enormously valuable through the year.

As has previously been the case, the Treasurer and the Minister for Finance and Deregulation have provided appropriate support to the organisation while respecting its independence. The Board would like to record its thanks to the former Minister for Finance and Deregulation, the Honourable Lindsay Tanner, for his diligence and wise counsel in dealing with important matters concerning the Fund.

The Future Fund's General Manager, Paul Costello, has informed the Board of his intention to leave the organisation by the end of the calendar year. A search is under way for a person to fill his role. On behalf of the Board I would like to thank Paul for his critical role in building the Agency in its early years. I would also like to thank the staff of the Agency for their work and commitment over the year.

David Murray AO

Chair, Future Fund Board of Guardians

Report from the General Manager

It is now four years since the Future Fund received its first contribution from Government and three years since, on the back of a newly built operating infrastructure, we began the move from holding these contributions as cash towards a more broadly based portfolio designed to achieve the investment returns set out in the Investment Mandate from Government.

At the end of the first year of this three year process (30 June 2008), the Future Fund portfolio (excluding the Telstra holding then still in lock-up) comprised \$34.6 billion in cash (62%) and \$21.1 billion in other financial assets (38%) – an asset mix which, given the dramatic events which were beginning to impact markets, resulted in a modest positive return of 1.5% for the year.

In 2008/09, we continued building out the exposure to broader markets with a focus on taking advantage of the opportunity to buy quality assets at attractive prices as existing owners were forced to restructure their portfolios. The scale of the adjustments in financial markets was so significant, however, that the portfolio could not fully escape the impact and a loss of 4.2% was reported. By 30 June 2009, the size of the cash position had reduced to \$22.3 billion (41%) and there was around \$31.9 billion invested in other assets (59%).

During the year to 30 June 2010, we continued this process and the cash reserves of the Fund had reduced to 13% by year end. Having carried less risk in our portfolio than many other investors through this three year period (thereby avoiding the worst of the impact of the Global Financial Crisis) and having built a portfolio less reliant on equity markets to generate returns than that of many other investors, it is pleasing to be able to report a return of 10.6% for the year.



In the Investment Report, we set out our approach to designing and implementing the Future Fund's investment program. We also detail the approach we are adopting for each of the sectors that make up the portfolio.

As part of a process of continuous assessment, we undertook a comprehensive review of our investment strategy during the year. While making some adjustments to our long-term direction and re-setting our medium-term target allocations, the review served to re-affirm the majority of our early judgements. A hallmark of this work was the level of collaboration across our investment team which generated fresh insights that should significantly enhance the outcomes of this project.

The 2009/10 year was also the first year of investing the three Nation-building Funds (Building Australia Fund, Education Investment Fund and the Health and Hospitals Fund) to the Government's Investment Mandates.

With responsibility for the allocation of the capital in these funds lying with the Government, our organisation's role is to meet the risk and return objectives of the Investment Mandate set by the Responsible Ministers. As these Funds are being used to finance infrastructure projects in the relevant areas of the economy over the medium term, the capital has been invested to produce a return modestly above the return on a portfolio of Australian bank bills and with a sharp focus on avoiding capital loss over the year. We are pleased to have produced a return comfortably in excess of the minimum mandated return while protecting the capital.

Staffing

Alongside the critically important work of shaping and developing the portfolio to grow the assets, we have continued to develop our organisation's capabilities and resources to ensure that the Board is advised and supported by an appropriately aligned team.

In line with our plans, staff numbers rose from 58 at the end of June 2009 to 71 at the end of June 2010. We have particularly focused on adding depth to our investment team to support the senior staff in each area who led the initial launch of the investment program. With the growing sophistication of the portfolio, we have also added to our capacity in key finance, operations and IT and legal areas to ensure we can fully support a larger program of investments. There are now a total of 90 mandates with 63 external managers.

The legislation governing the Future Fund requires the use of external investment managers. While this is likely to result in higher portfolio management costs compared to organisations which elect to manage a proportion of their assets internally, it has the important advantage of keeping the focus firmly on the optimal design of the overall

investment program rather than the challenge of building and supporting internal asset management teams.

In some sectors there is a substantial universe of high quality investment management firms from which our sector specialists can construct robust and innovative programs. In other sectors this is not the case and our internal teams work hard to structure terms which provide us with the assurance we require that our capital will be thoughtfully invested. In all cases, we strive to achieve the highest degree of alignment possible – including the use of performance based fees.

Looking ahead

Our organisation is now moving out of its start-up phase. Having deployed a significant amount of capital over the last three years our focus is increasingly on refining the combination of assets held in pursuit of our objective.

Operationally, we have commenced work to further enhance our technology systems and to consolidate our approach to reporting, compliance and risk management. These systems will provide the framework for an efficient and effective organisation for years to come.

It is also time to turn greater attention to the development of our people. The staff have applied themselves enthusiastically and professionally to the task of building out the investment program through these tumultuous years. It is now appropriate to take stock, refine the way we do things and invest in the sustainability of the organisation. This includes revisiting how we exhibit and apply the organisational values which have stood us in good stead on our journey so far.

I would like to thank the staff of the Agency for their professionalism, energy and commitment. It has been an honour to have worked closely with them and their contribution has been critical to helping preserve the real value of the assets of the Future Fund through the global financial crisis – a not insignificant achievement. I would also like to acknowledge the importance of the Board's support and guidance through this initial phase in the investment of the assets of the Future Fund and Nation-building Funds.



Paul Costello
General Manager

Our values

Integrity – applying high ethical and professional standards

We require this from our people and expect it from our partners. Our actions should be able to withstand the test of hindsight.

Excellence – achieving the highest standards in everything we do

We must strive for excellence as individuals and have high expectations of each other. Where we see these standards slipping we must take steps to get things back on track.

Innovation – always looking for ways to do things better

We expect our people to be searching for fresh ways of addressing perennial challenges and will support this by recognising that we can learn from our mistakes as well as our successes.

Teamwork – working cooperatively to achieve our common goal

We must encourage open discussion to improve our decision-making and ensure we treat each other with fairness and respect through this process.

Partnership – treating others equitably for mutual benefit

We recognise the value of enduring relationships with external providers and will work towards building highly productive, commercially rigorous partnerships.

Investment beliefs of the Future Fund Board of Guardians

Mission beliefs

The Board believes:

- (i) that the single measure embodying the goal of the Future Fund and Nation-building Funds is achieving the mandated returns over rolling 10 year and 12 month periods respectively. For the Future Fund, while the amount of risk taken cannot be captured in one figure, it is best assessed by reference to downside outcomes over rolling three year and 10 year periods;
- (ii) that peer group risk should not be used to shape strategy. The Future Fund Investment Mandate provides an unusually long-term investment horizon and this presents a competitive opportunity to add value;
- (iii) that while quantitative measurement of risk is important, so is building qualitative views of risk through understanding the environment and its potential impact on the portfolio. In addition, operational, counterparty and reputational risk need assessment and management;
- (iv) that the amount of risk taken should be conditioned by what strategy is most likely to meet the investment goals given current conditions.

Governance beliefs

The Board believes:

- (i) that high quality governance of the investment process is critical to success. The likelihood of meeting investment goals is directly related to the time, expertise and organisational effectiveness applied to decisions by the Board and management. Within this, the clear identification and separation of the Board's and management's responsibilities is particularly important;
- (ii) that it should ultimately be responsible for all investment decisions. This leads to decisions being tiered with the Board retaining control over top tier decisions, passing over responsibility below this tier to management subject to the Board's oversight;
- (iii) that its role is to act as a principal, acting in complete alignment with the Fund's mission. It has a critical role in managing agency issues, including those of management, and influence over compensation levels and incentives are critical to achieving success in this regard;
- (iv) that there is value in ensuring adequate time, diversity of view and specialist advice are applied to its deliberations.

Investment strategy beliefs

The Board believes:

- (i) that its focus should be on the effective management of beta (market related risk) because it is a stronger driver of long-term returns than alpha (skills related risk);
- (ii) that markets can be inefficient and skilful managers can add value after fees (albeit that the degree of inefficiency varies across markets and over time) and that this return is, in general, lowly correlated with market returns;
- (iii) that a flexible approach to asset allocation exposures is appropriate;
- (iv) that a higher expected return per unit risk (investment efficiency) can be obtained from a broadly diversified allocation across asset classes. In addition, the long time horizon supports a tolerance for illiquid assets;
- (v) that while the quantification of returns, risks and correlations are necessary inputs in the design and review of investment strategy, the difficulty and limitation of these assumptions means qualitative considerations are also important.

We are a funds management business focused on delivering high, risk-adjusted returns over the long term on contributions to special purpose public funds. Operating independently from Government, we will tailor the management of each fund to its unique mandate whilst delivering efficiency through common infrastructure.

*Future Fund Board of Guardians
mission statement*

Future Fund

Background

The Future Fund was established in early 2006, under statute, to make provision for the unfunded superannuation liabilities of employees of the Commonwealth that will become payable during a period when an ageing population is likely to place significant pressure on the Commonwealth's finances.

Contributions totalling \$40.4 billion in cash were made to the Fund in the period from May 2006 to June 2007 with a further \$10.9 billion being contributed by June 2008. This brought the total cash contributions to the Fund to \$51.3 billion. No further cash contributions have been made since the commencement of the 2008/09 financial year.

In addition, 2,105 million shares in Telstra (ASX:TLS) were transferred to the Fund in February 2007 and a further 57 million shares during 2007 and 2008. The total value of these shares on their respective transfer dates was \$9.209 billion. All transferred shares were subject to a restriction that they could not be traded until 20 November 2008, subject to certain limited exceptions including disposal through a Dividend Reinvestment Plan (DRP) initiated by Telstra. 126 million shares were disposed of via this mechanism during the lock-up period.

Under the *Future Fund Act 2006* withdrawals may not be made from the Fund (apart from meeting operating costs) until at least 1 July 2020 unless the value of the Fund exceeds the target asset level (TAL). This is the amount that is expected to offset the present value of projected unfunded superannuation liabilities. The office of the Australian Government Actuary, in their 2010 report, concluded that the current assets of the Future Fund are below the TAL and so, at this stage, no withdrawal before 2020 is expected.

The Future Fund Board of Guardians is required under the Act to seek to maximise the return earned on the Fund over the long term, consistent with international best practice for institutional investment and subject to its obligations under the Act and any Directions given by the responsible Ministers.

These Directions serve to articulate the Government's expectations for how the Fund will be invested and managed by the Board. Investment Mandate Directions were first issued to the Future Fund Board of Guardians by the Responsible Ministers – the Treasurer and Minister for Finance and Administration (now Minister for Finance and Deregulation) – in May 2006 and remain in place. These set out the following obligations on the Board:

- (i) An objective of achieving an investment return averaging at least the Australian Consumer Price Index (CPI) plus 4.5% to 5.5% per annum over the long term (the benchmark return). The Directions note that during the initial transition period, as the Board develops a long-term strategic asset allocation, a return lower than this benchmark return is expected;
- (ii) In targeting this benchmark return, the Board must determine an acceptable but not excessive level of risk for the Fund measured in terms such as the probability of losses in a particular year;
- (iii) A limit for holdings on any listed company in order to prevent triggering the takeover provisions of the *Corporations Act 2001*;
- (iv) A restriction on acquiring a direct equity holding of voting shares in Telstra Corporation Limited except as a result of a transfer of financial assets by the responsible Ministers;
- (v) A requirement to act in a way that minimises the potential to effect any abnormal change in the volatility or efficient operation of Australian financial markets and is unlikely to cause any diminution of the Australian Government's reputation in Australian and international financial markets; and
- (vi) A requirement to have regard to international best practice for institutional investment in determining its approach to corporate governance principles, including in relation to its voting policy.

Interpreting the mandate

The Board has interpreted the requirement to achieve a return of at least CPI +4.5% per annum over the long term as meaning over rolling 10 year periods.

While performance is reported and discussed at a high level each quarter, and in detail each year, outcomes over these short periods of time are not appropriate indicators of the likelihood of achieving the outcomes set out in the investment mandate over the long term. During the first 10 years of investing, returns over rolling five year periods should provide a better indication of the organisation's likely performance against the mandate.

As noted above, in aiming to achieve the targeted return over the long term, the Board is required to take "an acceptable but not excessive" level of risk. A number of potential indicators of risk in this context were considered. Importantly the Board explicitly rejected the concept of peer risk (the risk of underperforming other institutional investors over the short term) as being inconsistent with the mission and mandate of the Future Fund.

The Board also determined that as it was not charged with ensuring that the Fund fully offset the pension liabilities of the Commonwealth, it would not frame its investment strategy around the risk of these obligations increasing relative to the asset base.

Rather, it was determined that the key risk that needed to be managed was the risk of significant capital loss over the medium term as this would negatively impact the ability to generate satisfactory real rates over the long term.

Accordingly, the Board decided that taking "an acceptable but not excessive" level of risk in aiming to achieve the required investment return meant, on a regular basis, reviewing the structure of the portfolio to balance the expected return based on market conditions against the tail risk (the worst 5% of potential outcomes) of a very poor return over the next three years. This recognises that such an outcome could result in real capital loss over the medium term.

Based on these considerations the Board adopted an initial long-term strategic asset allocation for the Fund as detailed in the 2007/08 annual report.

During the 2009/10 year a comprehensive review of the investment strategy was undertaken. On the basis that a better balance between the return seeking and risk mitigation objectives of the investment mandate could be achieved by making some changes to the design of the portfolio, the Long Term Strategic Asset Allocation (LTSAA) and the nearer term Target Asset Allocation were modified. These changes are discussed in some detail further in this report.

Portfolio Design

A principle enshrined very early in the development of the investment program of the Future Fund was the value of maintaining a high degree of flexibility in order to capture opportunities thrown up by dislocated markets. It was recognised that many institutional programs struggle to take advantage of these because their strategic portfolios are very tightly defined.

For this reason, both the LTSAA and the shorter-term Target Asset Allocation of the Future Fund are described in six broad categories (see table below)

This provides the organisation with a governance framework which allows the broad return and risk characteristics to be monitored and controlled whilst simultaneously providing the opportunity for agile navigation of emerging opportunities within the categories.

Within these broad categories (with the exception of cash) a fine grained investment strategy is developed. This results in a number of exposures, each with their own characteristics, being created at a sub-category level. Collectively these enable an insightful analysis of the total risk and return complexion of the investment program and the extent to which there is an appropriate exposure to key factors (e.g. illiquidity, real and nominal interest rate risk, equity risk, credit risk).

Broad investment categories

Category	Definition	Sectors covered
Listed equities	Exposure to corporate enterprise gained through public markets	Australian equities, global developed market equities, global emerging market equities
Private equity	Exposure to corporate enterprise gained through private ownership	Venture capital, growth equity, buy-out, distressed debt for control
Debt	Exposure to the credit component of interest bearing securities	Primarily non-government fixed interest securities extending to mortgages, high yield credit and corporate loans
Tangible assets	Exposure to investments where the return comes primarily from the income return on a physical asset	Real estate, infrastructure, utilities, timber and agricultural assets gained through public or private markets
Alternative assets	Exposure to assets not covered in the categories above	Skill based absolute return strategies and other risk premia providing diversity of return streams
Cash	Exposure to domestic, very short duration fixed interest investment with tightly managed credit risk	Australian bank bills and deposits

Setting the Investment Strategy

The comprehensive review of the investment strategy of the Fund undertaken this year resulted in modest changes to both the LTSAA and the Target Asset Allocation as outlined below:

The LTSAA

The LTSAA is a notional portfolio which represents the level of exposure to each of the broad categories which might, on average, be held over the long term. It should be regarded as an equilibrium exposure to the investment categories rather than a weighting which is specifically targeted. The actual holding at any point in time will reflect the fact that the range of opportunities available is constantly shifting given that markets are seldom at fair value.

In addition to the allocation of capital to the six categories (with listed and private equity identified separately within a broader Equity category) totalling 100% of the Future Fund, a portfolio of synthetic overlays is used to further adjust the total portfolio risk exposures. The principal overlays in use are a foreign currency hedging program, designed to target a specific foreign currency allocation at the total portfolio level, and an interest rate program, designed to target a specific level of duration exposure.

The original LTSAA was developed in 2007/08 and the chart below shows the changes to this allocation as a result of the review during the year.

Category	Original LTSAA (2007/08)	Revised LTSAA (2009/10)
Equity	35%	40%
Listed equity	27.5%	32.5%
Private equity	7.5%	7.5%
Debt	20%	15%
Tangible Assets	30%	25%
Alternative Assets	15%	15%
Cash	0%	5%
Total capital allocation	100%	100%
plus		
Nominal interest rate overlay	7.5%	0%
Developed markets foreign currency	15%	10%
Emerging markets foreign currency	5%	10%

The key drivers of the changes to this portfolio are:

a) *a wish to reduce the level of illiquidity in the portfolio:*

The recent financial crisis brought into sharp relief the potential costs associated with a lack of liquidity in portfolios, and the dangers of assuming a stable environment. Considering the impact of the financial crisis on the original LTSAA demonstrated the extent of the distortion to the portfolio balance and significant cashflow constraints that would have occurred. While we are conscious this was an extreme event, it served to encourage us to look at the level of inherent illiquidity in the original LTSAA and decide to reduce this. The reduction in Tangible Assets from 30% to 25%, the clearer distinction between listed and private equity and the introduction of an allocation to cash (see below) reflect this decision.

b) *an explicit recognition of the option value of holding cash*

The original portfolio construction had a zero weighting to cash on the basis that, as a long-term investor seeking a return well in excess of cash and with no expected withdrawals until 2020, an explicit allocation to cash would act as an unnecessary drag on performance.

With the benefit of operating the portfolio for the past few years, recognition of the value of having the 'dry powder' to respond opportunistically to attractive investments has grown. This led to the conclusion that a small cash buffer for this purpose is warranted. In addition, holding a modest level of cash reserves is appropriate to support the potential settlement obligations within our currency hedging program, particularly given the volatility of the Australian dollar and its high correlation to economic cycles.

The reduction in expected return that comes from holding cash has been compensated for by increasing the level of risk taking elsewhere in the portfolio – mostly through an increase in the allocation to listed equities. The revised LTSAA includes a 5% allocation to cash (up from 0%) accompanied by a 5% increase in listed equities (from 27.5% to 32.5%).

c) *a wish to reduce the level of real interest rate risk in the program*

It is our view that the decline in real interest rates which has characterised the last two decades, and materially contributed to increases in the prices of many assets, is unlikely to continue. At the same time we can envisage certain scenarios which would drive a rise in real rates that could be damaging for our portfolio. We therefore chose to reduce the overall level of exposure to real rates. With the equities, debt and tangible assets programs already having considerable exposure to this risk, the additional allocation through the 7.5% interest rate overlay in the previous LTSAA was deemed no longer appropriate. This was reduced to 0%.

d) *a reduction in the level of developed markets foreign currency and an increase in emerging markets foreign currency exposure*

Given the expected continuation of the interest rate differential between Australia and most developed markets, holding developed markets foreign currency is expected to be a drag on expected returns. In contrast, given the pro-cyclicality of the Australian dollar (that is, the likelihood that it will fall in value at the same time as the value of the Fund's globally diversified portfolio of risk assets is also falling), holding some developed foreign currency exposure is expected to act as a useful mitigant by protecting the value of those assets in AUD.

With an increased range of strategies available to the Fund to protect the portfolio in this circumstance, and hence less reliance on exposure to developed markets foreign currency as a hedge, it was decided to reduce this from its previous 15% level to 10%. At the same time we have a high conviction in the long-term rise of emerging market economies. Recognising the positive return drivers this creates for currencies in these markets, it was decided to lift the level of emerging markets foreign currency in the LTSAA from 5% to 10% of the total value of the Future Fund.

While the Board does not place an inappropriate reliance on quantitative modelling tools in determining the construction of the portfolio, the revised LTSAA is expected to produce a real return of between 8% and 9% pa over the long term with a very high expectation of avoiding capital loss over any three year period. In the opinion of the Board, this type of portfolio appropriately balances the obligations to maximise returns and exceed the benchmark set out in the Investment Directions with the requirement to take appropriate but not excessive risk.

The Target Asset Allocation

While the LTSAA provides a broad framework for the portfolio which might, on average, be held over time, a combination of assets which reflects a judgement about the current economic environment, and hence the expected reward for taking on risk in different markets, is set from time to time.

This portfolio is constructed with a three year view and reflects the practical challenge of building up a high quality exposure to areas like tangible assets, private equity and absolute return strategies. By setting realistic objectives for the development of these programs in the early years of the Fund's development, we are able to manage to these whilst being thoughtful about the best use of funds which will be deployed to these opportunities in future years.

In considering the structure of the portfolio over the medium term, the following views have been taken into account:

- 1 *A view that longer-term risks to economies and markets are higher than usual with an elevated possibility of regime change and our portfolio must be sensitive to this*

Weighing on markets are a number of structural issues including the need for debt deleverage throughout much of the world, global imbalances leading to potential disruptions to capital markets, the threat of one or more sovereign debt crises, and the social and political fallout from higher unemployment in some developed market economies.

On a more positive note, the potential for the provision of a burst of much needed final demand from emerging economies, led by China, through a rebalancing of economic activity towards domestic growth is recognised. This uncertainty has led to settling on a preference for shorter-horizon investment strategies over longer-horizon ones. This should protect against the risk of lower trend growth not yet being appropriately reflected in investor expectations and pricing which, in turn, would lead to an increased chance of write downs in asset values.

Where attractive risk premia are offered for longer-horizon assets these will be considered but a more cautious approach to these opportunities than might have been taken in previous years is appropriate.

- 2 *A view that our portfolio must be reasonably robust in a range of economic scenarios*

Considerable work was done during the year on developing plausible forecasts for how the market and macro-economic environment might develop over the medium term. By seeking to understand how different assets and risk factors might fare under a range of conditions, we believe our chances of building an investment strategy which is as robust as possible to the uncertainty is improved.

Scenarios ranged from an environment of sustainable growth (the re-emergence of growth in the developed world and a reduction in the current imbalances between the developed and developing world leading to reduced public sector balance sheets and reducing worries about sovereign credit), through to an environment where the recovery in the developed world peters out and policy errors are made which compound this weakness leading to further contraction (a double dip recession).

Various portfolios were tested against these outcomes to determine the most effective trade-off between strong expected returns in benign environments and mitigating losses in environments where returns on assets are naturally weak.

- 3 *A view that a number of themes will dominate outcomes for investors over the medium term and our portfolio should thoughtfully integrate these*

All other things being equal, we are encouraged to research and invest in opportunities that are positively impacted by these themes and avoid those negatively impacted. Embedding this perspective across a widely diversified portfolio is a challenging exercise requiring a significant investment in data management to ensure we have a comprehensive understanding of underlying exposures. From a top-down perspective, however, we plan to target future allocations to position the Fund to take advantage of these themes.

Key themes for the medium-term portfolio are:

- The likelihood of the need for a significant amount of debt reduction and deleverage over coming years. This influences the nature of the listed equity program we are running (a focus on less levered companies with more robust cash flows) as well as providing opportunities in our private equity program through the provision of growth capital to entities unable to access this through traditional sources. Credit markets will be impacted by similar conditions and financing pressures in the tangible assets sectors should provide opportunities to investors with sufficient 'dry powder';

- The likelihood that there will continue to be rising wealth in emerging economies, especially China, which will provide opportunities for investors if thoughtfully targeted;
- The likelihood that, in part on the back of this rising wealth, there will be growing demand for a number of resources which will lead to scarcity issues, rising prices and an impetus to develop technological solutions to this emerging problem.

Taking these themes into account led to the development of the following Target Asset Allocation for 30 June 2011. As noted above, this one year plan is the first stage of a multi-year program to add greater diversity to the investment program. It reflects how far along the journey we expect to be by the end of the 2010/11 year.

Target Asset Allocation 30 June 2011

Category	Target Allocation at 30 June 2011
Equity	40%
Listed equity	34.5%
Private equity	5.5%
Debt	16%
Tangible Assets	14.5%
Alternative Assets	20%
Cash	9.5%
Total capital allocation	100%
plus	
Nominal interest rate overlay	0%
Developed markets foreign currency	10%
Developing markets foreign currency	10%

Relative to the LTSAA, this Target Asset Allocation reflects a belief that over the near term the level of market dislocation and diminishing competition for investment opportunities should provide hedge fund managers (which comprise a material component of the Alternatives category) with a compelling landscape in which to earn strong risk adjusted returns. The likely heightened levels of volatility in financial markets going forward attracts us to strategies with limited market exposure, and at the same time this volatility should suit the flexible and intense management style of many of these managers. The 20% target allocation (relative to an equilibrium level of around 15%) exemplifies this perspective.

In addition, the lower expected allocation to Tangible Assets and higher weighting to Cash relative to the LTSAA reflect the reality of building out this exposure from a standing start in mid 2007. Since that time the Tangible Assets category has grown to 9.4% of the portfolio and is targeted to grow to 15.5% during the 2010/11 year. A higher level of cash than equilibrium will be held pending this investment and as a funding source for opportunities that we anticipate an uncertain future may present.

The June 2011 target portfolio has a slightly lower return expectation than the LTSAA (but still above the minimum benchmark return of CPI +4.5%) with modestly lower levels of both expected volatility and three year downside risk (largely because of the higher cash component).

A more detailed discussion about the approach being used for the construction of the Target Asset Allocation is provided in the next section of this report. While a series of benchmarks which approximate the characteristics of each category of this portfolio has been developed, and the skill of the management team in implementing this program by producing a return in excess of this 'policy portfolio' of benchmarks is measured and rewarded, the focus is on achieving absolute returns in line with those set by Government in the mandate.

This is an important cultural feature of the organisation discussed elsewhere in this report. It means that any investment opportunity must be considered in the context of its contribution to the total portfolio return rather than in the context of the relevant sector. It is this approach which led to the focus on opportunities in credit markets in the first years of the investment program and the increase in the weighting to Alternatives over the next stage.

The following benchmarks are used to construct the policy portfolio with the weightings set by the Board from time to time.

During the financial year to 30 June 2010, the actual portfolio outperformed the policy portfolio (weightings to these market benchmarks set by the Board from time to time to reflect the investment strategy) by 1.5%. In 2008/09 the actual portfolio outperformed the policy portfolio by 3.1%.

Category/sector	Policy Benchmark Representative Index
Equities	
Australian equities	ASX 200 (ex A-REITS) Accumulation Index
Global developed markets equities (ex Australia)	MSCI World ex-Australia (currency hedged)
Global developing markets	MSCI Emerging Markets (currency hedged)
Private equity	Cambridge Associates Private Equity Universe
Tangible Assets	CPI +5% pa
Debt	70% Barclays Capital Global Aggregate [ex Sovereign] Index (duration and currency hedged) and 30% Merrill Lynch High Yield Master Index (duration and currency hedged)
Alternatives	UBS Bank Bill Index plus 3% pa
Cash	UBS Bank Bill Index
Foreign Currency	
Developed markets currency	MSCI ex Australia weightings
Developing markets currency	JP Morgan ELMI+ Index
Interest Rate Duration	An exposure (equally weighted between Australia and international) to 10 year zero coupon sovereign bonds

Sector Reviews

This section discusses the approach that has been adopted in building out each of the sectors that make up the portfolio.

Listed Equities

For reasons of practical convenience, in the early stages of the Fund's investment life the listed equities program was built out using passive managers. Over time this has been transformed into a program that is now predominantly invested through a range of active managers, albeit still supplemented by some cost effective passive management.

The portfolio maintains a broad diversification across sectors and geographies. During the year we retested our domestic equity exposure, and have decided to maintain around 30% of our listed equities portfolio in Australian equities in the medium term. There are a number of drivers behind this decision including our more positive view on the Australian economy versus other developed countries, the potential for Australian companies to be able to pass through Australian inflation and thus offer some protection if domestic inflation rises, and the added benefit of not having to currency hedge the holdings. Our Australian equities portfolio also gives us direct and indirect exposure to growth in emerging markets.

We favour a barbell approach to managing the non-Australian exposure of the portfolio, driven by our central case view of likely anaemic growth and volatile market

conditions in the developed world and stronger growth prospects in emerging markets.

At one end of the barbell is a relatively defensive approach to developed markets. This is reflected in a conscious bias towards high quality companies – those that are typically highly cash generative, have strong balance sheets and high and stable earnings patterns – and in moderating the level of market sensitivity in the portfolio.

At the other end of the barbell is a meaningful weight to emerging markets to access the greater potential growth in these markets.

Private Equity

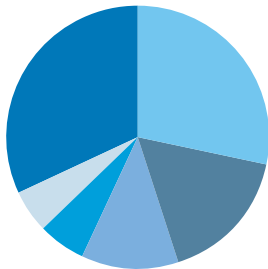
Given the difficult environment we have taken a highly selective and opportunistic approach to allocating new commitments. As a result over the year we have committed to only two new managers, with a total value of \$200m, which brings our total commitments to \$7.8 billion as at 30 June 2010.

The deal environment also proved challenging, with buyout managers continuing to struggle to raise finance for acquisitions. This resulted in only \$600 million in capital being called during the year.

This capital was reasonably evenly split across growth equity, buyout, secondaries and distressed opportunities managers with a small amount called by our venture capital managers. As of year end, approximately 45% of our invested capital was in distressed strategies, 30% in buyout related opportunities, 15% in venture and growth equity and 10% in secondaries.

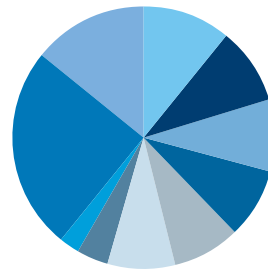
Listed Equity: Region Exposure as at 30 June 2010

	%
Australia	32
United States	28
Rest of World	17
Europe (ex United Kingdom)	12
United Kingdom	6
Japan	5



Listed Equity: Sector Exposure as at 30 June 2010

	%
Financials	25
Materials	14
Cons. Staples	11
Industrials	9
Energy	9
Health Care	9
Information Technology	8
Cons. Discretionary	8
Telecommunication	4
Utilities	3



Our distressed opportunities managers are buying companies that are in financial difficulties, seeking to then transform these companies through a financial restructuring and/or business reorganisation. With the ongoing uncertainty in the economic climate we continue to find this a very attractive space for us to be investing in.

We have also been attracted to finding pockets of idiosyncratic growth on either a sector or geographic basis and have spent much of the past year looking for, and working on, investment opportunities in that space. We believe that some young businesses will continue to grow (and need capital) regardless of the economic cycle. With limited alternative funding sources at present, an opportunity is created for private equity managers to earn attractive returns from this space. Both of the new manager appointments this year were in this area.

Our buyout and secondaries managers have been selected based (among other things) on their experience in generating strong returns in volatile economic environments. After a slow start, investments in this area picked up during the second half of the year as sellers started to return to the market and some of the buyer uncertainty diminished.

Tangible Assets

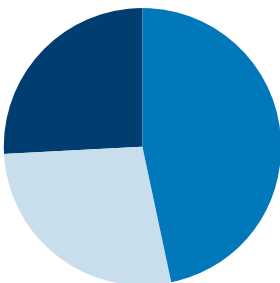
The Fund's tangible assets allocation is intended to provide long-term, consistent income streams which, for the most part, are expected over time to increase at least in line with inflation. Our exposures in this area currently come from property, infrastructure and timberlands. We are flexible in the different ways of accessing these markets and consider both the listed and unlisted markets. We are prepared to invest via pooled funds, co-investments, separate accounts and individual investments, depending on the merits of each in the particular circumstances.

Property

Over time we expect our primary property exposure to be actively managed investment grade property in the principal sectors (office, retail, industrial and residential). To date, we have been pursuing opportunities primarily in the retail sector, where we have seen good value and which has traditionally been difficult to access. We have made investments here in Australia and in the United Kingdom. We have also built a material exposure to the listed markets, both domestically and globally. This exposure has been carefully constructed to focus on higher quality trusts with strong and sustainable business models, and has been progressively increased as these markets have stabilised.

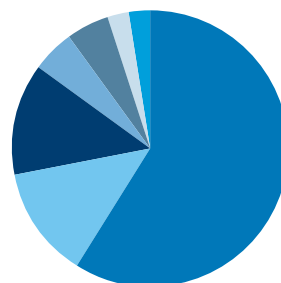
Property: Region Exposure as at 30 June 2010

	%
Asia Pacific	47
Americas	27
Europe	26



Property: Sector Exposure as at 30 June 2010

	%
Retail	59
Office	13
Diversified	13
Industrial	5
Residential	5
Hotel	2
Healthcare	2



Data does not sum due to rounding

The retraction of debt capital in the US real estate markets has also generated attractive opportunities for new capital. We have sought to opportunistically exploit this with investments in both property debt and equity. We expect similar opportunities may emerge in Europe over coming years.

Our existing portfolio has benefited from investment during the cyclical lows in the global property market and its subsequent recovery. We continue to be presented with quality property opportunities both here in Australia and globally.

Infrastructure

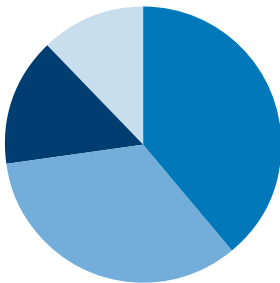
We took opportunities during the year to increase our exposure to Southern Water in the UK and to Australia Pacific Airports Corporation (the owner of Melbourne and Launceston airports). Both of these assets are of high quality and provide important services in their respective markets, reducing cashflow volatility.

As with the property sector, we have taken advantage of the good value within the listed markets relative to unlisted markets to build exposure to listed infrastructure stocks, both domestically and globally. Our approach to this opportunity is highly selective, however. It emphasises detailed, bottom-up analysis and careful stock selection to address the significant issues with many listed infrastructure stocks associated with excessive leverage and a lack of alignment with external managers.

Looking forward, market conditions remain challenging with limited transaction activity occurring in unlisted markets. Significant buy-sell spreads are common and careful assessment of growth prospects is essential,

Infrastructure: Region exposure as at 30 June 2010

	%
Australia	39
UK	34
Europe	15
North America	12



especially for assets exposed to economic growth such as tollroads, ports and airports. We have therefore adopted a steady but considered approach to building exposure in quality assets through market cycles.

Timberlands

During the year we adopted a strategy to gain exposure to the timberland asset class. Timberland assets are primarily plantations and associated land which are growing a mix of high value logs and pulpwood fibre in a sustainable manner. A timberland exposure gives the Fund access to asset returns which are linked to growing population and affluence, while the biological growth component is uncorrelated with returns from other asset classes. The investment program commenced in a modest way towards the latter part of the year.

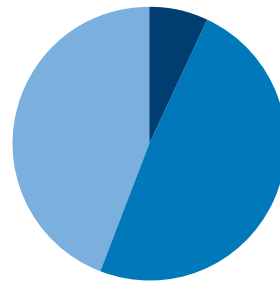
Debt

Against a backdrop of extreme credit market volatility over the life of the debt program, we have focused on opportunistically deploying capital into areas most affected by the supply-demand imbalance for credit between buyers and sellers. The debt program initially focused on very high grade domestic opportunities given the pervasive economic uncertainty in the early stages of the Fund's investment life. This included the provision of liquidity to the Australian banking sector and a significant allocation to domestic residential mortgage backed securities.

Infrastructure: Sector exposure as at 30 June 2010

	%
Economic ¹	49
Regulated ²	44
Contracted ³	7

- 1 Assets where performance is linked to economic activity
- 2 Natural monopolies providing essential services
- 3 Investments generating revenue from long-term contracts



In the year following the collapse of Lehman Brothers in September 2008 and the resulting meltdown in global credit markets, we both rapidly increased the size of the debt allocation as well as broadened the scope to encompass a number of global investment grade and high yield credit sectors. Within investment grade sectors, the focus centered on the North American corporate, mortgage and structured credit markets. We also exploited the distressed selling seen in corporate loan markets and focused on senior secured corporate loan opportunities given a view that we could be headed into a period of elevated defaults and uncertain recoveries.

The more liquid credit markets rallied significantly during fiscal 2009/10 and we experienced very strong performance across the debt portfolio. This has provided some opportunity to sell into the market strength seen in early 2010. While this has resulted in a modest reduction in the size of the overall debt portfolio, we have actively rotated the exposures within the portfolio to focus on more idiosyncratic opportunities across global markets that have attracted limited capital flows to date. This involves allocations within niche and less liquid strategies where we still see substantial excess spread available to investors.

Alternatives

The Alternatives program has evolved considerably over the past financial year, growing in size from \$2.7 billion to \$9.8 billion over this time. The hedge fund industry has had an impressive rebound from the fallout of 2008,

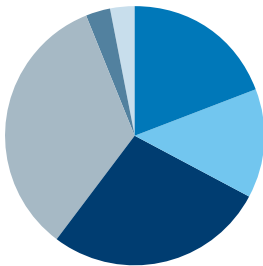
benefiting from ongoing market volatility and the strength of the equity and credit market rallies. At the same time it continues to experience diminished competition for investment opportunities, driven mainly by the reduction of leverage and bank proprietary risk taking but also due to investor withdrawals.

An important milestone in the development of the Alternatives program during the year was the appointment of a fund of hedge fund partner. This relationship has delivered us prompt, diversified and tailored exposure to a range of skill-based strategies which we feel offer attractive risk-reward profiles. This relationship has also played a role in informing our internal choices on issues such as risk and portfolio management whilst we continue to build our direct investment program.

In the early stages of the investment program our activities within the direct hedge fund portfolio were fully focused on capitalising on the attractive cyclical entry point and market environment for distressed and event driven credit strategies. While we retain a keen interest in this area, the last year has seen a shift in strategy toward increasing portfolio diversity and we have made a number of direct hedge fund manager appointments across a broader range of strategies. Recent activity has focused on multi-strategy hedge funds, which we value for their ability to allocate efficiently among disparate opportunity sets, as well as macro-directional managers given the significant diversification benefits we expect them to bring to the broader Fund. As of 30 June, the three largest sector exposures within the Alternatives portfolio were: Distressed & Event Driven at 38%; Multi-Strategy/Relative Value at 24%; and Macro Directional at 19%.

Debt Sector Mix as at 30 June 2010

	%
Investment Grade: Financial	19
Investment Grade: Non-Financial	14
Sub-Investment Grade Corporate	28
Securitised Assets	33
Emerging Markets Debt	3
Private Debt	3



Currency

Our approach to the management of currency risk in the investment program reflects our belief that we should consider offshore investments on a fully hedged basis and then separately evaluate to what extent we wish to hold an exposure to foreign currencies. This means we explicitly manage the size and nature of the foreign currency exposures rather than allowing them to be shaped by our underlying investments.

In this context, at the end of the year we held an exposure equivalent to 9.9% of the total portfolio to foreign developed market currencies. We also held a 5% exposure to emerging market currencies which not only provides further diversification for the portfolio but also offers a source of additional return from the exposure to fast-growing economies.

Telstra

Following the third stage of the privatisation program of Telstra Corporation Limited, the Government transferred 2.1 billion shares in the company to the Future Fund (16.4% of Telstra) and imposed a two year escrow on them. On 20 November 2008, these shares emerged from this escrow allowing them to be traded.

From the time of the transfer it was recognised that a holding of this size (representing 11.3% of the total value of the Future Fund at 30 June 2009) carried too great an exposure to a single security. Accordingly, the Board set the objective of undertaking a best endeavours sell-down of this holding over the medium term to a level consistent with the broader investment strategy and with a view to optimising the long-term value of the total Fund.

On 20 August 2009 we sold 684.4 million shares in a block trade at a price of \$3.47 per share (a discount of 4.9% to the prevailing market price of \$3.65). This was a 1.4% premium to VWAP since the end of the escrow in November 2008. The transaction yielded gross proceeds

to the Fund of \$2.4 billion and meant that the residual stake held by the Future Fund is 10.9% of the company. As part of that transaction, an undertaking was made to place these shares in a trading lock-up for a period of six months.

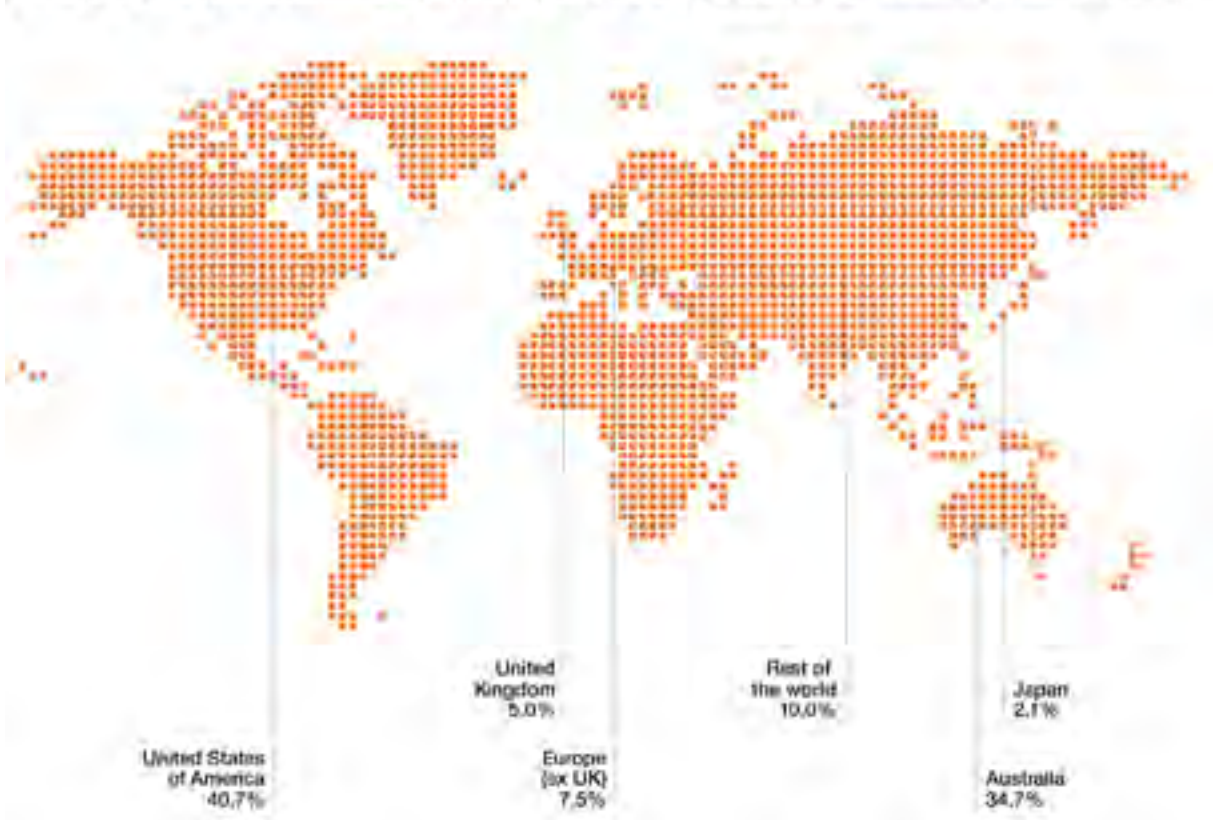
At 30 June 2010, the closing price of Telstra shares was \$3.25. Taking into account the dividends received during the year, the performance of the shares held throughout the period was 6.7%.

Performance

The return on the Future Fund portfolio (ex Telstra) over the year was 10.6% (minus 4.2% in 2008/09). Since the first contribution to the Future Fund in May 2006 the return has averaged 3.5% pa (ex Telstra). Over the same period, CPI has averaged 2.9% pa.

The investment program effectively commenced at the beginning of the 2007/08 financial year once the operating infrastructure for the Fund (back and middle office) was built. On 1 July 2007, the portfolio consisted of 91%

Future Fund investments by geography at 30 June 2010 (excluding Telstra holding)



cash and a 9% passive allocation to listed equity markets (split equally between Australia and the rest of the world) which had recently been built. Over the three year period from 1 July 2007 to 30 June 2010, the return (after all operating costs) has averaged 2.5% pa.

While modest in absolute terms, given the impact on financial markets of recent events and the loss of capital experienced by so many institutional investors over the period, it is pleasing to be able to report this outcome.

By virtue of its investment horizon and mandate, and the investment philosophy and beliefs of the organisation, the Future Fund portfolio is constructed differently from many others. It places a lower reliance on listed equity markets to generate returns (around one-third of the assets compared to around half for many funds) and seeks a greater contribution from Alternatives and Tangible Assets.

This approach meant that the impact on the portfolio of the rout on global equity markets in 2008 and early 2009 was more subdued than for many investors. The reduction in value of just over 4% last financial year was significantly less than the double digit losses experienced by many investors around the world.

While the strong bounce back in prices on equity markets in the 2009/10 year lifted the returns for many of those funds badly hit during the previous year, the Future Fund was able to achieve a similar return despite a lower reliance on recovering equity markets. The Debt and Alternatives components of the portfolio generated similar returns to Listed Equities over the year, and with similar amounts of capital allocated, made a slightly higher contribution to the total return.

Working to achieve diversity in the sources of return, thereby lowering the overall riskiness of the portfolio without compromising expected outcomes, is a core component of the investment strategy.

Operating Costs

The Future Fund portfolio (ex Telstra) management costs for 2009/10 were \$266 million. This includes investment manager fees, core custody and portfolio administration charges as well the costs of the Board and Agency. These costs, as a proportion of the assets under management, make up the Indirect Cost Ratio – a common way of expressing and comparing investment management costs in Australia.

The Indirect Cost Ratio for 2009/10 (ex Telstra) was 0.436% (0.203% in 2008/09). More detail on these costs is provided on page 44. The increased expense reflects the costs of transferring a further \$14 billion out of cash into the broader investment program over the year as well as the payment of performance fees to managers where returns were significantly above agreed hurdles.

Performance based fees, if appropriately structured, provide an important element of alignment between the external investment manager and the investor. Care is taken to create appropriate incentives with these fees.

Operating costs are expected to continue to grow as the portfolio becomes more diversified and while we are very conscious of the impact of these costs, our focus is on maximising the after-cost returns rather than simply keeping costs low.

Nation-building Funds

Background

The Nation-building Funds (Building Australia Fund, Education Investment Fund and Health and Hospitals Fund) were established by the *Nation-building Funds Act 2008* to provide financing resources to meet the Australian Government's commitment to Australia's future through investment in critical areas of infrastructure such as transport, communications, energy, water, education, research and health.

The Funds came into existence on 1 January 2009.

Between January and June 2009 the Government contributed \$10,935 million into the Building Australia Fund including \$2,468 million from the Communications Fund and \$966 million from the Telstra Sale Special Account with the balance from the 2007/08 budget surplus. Since inception a total of \$1,675 million has been withdrawn from the Building Australia Fund including \$740 million during the 2009/10 year.

On 1 January 2009, the Education Investment Fund was credited with \$6,484 million from the Higher Education Endowment Fund (HEEF) and the HEEF was discontinued. Since inception a total of \$1,355 million has been withdrawn from the Education Investment Fund including \$1,248 million during the 2009/10 year.

The Health and Hospitals Fund received contributions totalling \$5,000 million from the 2007/08 budget surplus between 20 February and 12 June 2009. Since inception a total of \$455 million has been withdrawn from the Health and Hospitals Fund including \$270 million during the 2009/10 year.

Contributions to the Nation-building Funds are made at the discretion of the Government. Arrangements for withdrawals from the Funds are detailed in the *Nation-building Funds Act 2008* and provide that relevant Portfolio Ministers must not make a payment from the respective Fund for an identified project unless the advisory Board for the Fund has advised that the project satisfies the relevant criteria.

Withdrawals may also be made to cover the administration and investment costs associated with investing the assets of each Fund.

The Appropriations Bills provide Parliament with a mechanism by which it may review the maximum amounts that can be paid from the Nation-building Funds each year.

Investment mandate and performance

The Board of Guardians is responsible for growing the assets of the Nation-building Funds in line with the Investment Mandates from the responsible Ministers, but has no role in determining or advising on payments from the Funds.

The Board is required to seek to maximise returns on each Fund consistent with international best practice for institutional investment and to take all reasonable steps to ensure there is sufficient money in the Funds to cover authorised payments.

Investment Mandates for each of the Nation-building Funds were issued by the responsible Ministers on 14 July 2009 and set a target benchmark return of the Australian three month bank bill swap rate +0.3% per annum calculated on a rolling 12 month basis (net of fees). The Board is required to invest in such a way as to minimise the probability of capital losses over a 12 month horizon.

Prior to the issue of the Investment Mandates the assets of the Funds were invested in a manner consistent with the Investment Mandate for the former HEEF which required the Board to seek to maximise returns with negligible chance of capital loss. Acknowledging the use of the former HEEF mandate, the performance of the three Funds against their benchmark is reported from 1 July 2009.

The Nation-building Fund Investment Mandates also require the Board to act in a way that minimises the potential to effect any abnormal change in the volatility or efficient operation of Australian financial markets and is unlikely to cause any diminution of the Australian Government's reputation in Australian and international financial markets.

Consistent with its obligations the Board has invested the assets of each of the Nation-building Funds in combinations of short and medium-term debt instruments that reflect the specific withdrawal and liquidity expectations of each Fund. The Board's Statement of Investment Policies in relation to the Nation-building Funds is available on the internet.

The benchmark return for each Fund in the 2009/10 year was 4.2% (Australian bank bill swap rate + 0.3%) and the return for each Fund exceeded this target. The Building Australia Fund and Education Investment Fund generated returns of 4.6% while the Health and Hospitals Fund generated a return of 4.7% for the year with the difference reflecting the differing withdrawal profiles for each Fund.

The management costs of the Nation-building Funds are met from the assets of the Fund and were \$8.3 million for the Building Australia Fund, \$5.5 million for the Education Investment Fund and \$4.6 million for the Health and Hospitals Fund. These costs include investment manager fees, core custody and portfolio administration charges as well as the costs of the Board and Agency. These costs, as a proportion of assets under management, make up the Indirect Cost Ratio.

The Indirect Cost Ratio for 2009/10 for the Building Australia Fund was 0.082%, for the Education Investment Fund it was 0.090% and for the Health and Hospitals Fund it was 0.095%. Further detail is provided on page 44.

At 30 June 2010 the value of the Building Australia Fund stood at \$9,763 million, the Education Investment Fund was valued at \$5,516 million and the Health and Hospitals Fund stood at \$4,736 million.

Investment Managers appointed by the Future Fund Board of Guardians at 30 June 2010

Asset class	Manager	
Australian equities	JF Capital Partners Perennial Growth Management	Macquarie Investment Management Vanguard Investments Australia
Global equities	Altrinsic Global Advisors Lazard Asset Management Pacific Co. Schroder Investment Management Australia Vanguard Investments Australia	IronBridge Capital Management Massachusetts Financial Services State Street Global Advisors
Developing market equities	Arrowstreet Capital Trilogy Global Advisors	State Street Global Advisors
Private equity	Adams Street Partners Apax Partners CDH Investments Hellman & Friedman Greenspring Associates Oaktree Capital Management TowerBrook Capital	Advent International Corporation Charterhouse Capital Partners HarbourVest Horsley Bridge Partners Nordic Capital Southern Cross Management
Property	Brookfield ING Clarion Real Estate Securities MGPA	Henderson Global Investors Lend Lease Quadrant Real Estate Advisors
Infrastructure	AMP Capital Investors The Campbell Group UBS Global Asset Management	Citi Infrastructure Partners RARE
Debt securities	Ares Management M&G Investment Management Limited Oak Hill Advisors Sankaty Advisors	Goldman Sachs Asset Management Macquarie Investment Management PIMCO Australia Vianova Asset Management
Alternatives	BlackRock Alternative Advisors Bridgewater Associates Centerbridge Partners L.P Makena Capital Management Och-Ziff Management	Brevan Howard Asset Management Canyon Capital Advisors King Street Capital Oaktree Capital Management Sankaty Advisors
Overlay strategies	Ashmore Investment Management Limited Insight PIMCO Australia	BlackRock Investment Managers Macquarie Investment Management
Cash	Colonial First State Global Asset Management	Macquarie Investment Management

Governance

The Board of Guardians defines corporate governance as relating to how an entity is structured, operated and controlled to optimally achieve its objective and it believes that a positive relationship exists between good governance and the creation of investment value. The Board's view of corporate governance applies both to its own operations and to how it manages the ownership rights and responsibilities that accrue to the Board's investments on behalf of the Commonwealth.

The purpose and funding and withdrawal arrangements for the Future Fund and Nation-building Funds are established in legislation together with the clear delineation of the relationships and responsibilities of the Commonwealth, as asset owner, and the Board of Guardians and Agency, as asset manager. These arrangements together represent the statutory governance framework for the Funds.

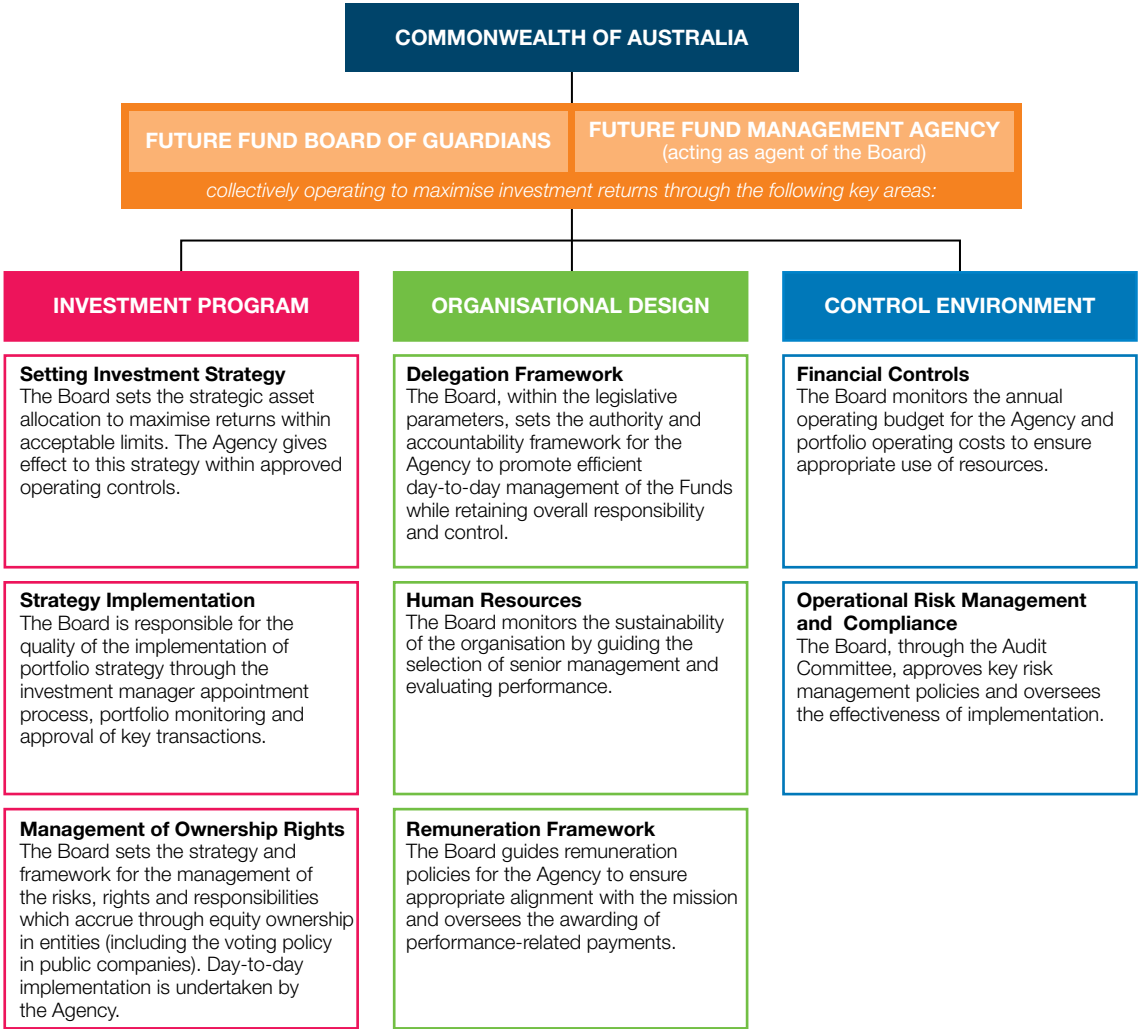
These statutory arrangements are supplemented by operational governance arrangements that reflect the obligation placed on the Board, through the legislation and the Investment Mandates, to seek to maximise returns on the Funds consistent with international best practice for institutional investment and to have regard to international best practice in its approach to corporate governance, including in relation to voting policy. The following pages detail the statutory and operational governance arrangements in some detail.

The board believes that a positive relationship exists between good governance and the creation of investment value.

Corporate governance framework

STATUTORY GOVERNANCE FRAMEWORK

OPERATIONAL GOVERNANCE FRAMEWORK



Statutory Framework

The statutory governance arrangements for the Future Fund and Nation-building Funds are set out primarily in the *Future Fund Act 2006* and the *Nation-building Funds Act 2008*.

This core legislation sets out the roles and responsibilities of the Government and of the Board and the Agency, while the *Financial Management and Accountability Act 1997*, together with other Commonwealth guidelines, procedures and orders, establishes arrangements for delegations and authorities, spending and the budget accounting treatment of costs, liabilities, income and expenses.

In particular the legislation provides the Government, through the responsible Ministers, with oversight of the Funds subject to the arrangements that establish the independence of the Board. The Government's role includes the appointment of Board members and the establishment of Investment Mandates for each of the Funds.

The legal framework retains beneficial ownership of the assets of each Fund in the Commonwealth. It also clearly states the purpose of each Fund and makes clear that contributions to the Funds are discretionary.

Withdrawals from the Future Fund may only occur once the superannuation liability is fully offset or from 1 July 2020, whichever is earlier, although investment and administration expenses may be drawn from the Future Fund throughout its existence. Withdrawals from the Nation-building Funds are determined by Government, subject to the advice of the relevant advisory board and oversight of the maximum spending from the Funds by Parliament through the Appropriation Bills.

The Board of Guardians, meanwhile, is responsible for investing the assets of the funds in accordance with the legislation. To assist it in this role, the Board receives recommendations and advice from the Agency which is also responsible for implementing investment decisions.

In undertaking this task, the Board operates independently from Government. This independence is emphasised in a number of ways, including:

- the expenses of the Funds are met from the assets of the Funds themselves rather than from appropriations through Parliament;
- the Board must be consulted on draft investment directions which must be consistent with the requirements of the legislation, and any submissions the Board makes on a draft direction must be tabled in Parliament. The investment mandates for each of the Funds clearly define the risk and return requirements and timeframe for investment activity and the legislation imposes very few limitations on asset allocation, selection of markets and portfolio design on the Board;
- Board members must be drawn from outside government and must meet the requirements of having substantial expertise and professional credibility in investing or managing financial assets or in corporate governance.

In addition, the Board is not involved in advising on macroeconomic management or policy formation and implementation and so is focused solely on the pursuit of its investment objectives in a commercial manner.

At the same time the legislation provides accountability arrangements, including the tabling in Parliament of an annual report and audited financial statements. The Board has also decided to publish public quarterly portfolio updates to provide details of the investment activity and performance of the funds.

Consistent with the recommendations of the Review of Corporate Governance of Statutory Authorities and Office Holders by Mr John Uhrig (the Uhrig Report), Statements of Expectations and Statements of Intent have been exchanged between the Minister for Finance and Deregulation and the Board and the Agency. These documents further delineate the responsibilities and communication arrangements between the parties and are available on the Future Fund's website.

The Agency appeared before hearings of the Senate Committee on Finance and Public Administration in October 2009 and February and May 2010. These public hearings are based upon the Outcome and Output structure detailed in the Portfolio Budget Statements.

The outcome for the Agency is managing and growing public funded investments to meet future financial needs and contribute to the prosperity of future generations of Australians.

This breaks down into two programs: management of the investment of the Future Fund and management of the investment of the Building Australia Fund, Education Investment Fund and Health and Hospitals Fund.

The Agency resource statement and resourcing for outcome table are included on page 131.

During the financial year the Agency received three requests under the *Freedom of Information Act 1982*. Details of the arrangements for seeking access to information are provided on page 130. In November 2009, the Minister for Finance and Deregulation announced the Government's intention to grant an exclusion under Schedule 2 of the *Freedom of Information Act 1982* for documents in respect of acquiring, realising or managing investments made by the Board. Legislation to implement this exclusion is currently being developed.

Board of Guardians

There are seven members of the Board of Guardians each appointed by the Treasurer and the Minister for Finance and Deregulation for terms of up to five years. The Board is accountable to the government for the safekeeping and performance of the assets of the Funds.

During the year, Mr Paterson's tenure as a member of the Board of Guardians expired and the responsible Ministers appointed the Honourable Peter Costello to the Board of Guardians.

To assist it in its task the Board has established an Audit Committee to oversee the compliance and audit functions, monitor control frameworks, review key financial statements, track legislative compliance and evaluate the efficiency and effectiveness of the risk management plan. All members of the Board are members of the Audit Committee with the exception of Mr Murray who is excluded as is customary due to his role as Chair and statutory Chief Executive of the Agency.

The Board has also established a Market Transaction Committee to monitor, advise and direct the Agency on behalf of the Board in relation to selected transactions. The Market Transaction Committee is chaired by Mr Watson. Other members of the committee are Ms Doyle, Dr Mulcahy and Mr Browne, who joined the Committee on the expiry of Mr Paterson's membership of the Board of Guardians.

Mr David Murray AO, Chair

Mr Murray was appointed on 3 April 2006 for a period of five years.

Mr Murray spent 39 years at the Commonwealth Bank of Australia (CBA), and was Chief Executive Officer from 1992 until his retirement in 2005. Mr Murray has substantial experience in the finance and banking sector and considerable knowledge of financial markets.

Mr Murray has strong corporate governance credentials, having guided CBA through a number of major changes, including its privatisation. In 2003, Mr Murray was awarded the Centenary Medal for his contributions to banking and corporate governance. He was appointed an Officer of the Order of Australia in 2007 for services to the finance sector, education and the community and is the inaugural Chair of the International Forum of Sovereign Wealth Funds.

Board of Guardians

(back row left to right) Brian Watson, Peter Costello, Trevor Rowe, Jeffrey Browne, Susan Doyle, (seated left to right) John Mulcahy, David Murray. (absent John Paterson)



Mr Jeffrey Browne

Mr Browne was appointed on 3 April 2006 for a period of five years.

Mr Browne was a Partner (New York) and Managing Partner of Australian Offices (Melbourne and Sydney) in the legal firm Sullivan & Cromwell and has extensive experience in capital market transactions. Mr Browne has also acted for the Commonwealth and state governments, mainly in relation to international bond offerings and privatisations.



Hon Peter Costello

Mr Costello was appointed on 18 December 2009 and his appointment expires on 2 April 2014.

Mr Costello served as a member of the House of Representatives from 1990 to 2009 and was Treasurer of the Commonwealth of Australia from March 1996 to December 2007. He served as Chair of the APEC Finance Ministers in 2007 and Chair of the G20 in 2006. He was a committee member of the International Monetary Fund, a Governor of the World Bank and the Asian Development Bank for approximately 10 years. He currently serves on an Independent Advisory Board to the World Bank and is a Managing Director and Board member of BKK Partners. Prior to entering Parliament, Mr Costello was a practising barrister.

Ms Susan Doyle

Ms Doyle was first appointed on 3 April 2006 and was reappointed for a period of four years from 3 April 2009. Ms Doyle took on the role of Chair of the Audit Committee upon the expiry of Mr Paterson's tenure.

Ms Doyle was Chair of the Australian Reward Investment Alliance (ARIA) until July 2009. Ms Doyle has had an extensive executive career in the funds management industry, particularly in the equities and fixed interest sectors, working with Commonwealth Funds Management, Suncorp Metway and Insurance Australia Group.

Dr John Mulcahy

Dr Mulcahy was appointed on 3 April 2006 for a period of five years.

Dr Mulcahy was Chief Executive Officer and Managing Director of Suncorp until March 2009. Dr Mulcahy has broad corporate experience and expertise in retail financial services having held a number of senior roles in the Commonwealth Bank including Group Executive, Investment and Insurance Services and previously the positions of Chief Executive of Lend Lease Property Investment Services and Chief Executive of Civil and Civic.

Mr John Paterson

Mr Paterson was appointed on 18 December 2006 and his term of appointment expired on 18 December 2009. During his tenure, Mr Paterson served as Chair of the Audit Committee.

Mr Paterson spent 31 years with JBWere & Son. He has extensive experience of financial markets having held roles as Director of Research, Investment Strategist, Managing Director of Were Stockbroking and Managing Director of Corporate Finance. He is a Director of Australian Foundation Investment Company, Deputy Chairman of Djerriwarrh Investments and is on the External Advisory Board of the Salvation Army (Southern Region).

Mr Trevor C Rowe AM

Mr Rowe was appointed on 3 April 2006 for a period of five years.

Mr Rowe is Chairman of Rothschild Australia Limited, Chairman of UGL Limited and Chairman of BrisConnections. He was a Director of Australian Securities and Exchange Limited (ASX) from 2003 to 2010. He served as Chancellor of Bond University from 2002 to 2009, Chairman of QIC from 2001 to 2009 and was a member of the Takeovers Panel from 2000 to 2003. He has been a member of the Foreign Affairs Council since 2000. Mr Rowe was awarded the Centenary Medal in 2003 for distinguished service to the finance industry and was appointed a Member of the Order of Australia in 2004 for service to the investment banking sector and contribution to public policy, higher education and the community.

Mr Brian Watson

Mr Watson was first appointed on 3 April 2006 and was reappointed for a period of three years from 3 April 2009.

Mr Watson has extensive experience in finance and investment management. Mr Watson spent 16 years with JP Morgan & Co in a number of senior roles, including Global Head of Equity Capital Markets and Global Head of Private Equity, both based in New York, and Chairman of JP Morgan Australia.

Mr Watson has held various positions on Australian Government Boards including Chairman of the Pooled Development Funds Registration Board and Deputy Chairman of Innovation Australia. He was Chairman of the Government's Venture Capital Review conducted in 2005.

Board and Board Committee Attendance

	Board meetings		Audit Committee		Market Transaction Committee	
	Eligible to attend	Attended	Eligible to attend	Attended	Eligible to attend	Attended
David Murray AO	13	13	–	4*	–	–
Jeffrey Browne	14	14	4	4	2	2
Hon Peter Costello	5	4	2	2	–	–
Susan Doyle	14	14	4	4	7	7
Dr John Mulcahy	14	14	4	4	7	7
John Paterson	8	8	2	2	5	5
Trevor Rowe AM	14	14	4	4	–	–
Brian Watson	14	14	4	4	7	7

*Mr Murray attended at the invitation of the Committee.

Future Fund Management Agency

The Board is supported and advised by the Future Fund Management Agency in the development and implementation of investment strategies. The Chair of the Board of Guardians is also the Chief Executive of the Agency, although in practice operational management has been delegated to the General Manager of the Agency in accordance with the arrangements of the *Financial Management and Accountability Act 1997*.

Operational leadership for the Agency is provided by the General Manager, Chief Investment Officer, Head of Operations and Head of Finance.

Mr Paul Costello, General Manager

Mr Costello took up his role as General Manager in November 2006. Previously he was the inaugural Chief Executive Officer of the New Zealand Superannuation Fund. Prior to that he was the Chief Executive Officer of the Superannuation Trust of Australia.

Mr David Neal, Chief Investment Officer

Mr Neal joined the Future Fund from Watson Wyatt Australia where he was Head of Investment Consulting. David started his career with Watson Wyatt in the United Kingdom and led the establishment of the firm's investment consulting business in Australia.

Mr Gordon McKellar, Head of Operations and IT

Mr McKellar has over 20 years experience in asset servicing including roles in Edinburgh, New York and Sydney. Most recently he was Head of Operations at BNP Paribas Securities Services. He has also held operational and client management roles with Deutsche Bank and Bankers Trust Company.

Mr Paul Mann, Head of Finance

Mr Mann is a CFA Charterholder and a Chartered Accountant with an extensive audit background in financial services gained at PricewaterhouseCoopers in Australia and the United Kingdom. He also has five years experience in the provision of fund accounting and tax reporting services to investment clients gained at National Custodian Services in Melbourne.

Operational governance

While the overarching governance arrangements are defined by legislation, the Board believes that effective governance of its own operations is essential to the successful pursuit of its objectives. In particular, the Board is focused on the prudent management of risk and considers risk in three broad categories: Investment risk, Strategic risk and Operational risk.

Investment risk includes the risk that the Board-approved investment strategy fails to achieve the mandated objectives. This comprises not only the development of an appropriate strategy but also the design and

execution of robust processes to select and monitor managers and investment opportunities through which to implement the strategy.

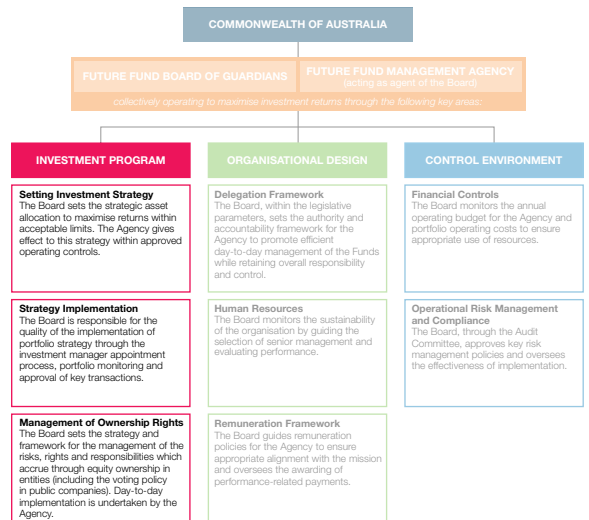
Strategic risk is the risk that the business and governance models and organisational culture are not fit to deliver the Board-approved investment strategy. The selection of people with the appropriate skills and the ability to successfully motivate and retain these people is a focus of the Agency and the Board.

Operational risk is the risk that processes, controls and systems are poorly designed, not fit for purpose or are not operating as intended to protect the organisation against financial, legal or reputational harm.

These categories of risk shape the governance structure adopted by the Board and are incorporated into the way the organisation structures and controls its activity.

As set out in the diagram on page 31 the Board structures its approach to governance through three pillars: the investment program, organisational design and the control environment. Each of these is addressed in turn.

Investment Program



Setting the investment strategy

The Board's approach to investment strategy is discussed in detail in the Investment Report starting on page 12.

Implementing the investment strategy

The Board oversees the quality of the implementation of the investment strategy by the Agency.

The governing legislation requires the use of external investment managers and this is consistent with the Board's preference to operate a modestly sized organisation with internal resources concentrated on the key issue of determining the most efficient allocation of risk across investment markets. This is complemented by a focus on selecting the most appropriate investment partners and closely monitoring their provision of services as well as tightly managing operational risks.

In implementing its investment strategy the Board invests through various jurisdictions and investment vehicles for a variety of commercial, legal and tax reasons. Properly structuring its investments can be essential to maintaining the Board's rights and entitlements including the benefit of sovereign immunity for tax purposes in certain jurisdictions. Failure to manage these matters can have a material impact on performance and would be inconsistent with the mandated objective to maximise returns whilst not causing any diminution of the Australian Government's reputation in financial markets.

The Board will only invest through arrangements and structures that are commonplace and well tested by other public investment institutions and funds in terms of compliance with applicable laws and regulations. The Board does not invest in schemes that contravene the OECD's key principles of transparency and information exchange for tax purposes. It only invests through jurisdictions that are regarded by the OECD as having substantially implemented the internationally agreed tax transparency standard. Central to this focus is operational, legal, financial and taxation due diligence which is undertaken both as part of the investment decision process and through the ongoing monitoring of mandate compliance and investment performance.

The manager selection process is detailed in the Board's Statement of Investment Policies and includes an assessment of specific criteria relating to demonstrated competitive advantage, the fit between the manager's style and process and the Fund's objectives, the strategies employed by the manager to control operational and financial risk, and the expected fees.

Exercise of Australian Voting Rights

Resolution type	No. of resolutions	WITH company board	ABSTAIN	AGAINST company board
Approve remuneration plan grant	146	70%	–	30%
Approve remuneration report	183	75%	–	25%
Amend/approve remuneration plan	35	80%	–	20%
Elect director	469	93%	–	7%
Other resolutions	304	93%	2%	5%
Total	1,137	87%	1%	13%
	(227 ballots)			
Not voted	29			
Total eligible	1,166			
	(235 ballots)			

In allocating capital to a manager, relevant issues include the proportion of the Fund allocated to the asset class for which the manager is appointed, the proportion of active risk to be allocated to the manager and the capacity of the manager to take on additional assets.

To assist in this aspect of the program, the Board and Agency draw on external advisers. These include specialists in areas such as front and back office investment manager research, market insights to assist in commercial due diligence of investment opportunities and the management of legal and tax risks.

The Board has also established monitoring practices to ensure that the portfolio is managed within predetermined limits set by the Board. These limits relate to the actual and target allocations to sectors and the exposure to individual managers as well as manager and portfolio performance. A monthly mandate compliance report is also provided to the Board.

Management of ownership rights

The exercise of the ownership rights is an important opportunity to encourage good corporate governance in investee companies. This reflects the view that good corporate governance, (i.e. how an organisation is structured, operated and controlled and how they manage environmental, social and regulatory responsibilities) protects and creates investment value.

A significant project during the year was the implementation of the organisation's voting policy. In previous years the exercise of all votes had been delegated to investment managers whose approach to voting had first been assessed as consistent with the Future Fund's corporate governance principles.

Since September 2009 voting rights in Australian companies have been managed directly by the Fund, rather than delegated, with a view to delivering more focused and consistent consideration of resolutions.

Responsibility for the exercise of voting rights in the global public equity portfolio continues to be delegated to the Future Fund's external asset managers, subject to close oversight by the organisation and regular reviews of the managers' ownership policies and practices. In all cases the right to override managers and determine voting decisions directly is retained.

In view of the size of its shareholding in Telstra, the Board manages the ownership rights attached to this holding directly.

The way in which the Board exercised the voting rights attached to its holdings in publicly listed Australian companies (including Telstra) in financial year 2009/10 is summarised on page 38.

The voting rights exercised by our asset managers in the global public equity holdings are monitored at both the whole portfolio and manager-by-manager levels.

In 2009/10 the Future Fund's managers were eligible to exercise proxy votes in respect of 42,544 resolutions at 4,097 shareholder meetings overseas. Those votes were exercised in 98% of cases at the resolution level and 98% of cases at the ballot (meeting) level. In the cases where the Future Fund's votes were not exercised generally the manager judged that it was not in the Fund's best interests to vote given structural impediments to shareholder voting, such as share blocking and onerous power-of-attorney requirements.

Each asset manager has the discretion to vote with or against the recommendation of the board of directors of the company for each resolution on the ballot. In aggregate the Fund's managers voted against company boards' recommendations in approximately 6% of resolutions voted.

In relation to private markets investments, ownership rights generally accrue in two forms:

- formal voting rights — shareholdings in companies and unitholdings in pooled vehicles; and
- rights to participate on the advisory boards of pooled vehicles.

Where shareholder voting rights accrued to pooled vehicles from the underlying investments, the managers of those vehicles analysed and exercised the voting rights on behalf of the Fund. Shareholder votes resulting from direct holdings in assets and unitholder votes from the Future Fund's interests in pooled vehicles were managed directly by the organisation's Private Markets team.

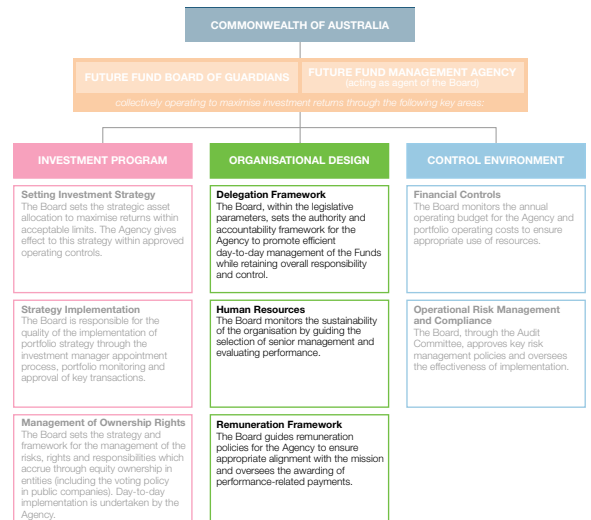
Many of the private markets pooled vehicles in which the Future Fund invests have advisory boards. The Fund has an appointment right in many of those cases and this right was exercised in all cases in 2009/10.

Looking ahead

The organisation's approach to the exercise of ownership rights will be further developed in the coming year. This will include more extensive engagement directly with investee entities to understand and clarify resolutions being put to shareholders and improve communication regarding material governance issues.

Work will also continue on the identification and integration of material environmental, social and governance risks and opportunities into the design and implementation of the portfolio.

Organisational Design



Delegation framework

While the Board is responsible for investing the assets of the Funds, the Agency provides support and advice and undertakes implementation of investment decisions including the appointment of external investment managers under delegation from the Board. The arrangements delineating the roles of the Board and Agency are outlined in the legislation and detailed in a Board-Agency authorisation protocol. This serves to provide clear lines of decision-making and accountability to promote efficient day-to-day management of the funds while retaining ultimate responsibility and control with the Board.

Human resource management

The Board supports the sustainability of the organisation and the development of an appropriately skilled and professional management team in the Agency through a focus on performance management and succession planning.

While there has been rapid growth in staff numbers over the first few years of the operation of the Agency, this has begun to slow. As part of an ambition to keep the focus of the investment team on the efficiency of the total portfolio the Board supports keeping the Agency as small as practicable. Staff numbers grew from 58 at the end of June 2009 to 71 at 30 June 2010.

There is a roughly even split between staff on the investment team and those in support functions (the operations, IT, finance, compliance, legal and corporate services teams). Full details of our current staffing arrangements are provided in the table below.

A commitment to professional development means that all staff have been allocated a training and development budget which can be accessed in accordance with the organisation's professional development guidelines.

The organisation is also committed to providing a safe working environment for its staff, contractors and others and the Human Resources Manager is responsible for managing Occupational Health & Safety (OH&S) at Agency premises. All staff are required to familiarise themselves with the OH&S policy which is available on the intranet. There were no accidents, dangerous occurrences or investigations reportable under section 74 of the *Occupational Health and Safety Act 1991*. The organisation intends to establish a Health & Safety Committee to further enhance its OH&S framework.

Consistent with the Commonwealth Disability Strategy the Agency reports on its activities as an employer through the Australian Public Service Commission's State of the Service survey. The Agency has established arrangements to ensure that documents are available to the public and to potential service providers in a variety of formats including Braille, larger print and audio, upon request.

Remuneration arrangements

The Board shapes the remuneration policies for the Agency to provide for the sustainability of the organisation through competitive remuneration and to ensure staff have appropriate alignment with the mission of the organisation. The Board also oversees the payment of performance related remuneration to Agency employees.

Remuneration is market competitive and designed to attract and retain appropriately skilled people. The level of remuneration is not tied to APS classification bands and levels for employees are externally benchmarked under a program coordinated by the General Manager and reviewed by the Board. Employees are able to salary sacrifice part of their total remuneration for a range of benefits.

At the commencement of the 2009/10 year salaries for senior executives, and the significant majority of other employees, were frozen at existing levels reflecting market conditions at the time. Adjustments to the remuneration arrangements for some junior and mid-level employees were made increasing the total remuneration expense for the Agency by around 1%.

Staffing details

FFMA Classification	Full time		Part time		Male		Female	
	08-09	09-10	08-09	09-10	08-09	09-10	08-09	09-10
FFMA 1	–	–	–	–	–	–	–	–
FFMA 2	1	2	1	1	–	–	2	3
FFMA 3	14	19	–	–	2	6	12	13
FFMA 4	35	41	2	4	23	30	14	15
FFMA 5	4	3	–	–	4	3	–	–
FFMA 6	1	1	–	–	1	1	–	–
Total	55	66	3	5	30	40	28	31

All staff are based in Melbourne aside from one full time FFMA Band 3 based in Sydney.
25 staff are employed under Australian Workplace Agreements, 46 staff are employed under Common Law Agreements.

A full review of remuneration arrangements has been undertaken at the commencement of the 2010/11 year in recognition of the very limited movement for most staff since commencing employment and the reinvigorated employment market in financial services. A benchmarking exercise using data from the Financial Institutions Remuneration Group (FIRG) has been undertaken to inform this review. Where this indicated that salaries were currently around market levels, they were adjusted to reflect inflation over the two year period since the last adjustment. Where the benchmarking exercise indicated a material shortfall in the competitiveness of an employee's salary, a larger adjustment was made to bring remuneration up to a market competitive level. The combined effect of these two categories of adjustments was that an increase in the total salary expense of approximately 8.5% was approved by the Board from 1 July 2010. Details of this will be reflected in the 2010/11 Annual Report.

Performance-related pay framework

All permanent employees are eligible to earn a performance-related payment in addition to their fixed remuneration. Performance-related payments are designed to align staff to the organisation's objectives and to reflect superior performance rather than delivery of expected outcomes.

Any payment under this framework is based on a combination of the investment performance of the Future Fund over rolling three year periods (the Investment Plan) and the individual performance of the employee over the year taking into account the responsibilities of their role (the Annual Plan). The mix between these two factors varies according to the role.

In 2009/10, the General Manager and Chief Investment Officer had a 60% weighting to the Investment Plan with 40% weighted to the Annual Plan. Investment staff had an equal weighting between the Investment Plan and Annual Plan and all other staff have a 25% weighting to the Investment Plan and 75% exposure to the Annual Plan.

Performance pay summary

FFMA Classification	Employees who received payments	Aggregated performance pay (\$)	Minimum performance pay (\$)	Maximum performance pay (\$)	Average payment (\$)
FFMA Band 1, 2 & 3	22	145,089	873	15,167	6,595
FFMA Band 4, 5 & 6	47	4,419,637	3,684	348,050	94,035
Total	69	4,564,726			66,155

The payments above include pro-rata performance pay for staff that were not employed for the full 12 month cycle but were eligible for payment. Two staff were not eligible for performance-related payments as they were on short-term arrangements.

Investment Plan

The Investment Plan recognises outperformance against both real return and relative return hurdles. Exposure is equally weighted between the two. For any payment to be triggered under the real return component, the rolling three year return must be at least CPI +4.5% pa (the benchmark return set by Government and the most important success indicator for the organisation). At this level, 50% of the real return component is payable. This rises in a linear way to 100% of this component being paid if returns over rolling three year periods are CPI +7.0% pa or more. While there is discretion to make a payment for performance between CPI +4.0% and CPI +4.49%, no payment can be made for performance below this level.

For any payment to be triggered under the relative return component, the Future Fund must, over rolling three year periods, outperform the 'policy portfolio' (a combination of weighted market benchmarks set by the Board to reflect its investment strategy. These are set out in the Investment Report). This component of the Investment Plan is designed to capture value added by the management team through adjustments to portfolio exposures (within Board-approved control bands) and through the investment manager and asset selection program. A linear scale applies with the maximum payment triggered where the excess return over the policy portfolio averages 150 basis points (or more) pa over a rolling three year period.

Annual Plan

The Annual Plan captures the performance of each individual in their role in the context of the Board's view of the organisation's overall performance. Individual performance is assessed taking into account both functional competence and behaviour. Performance over the year must be outstanding in every respect for an employee to receive their maximum entitlement under this plan.

Performance-related payments to staff in 2009/10

Performance-related payments to staff amounted to approximately 36% of the fixed salary expense in 2009/10. This was 63% of the maximum potential payment.

A breakdown of these payments by classification band is provided in the table below.

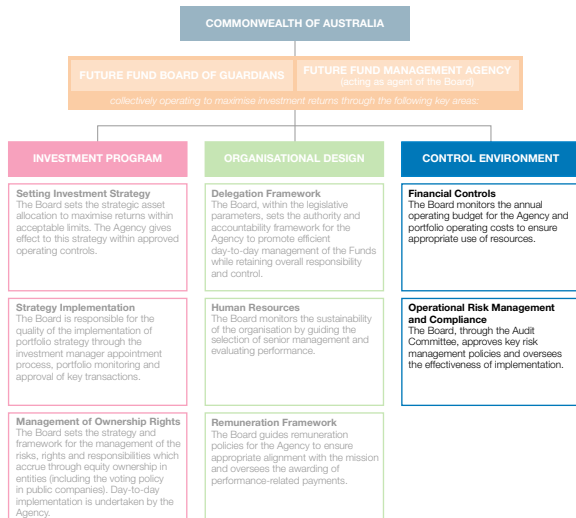
Additional disclosures relating to the remuneration of senior executives are set out in the financial statements. As noted above, there was no increase in the fixed salaries of these senior executives relative to the previous year although small variations in reported earnings occurred due to timing of payroll cycles.

To further align employee remuneration with the long-term performance of the Future Fund, employees are able to defer receipt of part or all of any performance-related payment to which they are eligible. These deferred payments remain tied to the Future Fund portfolio for a minimum of two years and are adjusted negatively or positively to reflect the earnings.

Board fees

Fees payable to Board members are determined by the Remuneration Tribunal. The Tribunal's Determination 2009/14, effective from 1 October 2009, set the annual fee payable to the Chair as \$175,340 and to all other members as \$87,680. The official travel entitlement for Board members was set at tier 1. Board members are not eligible for performance-related payments.

Control Environment



Financial controls

All costs for investment activity and the operations of the Board and Agency are met from the assets of the Funds, rather than from appropriations through Parliament. The Board monitors the annual operating budget for the Agency to ensure the appropriate use of resources consistent with the organisation's objectives.

A monthly report of Agency operating costs against this budget is provided to the Board.

The Board also monitors portfolio operating costs in addition to direct Agency and Board operating expenses.

The purchase of goods and services by the Agency is consistent with the Commonwealth Procurement Guidelines and is based on the principles of value for money, open and effective competition, ethics and fair dealing, accountability and reporting, national competitiveness and industry development, and support for other Australian Government policies. These principles have been incorporated into the appropriate internal policies and internal audit conducts probity reviews to help ensure compliance.

The Agency publishes certain mandatory information on its procurement activity on its website and additional information on expenditure on contracts and consultancies is available on the Austender website at www.tenders.gov.au. The organisation did not undertake any campaign advertising during the year and incurred no reportable recruitment advertising costs.

During 2009/10 eight new consultancy contracts were entered into by the Agency involving total actual expenditure of \$233,322. In addition, four ongoing consultancy contracts were active during the 2009/10 year, involving total actual expenditure of \$428,676.

The *Environment Protection and Biodiversity Conservation Act 1999* requires the Agency to report on how its activities accord with ecologically sustainable development and on its environmental performance. As detailed in the section on the management of ownership rights in this report, the Agency has appointed an investment specialist to oversee ownership rights and to consider the integration of material environmental, social and governance risks and opportunities into the design and implementation of the portfolio. In terms of its own activities, the organisation remains a small tenant in a large multi-tenancy office building without separate metering of water or electricity. While building management has upgraded energy and water management systems throughout the building during the year, it is not possible to track the impact on energy and water use in the Agency's tenancy. During the year low energy lighting and motion sensors were installed in eight newly created meeting rooms.

The purchase of investment management, investment advisory, master custody and safekeeping services for the purpose of managing and investing the assets of the public asset funds are excluded from the mandatory provisions of the Commonwealth Procurement Guidelines.

Operating costs

The legislation requires the Board and Agency to report on various aspects of the costs incurred in investing the assets of the Future Fund and the Nation-building Funds and these are reported as follows.

Disclosure of costs as required under section 81 of the Future Fund Act 2006*

Future Fund

Purpose	Amount debited 2007/08	Amount debited 2008/09	Amount debited 2009/10
Contracts with investment managers	\$29,637,603	\$55,727,014	\$244,766,537
Board remuneration and allowances	\$709,134	\$743,311	\$757,417
Agency remuneration and employment costs	\$6,049,866	\$12,424,311	\$16,189,583
Consultants to the Board and Agency	\$6,808,930	\$11,457,160	\$11,760,416
Agency operations	\$5,033,200	\$8,209,483	\$12,986,047

Building Australia Fund

Purpose	Amount debited 2007/08	Amount debited 2008/09	Amount debited 2009/10
Contracts with investment managers	Zero	\$382,011	\$6,421,224
Board remuneration and allowances	Zero	Zero	Zero
Agency remuneration and employment costs	Zero	Zero	Zero
Consultants to the Board and Agency	Zero	Zero	Zero
Agency operations	Zero	\$3,500	\$10,028

Education Investment Fund

Purpose	Amount debited 2007/08	Amount debited 2008/09	Amount debited 2009/10
Contracts with investment managers	Zero	\$785,242	\$4,317,170
Board remuneration and allowances	Zero	Zero	Zero
Agency remuneration and employment costs	Zero	Zero	Zero
Consultants to the Board and Agency	Zero	Zero	Zero
Agency operations	Zero	\$3,500	\$10,028

Health and Hospitals Fund

Purpose	Amount debited 2007/08	Amount debited 2008/09	Amount debited 2009/10
Contracts with investment managers	Zero	\$45,895	\$3,466,798
Board remuneration and allowances	Zero	Zero	Zero
Agency remuneration and employment costs	Zero	Zero	Zero
Consultants to the Board and Agency	Zero	Zero	Zero
Agency operations	Zero	\$3,500	\$10,028

* Note that these costs are reported on a cash basis whereas the costs in the table on page 44 include accruals.

The Board has deemed it appropriate to use as its benchmark measurement for costs the disclosure measures prescribed for financial products as laid out in Schedule 10 of the related Regulations to the *Corporations Act 2001*. These prescribed disclosures have been further clarified by ASIC through its Information Releases.

The Board has not presented a relative benchmark measure but has reported its costs, as defined below, to enable readers of the Annual Report to make their own comparisons to other financial institutions. The Board also reports comparisons to the previous year, where applicable.

The costs reported are the total costs for the year, rather than only the items reported in the table, and are extracted from the respective Financial Statements.

As the funds do not incur costs associated with, nor charge fees to, members there is no disclosure of fees and costs charged directly to members as required under the Regulations. The Board has deemed it appropriate to report costs under the following categories as defined by Schedule 10 of the Regulations.

- **Management costs:** these costs include custody fees (exclusive of settlement costs), amounts paid to external fund managers (including performance fees) and any other investment-related expenses and reimbursements, inclusive of amounts incurred in administering the fund. This also includes all internal operating costs including remuneration of Board and staff.
- **Transactional and operational costs:** these costs include brokerage, stamp duties and custody costs charged for transaction settlement.
- **Indirect cost ratio:** the ratio of the fund's management costs to the fund's average net assets.

As noted in the Investment Report, the increased expense incurred during 2009/10 reflects the costs of the continued expansion of the investment program and, in the case of the Future Fund, the continued transfer from cash into the broader program over the year. Performance-based fees are negotiated with a number of the appointed investment managers, and accruals for these fees (where relevant) have been made in 2009/10 for the first time.

Operating costs are expected to continue to grow as the portfolio becomes more diversified. While we are very conscious of the impact of operating costs, our focus is on maximising after-cost returns rather than simply keeping costs as low as possible.

Cost disclosures

	2009/10			2008/09	2007/08
	Management costs	Transactional and operational costs	Indirect cost ratio	Indirect cost ratio	Indirect cost ratio
Future Fund (including Telstra holding)	\$269,139,800	\$70,749,200	0.410%	0.179%	0.066%
Future Fund (excluding Telstra holding)	\$266,385,387	\$42,188,200	0.436%	0.203%	0.075%
Building Australia Fund	\$8,269,284	\$278,951	0.082%	0.028%	–
Education Investment Fund	\$5,483,348	\$177,879	0.090%	0.028%	–
Health and Hospitals Fund	\$4,642,515	\$158,669	0.095%	0.031%	–
Higher Education Endowment Fund	Discontinued	Discontinued	Discontinued	0.028%	0.017%

Operational Risk Management and Compliance

The Board's Audit Committee oversees the compliance and audit functions, monitors control frameworks, reviews key financial statements, tracks legislative compliance and evaluates the efficiency and effectiveness of the risk management plan.

All members of the Board are members of the Audit Committee, with the exception of Mr Murray, who is excluded as is customary due to his role as Chair and statutory Chief Executive of the Agency. The Agency also operates an Operational Risk and Compliance Committee to assist the Audit Committee in the effective management of operational risks.

The Audit Committee has approved the fraud risk assessment and fraud control plan prepared by the Agency. The Chief Executive Officer is satisfied that fraud risk assessments and fraud control plans have been prepared and comply with the Commonwealth Fraud Control Guidelines, that appropriate fraud prevention, detection, investigation and reporting procedures and processes are in place and that annual fraud data is collected and reported that complies with the Commonwealth Fraud Control Guidelines.

PricewaterhouseCoopers provides internal audit services reporting to the Audit Committee and has full access to staff and information when conducting its reviews. The Australian National Audit Office undertakes the external audit of the organisation engaging a professional accounting firm to assist in this process.

The Audit Committee has identified the key risks to the successful delivery of the Board's mission and, in conjunction with the Agency, monitors the effectiveness of controls designed to manage each key risk.

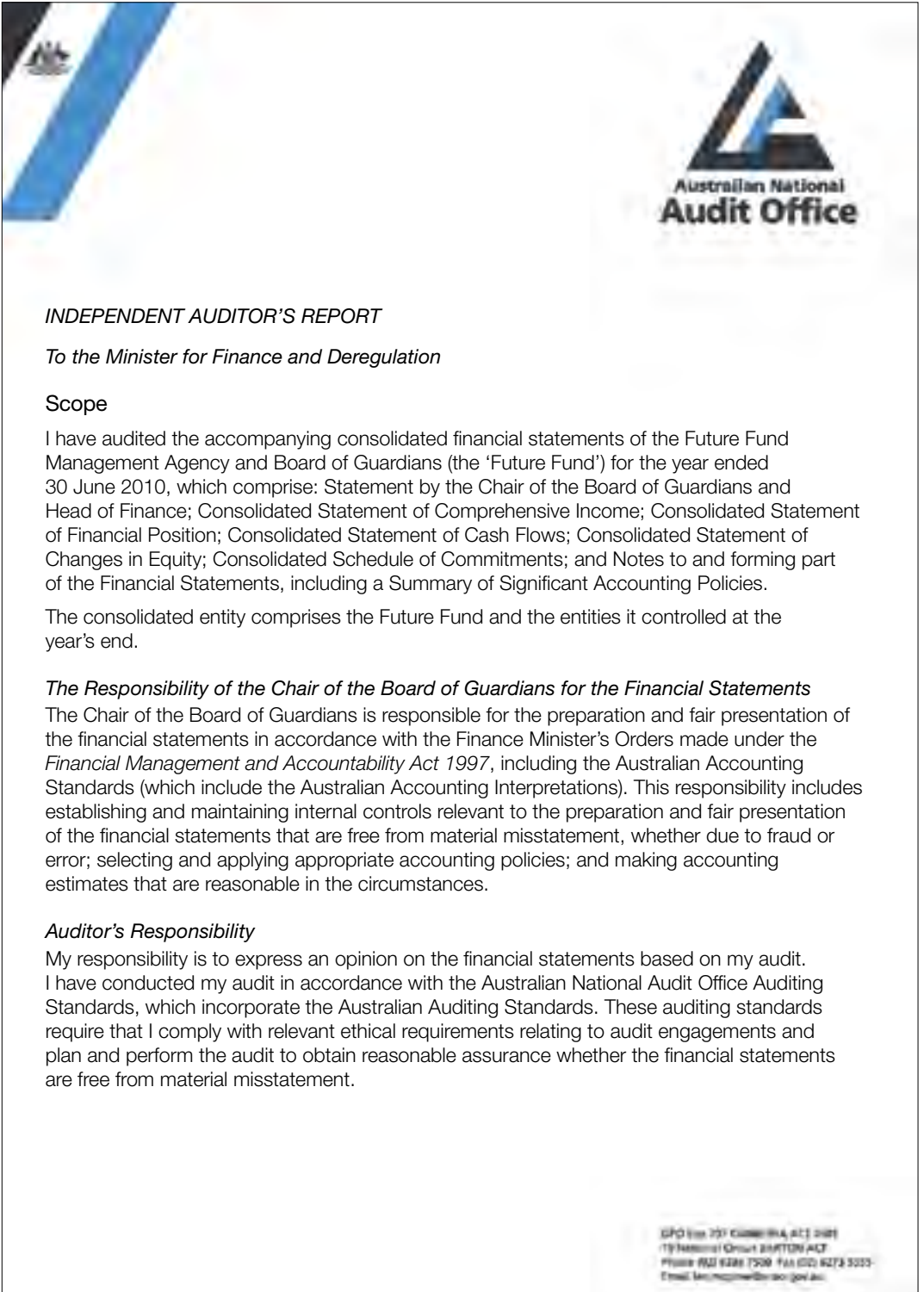
The Agency's Operational Risk and Compliance Committee meets on a monthly basis and supports the Audit Committee in managing these risks. The Operational Risk and Compliance Committee maintains a risk register which documents the key risks and core controls that mitigate the likelihood and consequence of an adverse event occurring. It monitors and reports to the Audit Committee on the effectiveness of these key controls and provides a sign-off on a quarterly basis.

Consolidated Financial Statements

For the financial year ended 30 June 2010

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These consolidated financial statements consist of the Future Fund Management Agency, the Board of Guardians and its subsidiaries



INDEPENDENT AUDITOR'S REPORT

To the Minister for Finance and Deregulation

Scope

I have audited the accompanying consolidated financial statements of the Future Fund Management Agency and Board of Guardians (the 'Future Fund') for the year ended 30 June 2010, which comprise: Statement by the Chair of the Board of Guardians and Head of Finance; Consolidated Statement of Comprehensive Income; Consolidated Statement of Financial Position; Consolidated Statement of Cash Flows; Consolidated Statement of Changes in Equity; Consolidated Schedule of Commitments; and Notes to and forming part of the Financial Statements, including a Summary of Significant Accounting Policies.

The consolidated entity comprises the Future Fund and the entities it controlled at the year's end.

The Responsibility of the Chair of the Board of Guardians for the Financial Statements

The Chair of the Board of Guardians is responsible for the preparation and fair presentation of the financial statements in accordance with the Finance Minister's Orders made under the *Financial Management and Accountability Act 1997*, including the Australian Accounting Standards (which include the Australian Accounting Interpretations). This responsibility includes establishing and maintaining internal controls relevant to the preparation and fair presentation of the financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's Responsibility

My responsibility is to express an opinion on the financial statements based on my audit. I have conducted my audit in accordance with the Australian National Audit Office Auditing Standards, which incorporate the Australian Auditing Standards. These auditing standards require that I comply with relevant ethical requirements relating to audit engagements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

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An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Future Fund's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Future Fund's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the Future Fund, as well as evaluating the overall presentation of the financial statements.

I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

Independence

In conducting the audit, I have followed the independence requirements of the Australian National Audit Office, which incorporate the requirements of the Australian accounting profession.

Auditor's Opinion

In my opinion, the consolidated financial statements of the Future Fund:

- (a) have been prepared in accordance with the Finance Minister's Orders made under the *Financial Management and Accountability Act 1997*, including the Australian Accounting Standards; and
- (b) give a true and fair view of the matters required by the Finance Minister's Orders including the Future Fund's consolidated financial position as at 30 June 2010 and its consolidated financial performance and cash flows for the year then ended.

Australian National Audit Office



Ian McPhee
Auditor-General

Canberra

27 September 2010

Statement by the Chair of the Board of Guardians and Head of Finance

In our opinion, the attached consolidated financial statements of the Future Fund Management Agency and the Board of Guardians (together the 'Fund') for the year ended 30 June 2010 are based on properly maintained records and give a true and fair view of the financial position and the financial performance of the Fund, in accordance with the matters required by the Finance Minister's Orders, made under the *Financial Management and Accountability Act 1997*, as amended, and are in compliance with Australian Accounting Standards.

In preparing the financial statements, the Fund has applied the exemption provided by the Minister for Finance and Deregulation allowing the Fund to present a financial report in a format consistent with that used in the funds management industry in place of the prescribed format as outlined in Annexure A to Schedule 1 of the Finance Minister's Orders. The effect of this exemption is that Fund will present its financial report as a single entity.



S Doyle
Acting Chair
27 September 2010



P Mann
Head of Finance
27 September 2010

Consolidated statement of comprehensive income

for the financial year ended 30 June 2010

	Notes	Year ended 30 June 2010 \$'000	Year ended 30 June 2009 \$'000
INCOME			
Dividends & imputation credits	4	1,266,538	1,474,530
Distributions	4	121,011	5,122
Interest income from financial assets not held at fair value through profit or loss	3	71,274	105,548
Net gain/(loss) on financial instruments held at fair value through profit or loss	4	4,085,339	(4,059,621)
Net foreign currency gains/(losses)	4	1,107,333	(715,126)
Other income	5	8,868	156
TOTAL INCOME/(LOSS)		6,660,363	(3,189,391)
EXPENSES			
Investment management fees and advisory fees		109,429	45,427
Investment manager performance fees		112,379	30,780
Custodian's fees		7,051	4,594
Brokerage, duties and other statutory charges		69,362	20,341
Other investment portfolio expenses		8,944	5,476
Agency employees' remuneration	6	18,096	14,277
Other expenses	6,7	14,628	8,591
TOTAL EXPENSES		339,889	129,486
OPERATING RESULT/(LOSS) FOR THE YEAR		6,320,474	(3,318,877)
Other comprehensive income		-	-
TOTAL COMPREHENSIVE INCOME/(LOSS)		6,320,474	(3,318,877)

The above statement should be read in conjunction with the accompanying notes.

Consolidated statement of financial position

as at 30 June 2010

	Notes	Year ended 30 June 2010 \$'000	Year ended 30 June 2009 \$'000
ASSETS			
Financial assets			
Cash and cash equivalents	16	3,024,421	1,869,674
Term deposits		–	3,200
Receivables	9	1,063,119	589,553
Investments	8	66,253,941	60,293,023
Other financial assets		2,129	427
Total financial assets		70,343,610	62,755,877
Non-financial assets			
Investment property at fair value	11,11A	158,339	–
Trees in a plantation forest	11A	85,618	–
Plant and equipment	10	2,531	1,285
Intangibles	10	11,221	145
Total non-financial assets		257,709	1,430
TOTAL ASSETS		70,601,319	62,757,307
LIABILITIES			
Financial liabilities			
Investments – Derivatives	8	2,072,570	818,187
Payables	12	1,238,379	972,307
Other provisions	13	1,439	268
Total financial liabilities		3,312,388	1,790,762
Non-financial liabilities			
Employee provisions	13	6,895	4,983
Total non-financial liabilities		6,895	4,983
TOTAL LIABILITIES		3,319,283	1,795,745
NET ASSETS		67,282,036	60,961,562
EQUITY AND AMOUNT ATTRIBUTABLE TO THE GOVERNMENT			
Contributions by Government	14	60,536,831	60,536,831
Accumulated results		6,745,205	424,731
TOTAL EQUITY AND AMOUNT ATTRIBUTABLE TO THE GOVERNMENT		67,282,036	60,961,562

The above statement should be read in conjunction with the accompanying notes.

Consolidated statement of cash flows

for the financial year ended 30 June 2010

	Notes	Year ended 30 June 2010 \$'000	Year ended 30 June 2009 \$'000
CASH FLOWS FROM OPERATING ACTIVITIES			
Proceeds from sale of financial instruments held at fair value through profit or loss		86,218,791	128,895,561
Purchase of financial instruments held at fair value through profit or loss		(89,318,410)	(128,618,343)
Interest received		68,037	112,180
Dividends received		971,079	1,140,984
Distributions received		110,007	5,122
Franking credit refunds received		323,224	291,820
Realised foreign exchange gains/(losses)		3,200,798	(2,032,640)
GST refund received		10,170	4,890
Other income received		6,042	28
Investment manager and advisory fees paid		(88,346)	(35,695)
Investment manager performance fees paid		(19,865)	–
Custodian's fees paid		(7,277)	(2,644)
Transaction fees paid		(122,466)	(18,646)
Other expenses paid		(48,506)	(31,576)
Net cash provided by/(used in) operating activities	16	1,303,278	(288,959)
CASH FLOWS FROM INVESTING ACTIVITIES			
Proceeds from sale of investments		3,200	53,700
Purchase of investment property		(156,054)	–
Purchase of trees in a plantation forest		(81,470)	–
Purchase of lease rights		(10,514)	–
Purchase of plant and equipment and software		(2,187)	(393)
Net cash provided by/(used in) investing activities		(247,025)	53,307
CASH FLOWS FROM FINANCING ACTIVITIES			
Amounts contributed by Government		–	–
Net cash received from financing activities		–	–
Net increase/(decrease) in cash held		1,056,253	(235,652)
Cash at the beginning of the reporting period		1,869,674	2,145,242
Effects of exchange rate changes on the balance of cash held in foreign currencies		98,494	(39,916)
Cash at the end of the reporting period	16	3,024,421	1,869,674

The above statement should be read in conjunction with the accompanying notes.

Consolidated statement of changes in equity

Item	Year ended 30 June 2010			Year ended 30 June 2009		
	Accumulated results	Contributed equity	Total equity	Accumulated results	Contributed equity	Total equity
	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000
Opening balance	424,731	60,536,831	60,961,562	3,743,608	60,396,090	64,139,698
Net operating result	6,320,474	-	6,320,474	(3,318,877)	-	(3,318,877)
Other comprehensive income	-	-	-	-	-	-
Total comprehensive income	6,320,474	-	6,320,474	(3,318,877)	-	(3,318,877)
Contributions made by Government	-	-	-	-	140,741	140,741
Closing balance	6,745,205	60,536,831	67,282,036	424,731	60,536,831	60,961,562

The above statement should be read in conjunction with the accompanying notes.

Consolidated schedule of commitments as at 30 June 2010

	Notes	30 June 2010 \$'000	30 June 2009 \$'000
BY TYPE			
CAPITAL COMMITMENTS			
Infrastructure, plant and equipment		–	–
Investments	8	8,064,995	7,418,243
Total capital commitments		8,064,995	7,418,243
OTHER COMMITMENTS			
Operating leases ^(a)		1,888	1,583
Other commitments ^(b)		3,532	1,275
Total other commitments		5,420	2,858
BY MATURITY			
CAPITAL COMMITMENTS			
One year or less		8,064,995	7,418,243
From one to five years		–	–
Over five years		–	–
Total capital commitments by maturity		8,064,995	7,418,243
OTHER COMMITMENTS			
Operating lease commitments			
One year or less		1,298	717
From one to five years		590	866
Over five years		–	–
Total operating lease commitments by maturity		1,888	1,583
Other commitments			
One year or less		3,086	829
From one to five years		446	446
Over five years		–	–
Total other commitments by maturity		3,532	1,275

Note: Commitments are GST inclusive.

(a) Operating lease commitments relate to rental commitments for the lease of property and for office equipment. Lease terms have between 1 and 4 years remaining with options to extend for periods up to a further 5 years. The Fund has no option to purchase any leased items at the conclusion of the lease term.

(b) Other commitments relate to contractual obligations for the provision of internal audit services, payroll services and consultancies.

The above schedule should be read in conjunction with the accompanying notes.

Notes to and forming part of the consolidated financial statements for the financial year ended 30 June 2010

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Note 1: Objectives of the Future Fund and the responsibilities of the Agency and the Board

The *Future Fund Act 2006* (as amended) ('the Act') commenced on 3 April 2006 and established the Future Fund Special Account ('the Fund Account'), the Future Fund Board of Guardians ('the Board') and the Future Fund Management Agency ('the Agency'), collectively referred to as the Future Fund ('the Fund'). The object of the Act is to strengthen the Commonwealth's long-term financial position by providing for unfunded public sector superannuation liabilities.

The Future Fund will make provision for unfunded superannuation liabilities that will become payable during a period when an ageing population is likely to place significant pressure on the Commonwealth's finances. The legislation quarantines the Fund, the balance of the Fund Account and Fund investments, for the ultimate purpose of paying unfunded superannuation liabilities and expenses associated with the investments of the Fund and the administration of both the Board of Guardians and the Future Fund Management Agency.

Future Fund Management Agency (the Agency)

The Agency is a statutory agency for the purposes of the *Public Service Act 1999* (the Public Service Act) and is prescribed for the purposes of the *Financial Management and Accountability Act 1997* (the FMA Act). The Agency is responsible for implementing the investment decisions made by the Future Fund Board of Guardians (the Board).

The Agency is responsible for the operational activities associated with the investment of funds in the Fund Account. This includes the provision of advice to the Board on the investment of the portfolio and managing the Board's contracts with investment managers, advisers and other service providers.

The Agency also supports the Board of Guardians in the investment of the assets of the Building Australia Fund, the Health and Hospitals Fund and the Education Investment Fund (together the 'Nation-building Funds').

Future Fund Board of Guardians (the Board)

The Board is a body corporate with perpetual succession and is a separate legal identity to the Commonwealth.

In line with subsection 18(1) of the enabling legislation, the Government issued the Board with the first Investment Mandate for the Future Fund, effective 22 May 2006. The objective of these directions is to give guidance to the Board in relation to its investment strategy for the Future Fund.

The roles and responsibilities of the Board are set out in the enabling legislation. The Board is collectively responsible for the investment decisions of the Fund and for the safekeeping and performance of the assets of the Fund. As such, the Board's primary role is to provide strategic direction to the investment activities of the Fund including the development and implementation of an investment strategy that adheres to the Investment Mandate.

The Board is also responsible for the investment of the assets of the Nation-building Funds as set out in the *Nation-building Funds Act 2008*. The assets and results of the Nation-building Funds do not form part of these financial statements.

Future Fund Investment Mandate Directions 2006

The objective of these directions is to give guidance to the Board in relation to its investment strategy for the Future Fund. The Future Fund Board of Guardians is required under section 18 of the Act to seek to maximise the return earned on the Fund over the long term, consistent with international best practice for institutional investment and subject to its obligations under the Act and any directions given by the responsible Ministers under subsection 18(1) or subclause 8(1) of Schedule 1 of the Act. Investments by the Future Fund will be confined to financial assets (see also Note 2.4).

Note 2: Summary of significant accounting policies

2.1 Basis of preparation of the consolidated financial statements

These consolidated financial statements comprise the Future Fund Management Agency and the Future Fund Board of Guardians, collectively referred to as the Future Fund ('the Fund'), in accordance with Section 80 of the *Future Fund Act 2006 (as amended)*.

The financial statements are required by section 49 of the *Financial Management and Accountability Act 1997*, and are general purpose financial statements prepared on a going concern basis.

The financial statements have been prepared in accordance with:

- Finance Minister's Orders (FMOs) (being the *Financial Management and Accountability Orders (Financial Statements for reporting periods ended on or after 1 July 2009)*);
- Australian Accounting Standards and Accounting Interpretations issued by the Australian Accounting Standards Board (AASB) that apply for the reporting period.

In preparing the consolidated financial statements, the Fund has applied the exemption provided by the Minister for Finance and Deregulation allowing the Fund to present a financial report in a format consistent with that used in the funds management industry in place of the prescribed format as outlined in Annexure A to Schedule 1 of the Finance Minister's Orders. The effect of this exemption is that the Fund will present its financial report as a single entity.

These consolidated financial statements have been prepared on an accrual basis and are in accordance with the historic cost convention, as modified by the revaluation of financial assets and financial liabilities (including derivative instruments) at fair value through the profit or loss account, the adoption of the fair value model in accounting for investment property and the revaluation of employee entitlements. Cost is based on the fair values of the consideration given in exchange for assets.

The consolidated statement of financial position is presented on a liquidity basis with assets and liabilities presented in decreasing order of liquidity and with no distinction between current and non-current.

Unless alternative treatment is specifically required by an accounting standard, assets and liabilities are recognised in the statement of financial position when and only when it is probable that future economic benefits will flow and the amounts of the assets or liabilities can be reliably measured. Assets and liabilities arising under agreements equally proportionately unperformed are not recognised unless required by an Accounting Standard.

Liabilities and assets which are unrecognised in the statement of financial position are reported as appropriate in the schedule of commitments or as contingencies in Note 17 to the financial statements.

Unless alternative treatment is specifically required by an accounting standard, revenues and expenses are recognised in the statement of comprehensive income when and only when the flow, consumption or loss of economic benefits has occurred and can be reliably measured.

Significant Accounting Judgements and Estimates

As a result of developments in global markets during the current period and immediate comparative period, generally known as the global financial crisis, liquidity in some investment markets has decreased. As a result, the volume of trading in a small proportion of investments held by the Fund has also decreased and may therefore be deemed to be investments in an inactive or unquoted market. The valuation of those investments is subject to a greater uncertainty and requires greater judgement. Further details surrounding the judgements and estimates used to value these investments are disclosed in Note 20F.

In relation to collective investment vehicles, significant judgement is required in making assumptions and estimates which are inputs to the fair value of such investments.

Note 2: Summary of significant accounting policies (continued)

2.2 Statement of compliance

The financial report complies with Australian Accounting Standards.

Adoption of new and revised accounting standards in the current reporting period

The Australian Accounting Standards Board (the 'AASB') has issued amendments to existing standards. These amendments are denoted by year and then number.

Australian Accounting Standards require the Future Fund to disclose Australian Accounting Standards that have not yet been applied, for standards that have been issued but are not yet effective. The Fund must also disclose new standards and interpretations affecting amounts reported in the current period and those standards adopted with no effect on the financial statements in the current period. The table below illustrates standards and amendments that apply to the Future Fund in the current reporting period for the first time.

Title	Nature of change and impact on the financial statements
AASB 101 <i>Presentation of Financial Statements</i> , AASB 2007-08 <i>Amendments to Australian Accounting Standards arising from AASB 101 and AASB 2007-10 Further Amendments to Australian Accounting Standards arising from AASB 101</i>	AASB 101 has introduced terminology changes (including revised titles for the financial statements) and changes to the format and content of the financial statements.
AASB 2009-2 <i>Amendments to Australian Accounting Standards – Improving Disclosures about Financial Instruments</i> .	The amendments to AASB 7 expand the disclosures required in respect of fair value measurements and liquidity risk. These are disclosed in Note 20. The Fund has elected not to provide comparative information for these expanded disclosures in the current year in accordance with the transitional reliefs offered in these amendments.

The next table illustrates standards and amendments that apply to the Future Fund in the current reporting period for the first time but have no effect on the financial statements in the current period.

Title	Nature of change and impact on the financial statements
Amendments to AASB 107 <i>Statement of Cash Flows</i>	The amendments specify that only expenditures that result in a recognised asset in the statement of financial position can be classified as investing activities in the statement of cash flows.
AASB 2008-5 <i>Amendments to Australian Accounting Standards arising from the Annual Improvements Project</i>	Amendments to 25 different standards which largely clarify the accounting treatment where previous accounting practice varied.

Standards and amendments that will become effective in future reporting periods

The table on the next page illustrates standards and amendments that will become effective for, and apply to, the Future Fund in future reporting periods. The nature of the impending change within the table has been out of necessity abbreviated and users should consult the full version available on the AASB's website to identify the full impact of the change. The expected impact on the financial report of adoption of these standards is based on the Future Fund's initial assessment at this date, but may change. The Future Fund intends to adopt all of the standards upon their application date. No accounting standard has been adopted earlier than the effective date in the current period.

Note 2: Summary of significant accounting policies (continued)

2.2 Statement of compliance (continued)

Title	Application date	Nature of impending change and impact expected on the financial report
AASB 2009-11 <i>Amendments to Australian Accounting Standards arising from AASB9</i>	Applies on a modified retrospective basis to annual periods beginning on or after 1 January 2013	<p>AASB 9 introduces new requirements for classifying and measuring financial assets, as follows:</p> <ul style="list-style-type: none"> • Debt instruments meeting both a 'business model' test and a 'cash flow characteristics' test are measured at amortised cost (the use of fair value is optional in some limited circumstances) • Investments in equity instruments can be designated as 'fair value through other comprehensive income' with only dividends being recognised in profit or loss • All other instruments (including all derivatives) are measured at fair value with changes recognised in the profit or loss <p>The concept of 'embedded derivatives' does not apply to financial assets within the scope of the Standard and the entire instrument must be classified and measured in accordance with the above guidelines.</p> <p>AASB 9 will not have a material impact on future consolidated financial statements of the Fund.</p>
AASB 2009-5 <i>Further Amendments to Australian Accounting Standards arising from the Annual Improvements Process</i>	Applies to annual reporting periods beginning on or after 1 January 2010	<p>Various amendments to Australian Accounting standards arising from the International Accounting Standards Board's annual improvement project.</p> <p>The adoption of these changes will not have a material impact on the consolidated financial statements of the Fund.</p>
AASB 2010-1 <i>Amendments to Australian Accounting Standards – Limited Exemption from Comparative AASB 7 Disclosures for First-time Adopters [AASB 1 & AASB 7]</i>	Applies to annual reporting periods beginning on or after 1 July 2010	This is not applicable to the Fund as it is not a first time adopter of AASB 7.

2.3 Principles of consolidation

Subsidiaries

The consolidated financial statements incorporate the assets and liabilities of all subsidiaries of the Fund as at 30 June 2010 and the results of all subsidiaries for the year then ended.

Subsidiaries are entities over which the parent entity has the power to govern the financial and operating policies, generally accompanying a shareholding of more than one-half of the voting rights. Any effects of potential voting rights that are currently exercisable or convertible are considered when assessing whether the parent entity controls another entity.

Note 2: Summary of significant accounting policies (continued)

2.3 Principles of consolidation (continued)

Subsidiaries are consolidated from the date on which control is transferred to the parent. They are de-consolidated from the date that control ceases. The purchase method of accounting is used for the acquisition of subsidiaries by the parent entity in preparing consolidated financial statements for the Fund.

The Fund presently has no allocation to minority interests as all subsidiaries are 100% owned. The list of all subsidiaries as at 30 June 2010 is disclosed at Note 15.

Intercompany transactions, balances and unrealised gains on transactions between companies are eliminated. Accounting policies have been changed where necessary to ensure consistency with the policies adopted by the Fund.

Associates

Associates are all entities over which the parent entity has significant influence but not control nor joint control. This is generally accompanied by a shareholding of between 20% and 50% of the voting rights. Associates are designated as investments and recorded at their fair value each balance date with changes directly credited to or charged to the statement of comprehensive income.

2.4 Financial assets

All investments of the Fund are in financial assets for the purposes of the GFS system in Australia as is required under section 16 of the Act.

The Fund's investment strategy has an allocation to Tangible Assets (including real estate, timber and infrastructure) which are non-financial assets. To access this economic exposure, the Fund invests in the securities of investments vehicles which in turn invest in non-financial assets. This approach is envisaged in the explanatory memorandum to the Bill.

Where the Fund holds a controlling interest in such a vehicle, it is treated as a subsidiary of the Fund and the underlying non-financial assets are consolidated onto the Fund's statement of financial position.

The non-financial assets in Note 10 include investments and intangible assets held by controlled vehicles.

Financial assets are recognised and derecognised on trade date where purchase or sale of an investment is under a contract whose terms require delivery of the investment within the timeframe established by the market concerned. Financial assets are initially measured at fair value, net of transaction costs that are directly attributable to acquisition or issue of the financial asset.

Further details on how the fair values of financial instruments are determined are disclosed in Note 20F.

Note 2: Summary of significant accounting policies (continued)

2.4 Financial Assets (continued)

Investments

All investments, including those in associates (refer 2.3 above) are designated as financial assets through profit and loss on acquisition. Subsequent to initial recognition, all investments held at fair value through profit and loss are measured at fair value with changes in their fair value recognised in the statement of comprehensive income each reporting date.

Investments in collective investment vehicles are recorded at fair value on the date which consideration is provided to the contractual counterparty under the terms of the relevant subscription agreement. Any associated due diligence costs in relation to these investments are expensed when incurred.

The following methods are adopted by the Fund in determining the fair value of investments:

- Listed securities, exchange traded futures and investments in listed managed investment schemes are recorded at the quoted bid price on relevant stock exchanges.
- Unlisted managed investment schemes and collective investment vehicles are re-measured by the Fund based on the estimated fair value of the net assets of each scheme or vehicle at the reporting date.

In determining the fair value of the net assets of unlisted managed investment schemes and collective investment vehicles, reference is made to the underlying unit price provided by the Manager (where available), associated Manager valuation reports and capital account statements and the most recent audited financial statements of each scheme.

Manager valuation reports are reviewed to ensure the underlying valuation principles are materially compliant with AIFRS and applicable industry standards including International Private Equity and Venture Capital Valuation Guidelines as endorsed by the Australian Private Equity and Venture Capital Association Limited (AVCAL).

- Derivative instruments including forward foreign exchange contracts, interest rate swap agreements, repurchase agreements, credit default swaps and options are recorded at their fair value on the date the contract is entered into and are subsequently re-measured to their fair values at each reporting date. The Fund does not designate any derivatives as hedges in a hedging relationship.
- Asset backed securities, bank bills, negotiable certificates of deposit and corporate debt securities which are traded in active markets are valued at the quoted market bid price. Securities for which no active market is observable are valued at current market rates using broker sourced market quotations and/or independent pricing services as at the reporting date.

Note 20F has further information surrounding the determination of fair values for investments.

Note 2: Summary of significant accounting policies (continued)

2.5 Revenue

Dividends, franking credits and distribution income are recognised when the right to receive payment is established.

Interest revenue is recognised in the statement of comprehensive income for all financial instruments that are not held at fair value through profit or loss using the effective interest method as set out in *AASB 139 Financial Instruments: Recognition and Measurement*. Interest income on assets held at fair value through profit or loss is included in the net gains/(losses) on financial instruments in the statement of comprehensive income.

Receivables for goods and services, which have 30 day terms, are recognised at the nominal amounts due less any provision for bad and doubtful debts. Collectability of debts is reviewed at balance date. Provisions are made when collectability of the debt is no longer probable.

Rental income from operating leases is recognised on a straight-line basis over the terms of the relevant leases.

Timberlands income is the operating income arising from timberland investments (that is, other than the changes in the fair value of the underlying timberland assets). Timber sales are recognised upon delivery to the customer at which point the significant risks and rewards of ownership are transferred to the customer and the revenue can be reliably estimated. Timber expenses include harvesting, haulage, administrative expenses and the depletion of plantation forest trees.

2.6 Other income

Services and resources received free of charge

Services and resources received free of charge are recognised as revenue when, and only when, a fair value can be reliably determined and the services would have been purchased if they had not been donated. Use of those resources is recognised as an expense.

Other income

Other income is measured at the fair value of consideration received or receivable.

Contributions of assets at no cost of acquisition are recognised as revenue at their fair value when the asset qualifies for recognition, unless received from another government agency as a consequence of a restructuring of administrative arrangements.

2.7 Transactions with the Government as owner

2.7.1 Credits to the Fund Account

From time to time the responsible Ministers may determine that additional amounts are to be credited to the Fund Account. In addition, the responsible Ministers may transfer Commonwealth-owned financial assets to the account. These amounts are shown as Contributions by Government in Note 14.

Note 2: Summary of significant accounting policies (continued)

2.7.2 Debits to the Fund Account

Amounts may be debited from the Fund Account in accordance with the purposes of the Fund Account as set out in the *Future Fund Act 2006* (as amended). The main purpose of the Fund Account is to discharge unfunded superannuation liabilities from whichever is the earlier of; (a) the time when the balance of the Fund is greater than or equal to the target asset level or (b) 1 July 2020.

2.8 Employee entitlements

Liabilities for services rendered by employees are recognised at the end of the financial year to the extent that they have not been settled. The nominal amount is calculated with regard to the rates expected to be paid on settlement of the liability.

2.8.1 Leave

The liability for employee entitlements includes provisions for annual leave and long service leave. No provision has been made for sick leave as all sick leave is non-vesting and the average sick leave taken in future years by employees of the Future Fund is estimated to be less than the annual entitlement for sick leave.

The leave liabilities are calculated on the basis of employees' remuneration, including the Agency's employer superannuation contribution rates to the extent that the leave is likely to be taken during service rather than paid out on termination.

The leave liabilities are calculated on the basis of employees' remuneration at the end of the financial year, adjusted for expected increases in remuneration effective from 1 July 2010. Liabilities for short-term employee benefits (i.e. wages and salaries, annual leave etc, expected to be settled within 12 months from the reporting date) are measured at their nominal amounts.

All other employee benefits are measured at the present value of the estimated future cash flows to be made in respect of all employees at the end of the financial year. The Australian Government Actuary has recommended the application of the shorthand method, as prescribed by the FMOs, for determining the present value of the long serve leave liability.

2.8.2 Superannuation

Staff of the Future Fund are variously eligible to contribute to the Commonwealth Superannuation Scheme (Defined Benefit), Public Sector Superannuation Scheme (Defined Benefit) or the Public Sector Superannuation Scheme (Accumulation Plan). Staff may join any other employee nominated schemes.

For any staff who are members of CSS (Defined Benefit) or PSS (Defined Benefit), the Future Fund makes employer contributions to the Australian Government at rates determined by an actuary to be sufficient to meet the cost to the government of the superannuation entitlements of its employees. The liability for superannuation benefits payable to an employee upon termination is recognised in the financial statements of the Australian Government.

As CSS and PSS are multi-employer plans within the meaning of AASB 119, all contributions are recognised as expenses on the same basis as contributions made to defined contribution plans. A liability has been recognised at the end of the financial year for outstanding superannuation co-contributions payable in relation to the final fortnight of the financial year.

Note 2: Summary of significant accounting policies (continued)

2.8.3 Performance-related Payments

All permanently employed staff at the Fund at the reporting date are eligible to receive an entitlement to a performance-related payment as approved by the Board. Employees who receive an entitlement may elect to have the entitlement converted to cash and paid to them. Alternatively, they may defer part or all of the payment for an initial two year period and receive a commitment from the Fund to pay them a future amount which will be dependent on the performance of the Fund over this two year period.

A liability has been recognised at the end of the financial year for outstanding performance-related payments payable in relation to the financial year. For employees who have elected to receive part or all of the entitlement as cash, the cash component of the entitlement is recognised as a liability at its nominal value. For employees who have elected to defer part or all of their entitlement, the deferred portion of their entitlement is measured at the present value of the expected future entitlement at the conclusion of the initial two year deferral period. The Fund has assumed that the portfolio will return CPI + 4.5% (being the minimum mandated return) in making the estimate of the future value of the entitlement. This future value has then been discounted at an appropriate Australian government bond rate to arrive at the present value of the liability. Actual returns are used to determine the present value of the entitlement for participation years where actual results are available.

2.9 Leases

A distinction is made between finance leases and operating leases. Finance leases effectively transfer from the lessor to the lessee substantially all risks and benefits incidental to ownership of leased non-current assets. Under operating leases the lessor effectively retains substantially all such risks and benefits.

The Future Fund holds operating leases only. Operating lease payments are charged to the statement of comprehensive income on a basis which is representative of the pattern of benefits derived from the leased assets.

2.10 Cash and cash equivalents

Cash means notes and coins held and any deposits held at call with a bank. Deposits held with a bank that are not at call are classified as investments. Cash is recognised at its nominal amount. Cash does not include any amounts held in escrow accounts, the use of which is restricted. These are treated as investments.

2.11 Financial Risk Management

Disclosures regarding the Future Fund's financial risks are presented in Note 20.

2.12 Trade Creditors

Trade creditors and accruals are recognised at their nominal amounts, being the amounts at which the liabilities will be settled. Liabilities are recognised to the extent that the goods or services have been received (and irrespective of the Fund having been invoiced).

2.13 Acquisition of Non Financial Assets

Non financial assets, apart from investment properties, timberland investments and trees in a plantation forest (Note 11 & 11A), are recorded at cost of acquisition except as stated below. The cost of acquisition includes the fair value of assets transferred in exchange and liabilities undertaken. Non financial assets are initially measured at their fair value plus transaction costs where appropriate.

Assets acquired at no cost, or for nominal consideration, are initially recognised as assets and revenues at their fair value at the date of acquisition.

Note 2: Summary of significant accounting policies (continued)

2.14 Plant and equipment – non financial assets

2.14.1 Asset recognition threshold on acquisition

Purchases of plant and equipment are recognised initially at cost in the statement of financial position, except for purchases costing less than \$2,000, which are expensed at the time of acquisition. The asset recognition threshold is applied to each functional asset. That is, items or components that form an integral part of an asset are grouped as a single asset.

The initial cost of an asset includes an estimate of the cost of dismantling and removing the item and restoring the site on which it is located. This is particularly relevant to 'makegood' provisions in property leases taken up by the Future Fund where there exists an obligation to restore the property to its original condition. These costs are included in the value of the Future Fund's leasehold improvements with a corresponding provision for the 'makegood' taken up.

2.14.2 Impairment of non-financial assets

All non-financial assets were assessed for impairment at 30 June 2010. Where indications of impairment exist, the asset's recoverable amount is estimated and an impairment adjustment made if the asset's recoverable amount is less than its carrying amount.

The recoverable amount of an asset is the higher of its fair value less costs to sell and its value in use. Value in use is the present value of the future cash flows expected to be derived from the asset. Where the future economic benefit of an asset is not primarily dependent on the asset's ability to generate future cash flows, and the asset would be replaced if the Future Fund was deprived of the asset, its value in use is taken to be its depreciated replacement cost.

2.14.3 Depreciation and amortisation

The depreciable value of plant and equipment assets is written off over the estimated useful lives of the assets to the Future Fund using the straight line method of depreciation. Leasehold improvements are amortised on a straight line basis over the lesser of the estimated useful life of the improvements or the unexpired period of the lease.

Depreciation and amortisation rates (useful lives) and methods are reviewed at each balance date and necessary adjustments are recognised in the current, or current and future reporting periods, as appropriate. The depreciable value of infrastructure, plant and equipment assets is based on a zero residual value.

Depreciation and amortisation expenses have been determined by applying rates to new depreciable assets based on the following useful lives:

Class of depreciable asset	2009 & 2010
Leasehold improvements	5 years
Computers, plant and equipment	3-5 years
Office equipment	5 years
Furniture	5 years

The aggregate amount of depreciation and amortisation allocated for each class of asset during the reporting period is disclosed at Note 10.

Note 2: Summary of significant accounting policies (continued)

2.15 Intangibles

Lease rights are stated at cost and are an amortisable intangible asset. These are amortised on a straight line basis over their expected useful life, net of their residual value. There has been no amortisation expense during the current period as the estimated residual value was equal to the carrying value.

Purchases of computer software licenses for periods 12 months or greater are recognised at cost in the statement of financial position except for purchases costing less than \$10,000, which are expensed at the time of acquisition.

Software assets are amortised on a straight line basis over their anticipated useful lives, being three to five years. Software assets are not subject to revaluation and consequently are carried at cost less accumulated amortisation and any accumulated impairments in the financial statements. All software assets are assessed for indications of impairment at each reporting date.

2.16 Taxation

The Future Fund is exempt from all forms of Australian taxation except for Fringe Benefits Tax (FBT) and the Goods and Services Tax (GST).

Revenues, expenses, assets and liabilities are recognised net of GST, except:

- where the amount of GST incurred is not recoverable from the Australian Taxation Office; and
- for receivables and payables (where GST is applicable).

Receipts and payments in the Statement of Cash Flows are recorded in gross terms (that is, at their GST inclusive amounts).

The net amount of GST recoverable from, or payable to, the taxation authority is included as part of receivables or payables.

Foreign taxes are payable on certain classes of income and capital gains. The majority of foreign taxes incurred by the Fund are withheld at source (income net of taxes is received by the Fund) under the withholding regimes of the relevant jurisdiction. These withholding taxes are generally a final tax and no further amounts are payable. To the extent the Fund is entitled to a lower withholding than that deducted at source, the Fund makes a claim to the respective foreign revenue authority for the difference and these amounts are recorded as receivables on the statement of financial position and in the statement of comprehensive income as revenue.

2.17 Foreign currency

(i) Functional and presentation currency

Items included in the consolidated financial statements of the Fund are measured using the currency of the primary economic environment in which the entity operates ('the functional currency'). The financial statements are presented in Australian dollars, which is the Fund's functional and presentation currency.

(ii) Transactions and balances

All foreign currency transactions during the period are brought to account using the exchange rate in effect at the date of the transaction. Foreign currency items at reporting date are translated at the exchange rate existing at reporting date. Exchange differences are recognised in the statement of comprehensive income in the period in which they arise.

Note 2: Summary of significant accounting policies (continued)

2.18 Derivative financial instruments

The Future Fund has entered into forward foreign exchange contracts to manage its exposure to foreign exchange risk and exchange futures contracts to gain indirect exposure to investment markets. The Future Fund also uses interest rate swaps and options to manage its exposure to interest rate risk; equity options to manage its exposure to equity market risk; and credit default swaps to manage its exposure to credit risk and/or gain indirect exposure to credit risk. The use of derivative financial instruments by the Fund is governed by the *Future Fund Act 2006* (as amended). Accounting policy information regarding derivatives is presented in Note 2.4 and further disclosure regarding the use of derivatives by the Fund is presented in Note 20.

The Fund has not designated any derivatives as cash flow or fair value hedges. All derivatives are accounted for at fair value through profit and loss as set out in Note 2.4.

2.19 Investment property

Investment property is held to earn rentals and for capital appreciation, or for both, but not for sale or use in the ordinary course of business. Investment property is measured initially at its cost, including transaction costs, and subsequent to initial recognition is measured at fair value. Gains and losses arising from changes in the fair value of investment property are included in the statement of comprehensive income in the period in which they arise.

Fair value is considered to be the amount for which a property could be exchanged on the date of valuation between a willing buyer and a willing seller in an arm's length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently and without compulsion. Fair value of investment properties includes the cost of amortised lease incentives, amortised direct leasing costs and the impact of straight-lining of rental income in accordance with Australian Accounting Standards.

Rental income is recorded as part of other operating income (Note 2.5) and property expenses are included as part of other portfolio expenses in the statement of comprehensive income.

2.20 Timberland investments and trees in a plantation forest

Trees in a plantation forest are considered biological assets and are stated at fair value less costs to sell, with changes recognised in the statement of comprehensive income.

Timberland investments are considered to be investment property as they are held for appreciation. Timberlands are initially recognised at cost upon acquisition comprising of the purchase price and any directly attributable transaction costs. Subsequent measurement is at fair value with changes recognised in the statement of comprehensive income.

2.21 Change in current period presentation of the statement of cash flows

The Fund has reclassified cash flows arising from the purchase and sale of investments as operating cash flows rather than investing cash flows. This is consistent with the Fund's primary purpose as an investment manager and industry practice. This is also consistent with the enabling legislation which establishes the Fund Account (see Note 1) and requires all income derived from an investment together with any realisation of investments to be credited to the Fund Account.

2.22 Rounding of amounts

Amounts have been rounded to the nearest thousand dollars unless stated otherwise in accordance with the Finance Minister's Orders.

Note 3: Investment income

	2010 \$'000	2009 \$'000
Interest income		
Term deposits	1,192	2,445
Cash at bank	70,082	103,103
Total interest income	71,274	105,548

Income relating to financial assets and financial liabilities classified as at fair value through profit or loss is included in 'Other gains and losses' in Note 4.

Note 4: Other gains and losses

	2010 \$'000	2009 \$'000
Dividend income		
Dividend income – domestic equities and listed managed investment schemes	656,777	821,578
Imputation credits refunded or refundable under Section 30 of the <i>Future Fund Act 2006</i>	253,737	329,905
Dividend income – international equities	356,024	323,047
Total dividend and imputation credit income	1,266,538	1,474,530
Distribution income		
Distributions – collective investment vehicles	121,011	5,122
Total distribution income	121,011	5,122
Net gain/(loss) on financial instruments held at fair value through profit or loss		
Net gain/(loss) on financial assets held at fair value through profit or loss	4,209,623	(4,093,447)
Net gain/(loss) on financial liabilities held at fair value through profit or loss	(124,284)	33,826
Total net gain/(loss) on financial instruments held at fair value through profit or loss	4,085,339	(4,059,621)
Net gain/(loss) arising on foreign currency	1,107,133	(715,126)

Note 5: Other income

	2010 \$'000	2009 \$'000
Other income		
Fee income for services provided (Note 25B)	943	60
Rental income from investment property	2,548	–
Timberlands income	2,644	–
Change in fair value of non-financial assets	2,085	–
Other income	546	–
Resources received free of charge (ANAO)	102	96
Total other income	8,868	156

Note 6: Expenses

	2010 \$'000	2009 \$'000
Agency employees' remuneration		
Wages and salaries	16,597	13,010
Superannuation	1,030	1,018
Leave and other entitlements payable	469	249
Total Agency employees' remuneration	18,096	14,277
Board of Guardians' remuneration		
Wages and salaries	697	681
Superannuation	63	61
Total Board of Guardians' remuneration	760	742
Other expenses	8,461	7,044
Timberlands expenses	3,268	–
Investment property expenses	827	–
Total other expenses	12,556	7,044
Depreciation		
Depreciation of infrastructure, plant and equipment	787	589
Total depreciation	787	589
Amortisation		
Amortisation of intangibles – computer software	68	60
Total amortisation	68	60
Total depreciation and amortisation	855	649

Note 7: Remuneration of Auditors

Financial statement audit services provided to the Future Fund totaled \$102,000 (2009: \$96,000). These services were provided free of charge. The fair value of all audit services provided by the Australian National Audit Office (ANAO) was:

	2010	2009
	\$	\$
Auditing the financial statements	166,600	148,000

No other services were provided by the ANAO.

Other audit fees provided by firms other than the ANAO were incurred by the consolidated group as follows:

	2010	2009
	\$	\$
Auditing the financial statements – subsidiary entities	289,404	7,646

Note 8: Investments

	2010 \$'000	2009 \$'000
Investment Summary		
Financial assets at fair value:		
Interest bearing securities	22,332,975	30,932,591
Listed equities and listed managed investment schemes	28,515,072	22,510,409
Collective investment vehicles	14,198,020	4,690,165
Derivatives	1,207,874	2,159,858
Total financial asset investments	66,253,941	60,293,023
Financial liabilities at fair value:		
Derivatives	(2,072,570)	(818,187)
Total financial liability investments	(2,072,570)	(818,187)

The tables below provide more detailed information of the investments held at balance date.

	2010 \$'000	2009 \$'000
Interest bearing securities		
At fair value:		
Bank bills – domestic	124,492	730,447
Bank bills – international	41,079	61,494
Negotiable certificates of deposit – domestic	5,605,026	15,109,437
Corporate debt securities – domestic	5,263,481	6,723,930
Corporate debt securities – international	3,615,159	2,158,560
Mortgage backed securities – domestic	872,163	1,159,861
Mortgage backed securities – international	2,430,821	2,303,456
Asset backed securities – international	1,259,160	267,388
Corporate credit (bank loans) – domestic	29,031	–
Corporate credit (bank loans) – international*	2,515,589	2,104,449
Government debt securities – international	440,998	256,792
Other interest bearing securities – international	135,976	56,777
Total interest bearing securities	22,332,975	30,932,591

* The Fund has invested in bank loans which draw down over time. At 30 June 2010 the value of unfunded commitments to these investments total \$35.758 million. This amount is included in the consolidated schedule of commitments.

Note 8: Investments (continued)

	2010 \$'000	2009 \$'000
Listed equities and listed managed investment schemes		
At fair value:		
Domestic listed equities and listed managed investment schemes	11,683,155	11,975,171
International listed equities and listed managed investment schemes	16,831,917	10,535,238
Total listed equities and listed managed investment schemes	28,515,072	22,510,409
Collective investment vehicles		
At fair value:		
Unlisted investments	13,582,898	4,452,546
Unlisted shares	615,122	237,619
Total collective investment vehicles	14,198,020	4,690,165
Derivatives		
At fair value: – financial assets		
Currency contracts	1,066,102	2,139,446
Interest rate swap agreements	11,949	6,205
Interest rate options	341	–
Equity options	64,557	–
Credit default swaps	59,632	14,207
Currency swaps	5,293	–
Total derivative financial assets	1,207,874	2,159,858
At fair value: – financial liabilities		
Currency contracts	(1,827,832)	(753,222)
Interest rate swap agreements	(195,025)	(27,649)
Interest rate options	(2,013)	(2)
Credit default swaps	(32,028)	(37,314)
Currency swaps	(15,672)	–
Total derivative financial liabilities	(2,072,570)	(818,187)
Total derivatives	(864,696)	1,341,671

Note 8: Investments (continued)

Restrictions on investments

Telstra

Included within the listed domestic equities sub-class above are Telstra shares transferred to the Fund by the Commonwealth Government under Part 3 of Schedule 1 of the *Future Fund Act 2006* (as amended). The fair value of these shares as at 30 June 2010 is \$4,391,949,110 (30 June 2009: \$6,880,794,595).

On 21st August 2009 the Board sold 684,369,089 shares at a price of \$3.47. Under the terms of the sale agreement the Board was restricted from selling any further Telstra holdings for a period of six months after the sale.

Cash provided as collateral and cash held in escrow

The Fund has entered into various derivative contracts which require the Fund to post collateral with counterparties under certain circumstances. The Fund provides cash as collateral when legally required. Any cash provided as collateral remains a financial asset of the Fund, however any alternate use of this cash is restricted as it is held by the counterparty. As at 30 June 2010, the Fund has nil cash which has been posted as collateral with counterparties.

The Fund has posted cash with a futures broker to cover exchange traded futures positions as required under clearing house rules. As at 30 June 2010, the Fund had posted \$208,010,071 in futures margins to cover open positions. This cash also remains a financial asset of the Fund, however any alternate use of this cash is also restricted.

The Fund has provided cash to an escrow agent for the purpose of meeting specified future investment obligations. This cash cannot be released without the explicit approval of the Fund and is included within 'collective investment vehicles' financial asset class in the Fund's consolidated statement of financial position. As at 30 June 2010, the Fund had cash of USD \$439,089,521 held in escrow.

Note 8: Investments (continued)

Collective investment vehicles

30 June 2010

As at 30 June 2010, the Fund and its subsidiaries had made commitments to a number of collective investment vehicles. Capital commitments (local currency), capital amounts called and paid (Australian dollars), the outstanding commitment (Australian dollars) and the fair value (Australian dollars) of the investments as at 30 June 2010 are shown in the table below.

Description of underlying strategy	Capital committed as at 30 June 2010 Local Currency	Outstanding commitment as at 30 June 2010	Capital called and paid as at 30 June 2010	Fair value as at 30 June 2010
		AUD equivalent \$'000	AUD equivalent \$'000	AUD equivalent \$'000
Private equity venture capital	USD \$1,764,000,000	1,842,947	244,459	228,333
Private equity buyout	EUR €655,000,000	704,531	282,674	236,067
Private equity buyout	USD \$400,000,000	473,569	–	–
Private equity distressed	EUR €300,000,000	195,775	287,414	305,408
Private equity distressed	USD \$360,000,000	318,401	120,870	118,048
Private equity secondaries	USD \$1,200,000,000	1,204,641	218,752	270,636
Private equity other	EUR €187,934,719	–	359,577	276,861
Private debt	EUR €330,000,000	478,562	–	–
Global Property	USD \$700,000,000	195,413	639,329	688,098
Global Property	EUR €180,000,000	156,423	122,916	80,549
Global Property	AUD \$390,387,500	–	390,387	390,387
Global Property	GBP £211,529,685	–	401,185	468,061
Global Infrastructure	GBP £ 327,976,232	–	649,938	593,906
Global Infrastructure	USD \$800,000,000	366,393	678,404	523,739
Alternative strategies	USD \$4,269,657,000	420,292	4,862,358	5,452,507
Private equity distressed – consolidated by parent	USD \$1,000,000,000	867,223	394,532	112,187
Private debt – consolidated by parent	USD \$500,000,000	574,202	16,677	–*
Global Property income – consolidated by parent	AUD \$108,300,00	–	108,300	–*
Global Infrastructure – consolidated by parent	AUD \$543,327,294	–	543,327	615,122*
Alternative strategies – consolidated by parent	USD \$3,740,000,000	230,865	4,001,029	3,838,111*
Timberland – consolidated by parent	USD \$125,000,000	–	137,988	–*
Total		8,029,237	14,460,116	14,198,020

* On consolidation of these entities, the investment in the collective vehicle is eliminated and the assets and liabilities of these vehicles are disclosed on the statement of financial position and in the notes. The information relating to the underlying commitments to these vehicles is presented in the above table for completeness.

Note 8: Investments (continued)

As noted in Note 20F, in determining the fair value of the net assets of unlisted unlisted managed investment schemes and collective investment vehicles, reference is made to the underlying unit price provided by the Manager (where available), associated Manager valuation reports and the most recent audited financial statements of the scheme.

Manager valuation reports are reviewed to ensure the underlying valuation principles are materially compliant with Australian Accounting Standards and applicable industry standards including International Private Equity and Venture Capital Valuation Guidelines as endorsed by the Australian Private Equity and Venture Capital Association Limited (AVCAL).

Collective investment vehicles

30 June 2009

As at 30 June 2009, the Fund and its subsidiaries had made commitments to a number of collective investment vehicles. Capital commitments (local currency), amounts called and paid (Australian dollars), the outstanding commitment (Australian dollars) and the fair value (Australian dollars) of the investments as at 30 June 2009 are shown in the table below.

Description of underlying strategy	Capital committed as at 30 June 2009 Local Currency	Outstanding commitment as at 30 June 2009 AUD equivalent \$'000	Capital called and paid as at 30 June 2009 AUD equivalent \$'000	Fair value as at 30 June 2009 AUD equivalent \$'000
Private equity venture capital	USD \$1,264,000,000	1,510,500	53,050	35,933
Private equity buyout	EUR €655,000,000	967,742	168,675	142,005
Private equity buyout	USD \$400,000,000	494,774	–	–
Private equity distressed	EUR €300,000,000	280,599	239,897	226,540
Private equity distressed	USD \$358,025,258	354,484	100,225	79,243
Private equity secondaries	USD \$1,200,000,000	1,389,207	95,179	94,003
Private equity other	EUR €181,084,341	–	349,715	257,578
Global Property	USD \$100,000,000	66,078	57,616	14,155
Global Property	EUR €180,000,000	241,612	70,685	41,624
Global Infrastructure	AUD \$226,001,000	–	226,001	237,619
Global Infrastructure	GBP £172,606,186	–	374,192	350,532
Global Infrastructure	USD \$800,000,000	337,645	651,903	542,500
Alternative strategies	USD \$2,587,591,000	716,312	2,645,054	2,560,925
Private equity distressed – consolidated by parent	USD \$1,000,000,000	857,775	379,160	107,508*
Alternative strategies – consolidated by parent	USD \$250,000,000	201,515	107,718	–*
Total		7,418,243	5,519,070	4,690,165

* On consolidation of these entities, the investment in the collective vehicle is eliminated and the assets and liabilities of these vehicles are disclosed on the statement of financial position and in the notes. The information relating to the underlying commitments to these vehicles is presented in the above table for completeness.

Note 8: Investments (continued)

Collective investment vehicles (continued)

Commitments made to collective investment vehicles as at 30 June 2010

As disclosed in the Schedule of Commitments and in the tables above, the Fund has committed to provide capital to various collective investment vehicles. The total of these commitments at balance date is \$8,029 million (2009: \$7,418 million). The Fund's commitment obligations, being capital calls, are set out in the various underlying subscription documents. Whilst the actual timing of the capital calls to be made by the managers of these vehicles is uncertain, as it is dependent on the managers sourcing suitable investment opportunities, the Fund has recorded the commitments as being current in accordance with the underlying legal documents (see the consolidated schedule of commitments). The Fund has appropriate liquidity planning in place to ensure a suitable allocation of resources will be available to cover these future commitments of capital.

Note 9: Receivables

	2010 \$'000	2009 \$'000
Receivables		
Imputation credits refundable	324,948	339,888
Interest receivable	7,439	1,667
Dividends & distributions receivable	112,960	59,423
Unsettled sales	617,658	188,575
Other receivables	114	–
Total Receivables	1,063,119	589,553

No amounts presented in the table above are considered to be past due or impaired.

Note 10: Non-financial assets

(See note 2.4)

	2010 \$'000	2009 \$'000
Investment property – at fair value	108,002	–
Timberland investment property – at fair value	50,337	–
<i>Total investment property</i>	158,339	–
Trees in a plantation forest	85,618	–
<i>Total trees in a plantation forest</i>	85,618	–
Plant and equipment		
Computers, plant and equipment – at cost	4,781	2,748
Accumulated depreciation	(2,250)	(1,463)
<i>Total plant and equipment</i>	2,531	1,285
Intangibles		
Lease rights	11,010	–
<i>Total intangibles – lease rights</i>	11,010	–
Intangibles – software licences		
Computer software purchased – cost	386	252
Accumulated amortisation	(175)	(107)
<i>Total intangibles – software licences</i>	211	145
<i>Total intangibles</i>	11,221	145

Note 10: Non-financial assets (continued)

	Year Ending 30 June 2010		
	Plant & equipment \$'000	Computer software \$'000	Total \$'000
Analysis of Plant and equipment, and Intangibles – software licenses			
Opening balance as at 1 July 2009			
Gross book value	2,748	252	3,000
Accumulated depreciation/amortisation	(1,463)	(107)	(1,570)
Net book value as 1 July 2009	1,285	145	1,430
<i>Additions:</i>			
by purchase	2,047	140	2,187
<i>Disposals:</i>			
Gross value of disposals	(42)	(16)	(58)
Accumulated depreciation/amortisation	28	10	38
<i>Depreciation/amortisation charge for the period</i>	(787)	(68)	(855)
Net book value as of 30 June 2010	2,531	211	2,742
Represented by:			
Gross book value	4,781	386	5,167
Accumulated depreciation/amortisation	(2,250)	(175)	(2,425)
	2,531	211	2,742

	Year Ending 30 June 2009		
	Plant & equipment \$'000	Computer software \$'000	Total \$'000
Analysis of Plant and equipment, and Intangibles – software licenses			
Opening balance as at 1 July 2008			
Gross book value	2,429	178	2,607
Accumulated depreciation/amortisation	(874)	(47)	(921)
Net book value as 1 July 2008	1,555	131	1,686
<i>Additions:</i>			
by purchase	319	74	393
<i>Disposals:</i>			
Gross value of disposals	–	–	–
Accumulated depreciation/amortisation	–	–	–
<i>Depreciation/amortisation charge for the period</i>	(589)	(60)	(649)
Net book value as of 30 June 2009	1,285	145	1,430
Represented by:			
Gross book value	2,748	252	3,000
Accumulated depreciation/amortisation	(1,463)	(107)	(1,570)
	1,285	145	1,430

Note 11: Investment property

	2010 \$'000	2009 \$'000
Fair value of investment property	108,002	–
	2010 \$'000	2009 \$'000
At fair value		
Balance at beginning of year	–	–
Acquisitions	107,898	–
Capital expenditure on investment properties	104	–
Straight-lining of rental income	63	–
Fair value adjustments on investment properties	(63)	–
Balance at end of year	108,002	–

The fair value of the Fund's investment property at 30 June 2010 has been arrived at on the basis of a valuation carried out on 1 March 2010 at \$102.0 million plus acquisition costs of \$6 million. The property was valued by Savills (VIC) Pty Limited who are independent valuers not related to the Fund.

Note 11A: Timberland investment property and trees in a plantation forest

	2010 \$'000	2009 \$'000
Fair value of trees in a plantation forest	85,618	–
Fair value of timberland investment property	50,337	–
	135,955	–

	Timberland investment property		Trees in a plantation forest	
	2010 \$'000	2009 \$'000	2010 \$'000	2009 \$'000
Balance at beginning of year	–	–	–	–
Acquisitions	48,067	–	81,470	–
Capital expenditure on timberland investment properties	–	–	–	–
Capital expenditure	–	–	31	–
Depletion of plantation forest trees	–	–	(2,096)	–
Net foreign currency gain	2,270	–	4,128	–
Fair value adjustments	–	–	2,085	–
Balance at end of year	50,337	–	85,618	–

Note 11: Investment property (continued)

Note 11A: Timberland investment property and trees in a plantation forest (continued)

The estimated fair value of the plantation forest trees and timberlands (collectively, timber investment) is based on either independent valuations prepared by independent real estate appraisers (members of the American Institute of Real Estate Appraisers), which have been prepared in accordance with Uniform Standards of Professional Appraisal Practice, or internal valuations prepared by the investment manager. Independent valuations are performed on each timber investment every three years. Manager valuations are performed annually. Estimated fair value of timber investment is based upon internal valuations as of 30 June, 2010 as the investments were acquired in a market based arms-length transaction during March 2010.

For timberland, the fair value estimate used in internal valuations is based on recent market prices at which similar properties were sold in at arm's length transactions.

For plantation trees, internal valuations are developed based on an income approach using a discounted cash flow model. Future cash flows are developed using recently prepared forecasts and business plans to estimate the future economic benefit that the timber investment will generate. Key assumptions used in the discounted cash flow model include changes in future prices of wood products, the age of available timber to be harvested, long-term growth rates, the discount rate, and operational costs such as harvesting and forest management costs. A long-term growth rate is applied to revenue and cost generated by the sale of the timber using an estimate of expected inflation rate.

The determination of fair value of timber investment involves subjective assumptions and estimates that are subject to significant uncertainty.

Timber values are adjusted for capital additions made to the property subsequent to the latest fair value measurement date. All expenditures associated with initial site preparation and planting are capitalised at cost, which approximates fair value.

Generally, costs incurred subsequent to two years after planting, such as fertilisation, vegetation, insect control, and pre commercial thinning, are considered to be maintenance and are expensed as incurred.

The Fund estimates its timber inventory using statistical information and data obtained from physical measurements, site maps, photo-types, and other information-gathering techniques. These estimates are updated annually and may result in adjustments of timber volumes, including timber growth rates and depletion rates.

Depletion is the cost of standing timber and is recorded as an expense as timber is harvested or sold. The depletion rate applied to the volume of timber sold is adjusted annually and is based on the relationship of incurred costs in the merchantable timber classification to estimated current merchantable volume. The estimated cost basis of timber harvested during the period from 23 March, 2010 (inception) through 30 June, 2010 was \$2,096,000 and this amount forms part of the timberlands expenses total as disclosed in Note 6.

Note 12: Payables

	2010 \$'000	2009 \$'000
Payables		
Unsettled purchases*	1,073,304	922,660
Other unsecured payables and accrued expenses	165,075	49,647
Total Payables	1,238,379	972,307

* Represents amounts owing under normal market settlement terms for the purchase of investment securities

Note 13: Provisions

	2010 \$'000	2009 \$'000
Employee provisions		
Annual leave	596	424
Long service leave	645	347
Other employee liabilities	5,654	4,212
Total Employee provisions	6,895	4,983
Other provisions		
Lease incentive	274	268
Prepaid income	1,165	–
Total Other provisions	1,439	268

Note 14: Contributions by Government

	2010 \$'000	2009 \$'000
Opening balance	60,536,831	60,396,090
Contribution from Government – cash	–	–
Contribution from Government – financial assets	–	140,741
Closing balance	60,536,831	60,536,831

Financial asset contributions represent Telstra shares transferred at the closing market price on the respective transfer dates from other wholly owned Australian Government entities. The transfer was non-reciprocal. The Future Fund has designated the transferred shares as being prospectively accounted for at designated fair value through profit and loss. Contributions are made under Schedule 1 to the *Future Fund Act 2006* (as amended).

Note 15: Subsidiaries

The consolidated financial statements incorporate the assets, liabilities and results of the following subsidiaries in accordance with the accounting policy described in Note 2.3.

Name of entity	Country of incorporation/ domicile	Class of shares	Equity holding	
			2010 %	2009 %
Future Fund Investment Company No.1 Pty Ltd[^]	Australia	Ordinary	100	100
– Secondary Overflow Cayman Fund, L.P.*	Cayman Islands	Ordinary	100	100
Future Fund Investment Company No.2 Pty Ltd[^]	Australia	Ordinary	100	100
– Sankaty Middle Market Opportunities Fund (Offshore II), Ltd*	Cayman Islands	Ordinary	100	–
– Sankaty Middle Market Opportunities Fund (Offshore Master II), L.P.*	Cayman Islands	Ordinary	100	–
– Global Hedged Strategies Fund L.P.	Canada	Ordinary	100	–
– Horsley Bridge Strategic Fund, L.P.*	United States	Ordinary	100	–
– Stud Park Shopping Centre Trust	Australia	Ordinary	100	–
– Hayfin Opal Holdings Limited	Cayman Islands	Ordinary	100	–
– Hayfin Opal Luxco 1 SARL	Luxembourg	Ordinary	100	–
– Hayfin Opal Luxco 2 SARL	Luxembourg	Ordinary	100	–
– Hayfin Opal Luxco 3 SARL	Luxembourg	Ordinary	100	–
Future Fund Investment Company No.3 Pty Ltd[^]	Australia	Ordinary	100	100
Future Fund Investment Company No.4 Pty Ltd[^]	Australia	Ordinary	100	100
– ASP Offshore Company Limited – Global Opportunities Secondary Fund II-A*	Cayman Islands	Ordinary	100	100
– Adams Street Global Opportunities Secondary Fund II-A, LP*	United States	Ordinary	100	100
– ASP Offshore Company Limited – 2009 Non-US Emerging Markets Fund-A*	Cayman Islands	Ordinary	100	100
– Adams Street Partnership Fund – 2009 Non-US Emerging Markets Fund-A, LP*	United States	Ordinary	100	100
– Greenspring GE (Offshore), L.P.*	Cayman Islands	Ordinary	100	100
– Greenspring Growth Equity, L.P.*	United States	Ordinary	100	100
– Oaktree FF Investment Fund, L.P.*	Cayman Islands	Ordinary	100	100
Future Fund Investment Company No.5 Pty Ltd[^]	Australia	Ordinary	100	100
Future Fund Investment Trust No.1	Australia	Ordinary	100	100
Future Fund Investment Trust No.2	Jersey	Ordinary	100	–
– Future Fund Investment Trust No.3	Jersey	Ordinary	100	–
– Future Fund Bull Ring (LP) Limited	England	Ordinary	100	–
Madison Timber, Inc.	United States	Ordinary	100	–
Madison Timber REIT, Inc.	United States	Ordinary	100	–

[^] Audited by the Australian National Audit Office

Note 15: Subsidiaries (continued)

* The financial statements of these subsidiaries which were used to prepare the consolidated financial statements are for a reporting period which is different from that of the parent. These subsidiary entities have the purpose of being investment holding entities and their assets and liabilities consist of investments which are consistent in nature to those which the Fund makes directly. On consolidation, these investments are, like the Fund's direct assets, designated at fair value through profit and loss and accounted for on the same basis as if the Fund had invested directly and not via the subsidiary. The Fund is able to obtain the information it requires to undertake the consolidation, notwithstanding the different reporting dates.

The Fund seeks to maximise after tax returns and, where it is legitimate to use a structure which protects the claim to sovereign immunity, this path has been taken. This includes the use of subsidiary holding vehicles. Importantly, the Fund does not invest in schemes and arrangements that use secrecy laws to conceal assets and income that are subject to tax or which create or promote false or fraudulent tax deductions. All investment opportunities are diligently evaluated to ensure they generate an adequate pre-tax return to the Fund. The Fund would not invest in a structure which has the dominant purpose of generating tax benefits. Full transparency and information exchange for tax purposes and compliance with all relevant laws will be ensured and the Fund adopts the OECD principles of transparency and information exchange for tax purposes as the required standard of disclosure.

Note 16: Cash flow reconciliation

	2010 \$'000	2009 \$'000
(a) Reconciliation of operating result to net cash from operating activities:		
Operating result	6,320,474	(3,318,877)
Non cash items included in the statement of comprehensive income	584	–
Depletion of trees in a plantation forest	2,096	–
Increase in fair value of trees in a plantation forest	(2,085)	–
Depreciation and amortisation	874	649
Purchase of investments	(89,318,410)	(128,618,343)
Proceeds from sale of investments	86,187,107	128,895,561
Net (gain)/loss on revaluation of investments	(4,055,649)	3,830,587
Net (gain)/loss on foreign currency	2,094,480	(1,317,514)
(Increase) / decrease in accrued income	(43,937)	193,938
(Increase) / decrease in other assets	(117)	(292)
Increase / (decrease) in employee provisions	1,911	1,856
Increase / (decrease) in other payables	115,604	43,600
Increase / (decrease) in other provisions	346	(124)
Net cash from operating activities	1,303,278	(288,959)

(b) Reconciliation of cash and cash equivalents

For the purposes of the cash flow statement, cash includes cash on hand and in banks net of any outstanding operating overdrafts. Cash at the end of the financial year is reconciled to the statement of financial position as follows:

	2010 \$'000	2009 \$'000
Cash and cash equivalents	3,024,421	1,869,674

Note 17: Contingent liabilities and assets

Contingencies

The Future Fund is not aware of any quantifiable or unquantifiable contingency as of the signing date that requires disclosure in the financial statements.

Remote contingencies

The Future Fund is not aware as at the signing date of any remote contingencies.

Note 18: Senior executive remuneration

Note 18A: Senior executive remuneration

The number of senior executives who received or were due to receive total remuneration of \$145,000 or more was as per the table below. The *Finance Minister's Orders 2009-2010* require the disclosure of actual and annualised remuneration in separate tables. All individuals listed in the table below worked for the full years ending 30 June 2010 and 30 June 2009, therefore the information is presented once only. Senior executives performing controlling functions directly impacting the outcomes of the Future Fund are included in the disclosure below.

Remuneration means any money, consideration or benefit including wages, salaries, performance pay, accrued leave entitlements, superannuation contributions, the cost of motor vehicles, commuting and allowances. Remuneration does not include reimbursement of out-of-pocket expenses incurred for work related purposes.

	2010	2009
The number of senior executives who received or were due to receive total remuneration of \$145,000 or more:		
\$145,000 to \$159,999	–	–
\$175,000 to \$189,999	1	1
\$340,000 to \$354,999	1	1
\$385,000 to \$399,999	–	1
\$400,000 to \$414,999	1	–
\$490,000 to \$504,999	–	1
\$505,000 to \$519,999	1	–
\$565,000 to \$579,999	–	1
\$580,000 to \$594,999	1	–
\$670,000 to \$684,999	1	1
\$685,000 to \$699,999	–	1
\$730,000 to \$744,999	2	1
\$775,000 to \$789,999	–	1
\$790,000 to \$804,999	–	1
\$895,000 to \$909,999	1	–
\$925,000 to \$939,999	1	–
Total	10	10
	\$'000	\$'000
The aggregate amount of total remuneration of executives shown above	6,022	5,691
The aggregate amount of separation and redundancy/termination benefit payments during the year to executives shown above	–	–

Note 18: Senior executive remuneration (continued)

Note 18A: Senior executive remuneration (continued)

Total expense recognised in relation to senior executive employment

	2010 \$	2009 \$
Short-term employee benefits:		
Salary (including payment for leave taken)	3,634,450	3,401,619
Movement in annual leave provisions	39,520	(10,711)
Superannuation	244,993	376,415
Performance-related payments	1,938,158	1,868,705
Total short-term employee benefits	5,857,121	5,636,028
Movement in long service provisions	164,582	55,059
Total	6,021,703	5,691,087

Note 18: Senior executive remuneration (continued)

Note 18B: Salary packages of senior executives

Average actual and annualised remuneration packages for substantive Senior Executives are presented below. No post-employment benefits, other long-term employee benefits, termination benefits or share-based payments were made to any executive during the current or prior period.

	30 June 2010			30 June 2009		
	No. of Senior Executives	Base Salary (including annual leave taken) \$	Total Remuneration Package \$	No. of Senior Executives	Base Salary (including annual leave taken) \$	Total Remuneration Package \$
Range of remuneration disclosed in 18A:						
\$175,000 to \$189,999	1	174,270	189,877	1	171,088	186,352
\$265,000 to \$279,999	1	257,743	272,243	1	245,205	268,623
\$295,000 to \$309,999	2	277,648	302,494	2	266,592	298,870
\$385,000 to \$399,999	–	–	–	2	372,926	396,038
\$400,000 to \$414,999	1	388,128	403,323	–	–	–
\$415,000 to \$429,999	1	398,494	423,494	1	368,312	418,312
\$445,000 to \$459,999	1	428,738	453,738	–	–	–
\$490,000 to \$504,999	2	478,728	503,728	2	444,505	498,407
\$505,000 to \$519,999	–	–	–	1	448,968	518,117
\$520,000 to \$534,999	1	474,326	524,326	–	–	–
Total	10			10		

The total remuneration packages disclosed above do not include performance-related payments. Senior executives, per their contracts, are eligible for performance-related payments.

Note 19: Average staffing level

	2010	2009
The average staffing level for the Agency during the period was:	65	48

Note 20: Financial instruments and financial risk management

Note 20A: Risk management framework

The Board of Guardians is collectively responsible for the investment decisions of the Fund and is accountable to the Government for the performance of the Fund. The Board's primary role is to set the strategic direction of the investment activities of the Future Fund consistent with its approved Investment Mandate. This is accomplished through setting the return targets, risk appetite and risk tolerance levels to manage investment risk. The Agency has the task and responsibility of providing considered research and accurate information and reporting to the Board to assist them in undertaking this role. The Agency monitors daily and reports to the Board monthly, compliance with the approved investment guidelines and with the approved strategic asset allocation.

Note 20B: Financial risk management objectives

The Investment Mandate set by the Government requires the Board to maximise returns above a benchmark rate whilst taking acceptable but not excessive risk. The Board sets, and reviews as deemed necessary, an asset allocation designed to achieve this outcome. It encapsulates a level of risk that is expected to deliver the key return objectives while limiting the downside risk. Particular attention is paid to the worst 5% of possible outcomes under portfolio modelling over a three year period (the 'Conditional Value at Risk' or 'CVaR' of the Fund) to ensure that medium-term risk in the portfolio is deemed acceptable whilst pursuing long-term returns.

The portfolio construction process involves considering a range of factors and ensuring that there is adequate diversity so that a negative outcome in any one area does not unduly impact the overall Fund return. The factors considered include the outlook for: global economic growth; inflation; global real interest rates; changes in risk premia attached to various asset classes; movements in the value of currencies held; and changes in liquidity and credit conditions.

Note 20C: Market risk

Market risk is the risk of loss arising from movements in the prices of various assets flowing from changes in interest rates, exchange rates, equity prices and other prices and derivatives contracts tied to these asset prices.

Note 20: Financial instruments and financial risk management (continued)

Note 20C (i): Interest rate risk

Interest rate exposure tables

The Future Fund's exposure to interest rates as at 30 June 2010 is set out below.

Financial asset	Note	Floating Interest Rate	Fixed Interest Rate	Non-Interest Bearing	Total
		2010 \$'000	2010 \$'000	2010 \$'000	2010 \$'000
Cash and cash equivalents		3,024,421	–	–	3,024,421
Bank bills		–	165,571	–	165,571
Negotiable certificates of deposit		–	5,605,026	–	5,605,026
Corporate debt securities		5,873,751	3,004,889	–	8,878,640
Mortgage backed securities		2,779,718	523,266	–	3,302,984
Asset backed securities		1,204,087	55,073	–	1,259,160
Corporate credit (bank loans)		1,895,560	649,060	–	2,544,620
Government debt securities		34,061	406,937	–	440,998
Other interest bearing securities		123,653	12,323	–	135,976
Other financial assets		–	–	44,986,214	44,986,214
Total financial assets		14,935,251	10,422,145	44,986,214	70,343,610
Derivatives (notional amount) – pay		(1,870,855)	(1,960,500)		(3,831,355)
Derivatives (notional amount) – receive		3,460,500	592,700		4,053,200

As at the reporting date the Future Fund's debt portfolio had an effective interest rate duration of 2.36 (2009: 0.73).

Note 20: Financial instruments and financial risk management (continued)

Note 20C (i): Interest rate risk (continued)

The Future Fund's exposure to interest rates as at 30 June 2009 is set out below.

Financial asset	Note	Floating Interest Rate	Fixed Interest Rate	Non-interest Bearing	Total
		2009	2009	2009	2009
		\$'000	\$'000	\$'000	\$'000
Cash and cash equivalents		1,869,674	–	–	1,869,674
Term deposits		–	3,200	–	3,200
Bank bills		–	791,941	–	791,941
Negotiable certificates of deposit		–	15,109,437	–	15,109,437
Corporate debt securities		7,710,528	1,171,962	–	8,882,490
Mortgage backed securities		2,878,087	585,230	–	3,463,317
Asset backed securities		251,442	15,946	–	267,388
Corporate credit (bank loans)		1,662,599	441,850	–	2,104,449
Government debt securities		151,177	105,615	–	256,792
Other interest bearing securities		56,777	–	–	56,777
Other financial assets		–	–	29,950,412	29,950,412
Total financial assets		14,580,284	18,225,181	29,950,412	62,755,877
Derivatives (notional amount) – pay		(149,800)	(879,200)		(1,029,000)
Derivatives (notional amount) – receive		879,200	149,800		1,029,000

As at the reporting date the Future Fund's debt portfolio had an effective interest rate duration of 0.73 (2008: 0.12).

Note 20: Financial instruments and financial risk management (continued)

Note 20C(i): Interest rate risk (continued)

Interest rate sensitivity analysis

The following table demonstrates the impact on the operating result of the consolidated entity for a 150 basis point (2009: 75 basis point) change in bond yields with all other variables held constant. It is assumed that the basis point change occurs as at the reporting date (30 June 2009 and 30 June 2010) and there are concurrent movements in interest rates and parallel shifts in the yield curves. A 150 basis point (2009: 75 basis point) movement would result in the following impact on the debt portfolios' (including derivatives) contribution to the Fund's consolidated operating result. The impact on the operating result includes the increase/(decrease) in interest income on floating rate securities from the basis point change.

	30 June 2010 Impact on operating result \$'000
+ 150 basis points	(534,097)
- 150 basis points	642,482
	30 June 2009 Impact on operating result \$'000
+ 75 basis points	(427,053)
- 75 basis points	447,661

Note 20: Financial instruments and financial risk management (continued)

Note 20C (i): Interest rate risk (continued)

Interest rate derivative contracts

The Fund had open positions in exchange traded interest rate futures contracts, interest rate swap agreements and interest rate option agreements as at 30 June 2010. The *Future Fund Act 2006* (as amended) governs the use of financial derivatives.

Interest rate derivatives are used by the Fund's investment managers to manage the exposure to interest rates and to ensure it remains within approved limits. The Fund's counterparties for interest rate swaps and options include major banking firms and their affiliates. The Fund diversifies its exposure by utilising multiple counterparties, by considering each counterparty's credit rating, and by executing such contracts pursuant to master netting agreements. All transactions are undertaken using ISDAs approved by the Fund. The notional value of the open positions and their fair value are set out below:

	Notional Value 2010 \$'000	Fair Market Value 2010 \$'000	Notional Value 2009 \$'000	Fair Market Value 2009 \$'000
Buy domestic interest rate futures contracts	4,014,911	80,242	2,346,034	14,446
Sell domestic interest rate futures contracts	–	–	–	–
Buy international interest rate futures contracts	1,246,187	11,067	2,249,365	(11,487)
Sell international interest rate futures contracts	(218,233)	(5,887)	(3,547)	133
Receiver (fixed) interest rate swap agreements	592,700	11,949	149,800	1,893
Payer (fixed) interest rate swap agreements	1,960,500	(195,025)	879,200	(23,337)
Over the counter interest rate options	(179,700)	(1,672)	250	(2)
Total	7,416,365	(99,326)	5,621,102	(18,354)

Interest rate futures contract open positions are cash margined daily with the relevant futures clearing exchange. Whilst the above fair market value represents the value of the open contracts at reporting date, these positions have been cash settled via postings to or from the associated margin account with the resulting gain or loss recorded in the income statement.

Note 20: Financial instruments and financial risk management (continued)

Note 20C(ii): Foreign currency risk management

The Fund undertakes certain transactions denominated in foreign currencies and accordingly is exposed to the effects of exchange rate fluctuations. The Board sets a target exposure to foreign currency risk and this is managed utilising forward foreign exchange contracts.

The Fund's exposure in Australian equivalents to foreign currency risk at the reporting date was as follows:

30 June 2010	USD \$'000	EUR \$'000	GBP \$'000	JPY \$'000	Other ¹ \$'000	Total \$'000
Cash & cash equivalents	1,552,289	229,964	79,323	30,909	27,061	1,919,546
Listed equities and listed managed investment schemes	8,047,474	1,978,541	1,410,242	1,311,731	4,083,930	16,831,918
Interest bearing securities	9,567,385	913,811	306,868	–	62,927	10,850,991
Collective investment vehicles	11,231,661	898,885	1,061,967	–	–	13,192,513
Other investments	27,997	11,826	939	–	3,280	44,042
Receivables	544,116	24,759	21,488	15,457	25,142	630,962
Payables	(747,992)	(20,957)	(5,927)	(5,200)	(41,640)	(821,716)
Total physical exposure	30,222,930	4,036,829	2,874,900	1,352,897	4,160,700	42,648,256
Forward exchange contracts						
– buy foreign currency	4,218,881	747,419	169,614	2,024,115	2,868,484	10,028,513
– sell foreign currency	(32,778,061)	(5,105,973)	(1,902,724)	(1,242,467)	(2,576,255)	(43,605,480)
Total derivative exposure	(28,559,180)	(4,358,554)	(1,733,110)	781,648	292,229	(33,576,967)
Total net exposure	1,663,750	(321,725)	1,141,790	2,134,545	4,452,929	9,071,289

(1) Other includes AUD equivalent exposures to other currencies which are immaterial on an individual basis.

Note 20: Financial instruments and financial risk management (continued)

Note 20C(ii): Foreign currency risk management (continued)

The Fund's exposure in Australian equivalents to foreign currency risk at 30 June 2009 was as follows:

30 June 2009	USD \$'000	EUR \$'000	GBP \$'000	JPY \$'000	Other ¹ \$'000	Total \$'000
Cash & cash equivalents	1,043,642	38,892	31,766	22,158	25,515	1,161,973
Listed equities and listed managed investment schemes	4,401,323	1,483,649	1,016,588	938,861	2,761,724	10,602,145
Interest bearing securities	6,799,315	804,351	142,066	–	1,301	7,747,033
Collective investment vehicles	3,434,267	667,746	135,906	–	–	4,237,919
Other investments	(37,949)	3,996	–	–	(1,845)	(35,798)
Receivables	207,427	10,102	9,871	1,933	24,205	253,538
Payables	(849,271)	(43,471)	(11,940)	(8,208)	(18,528)	(931,418)
Total physical exposure	14,998,754	2,965,265	1,324,257	954,744	2,792,372	23,035,392
Forward exchange contracts						
– buy foreign currency	3,990,415	1,907,840	972,405	1,710,501	1,017,332	9,598,493
– sell foreign currency	(17,656,226)	(4,204,630)	(1,229,887)	(144,994)	(741,582)	(23,977,319)
Total derivative exposure	(13,665,811)	(2,296,790)	(257,482)	1,565,507	275,750	(14,378,826)
Total net exposure	1,332,943	668,475	1,066,775	2,520,251	3,068,122	8,656,566

(1) Other includes AUD equivalent exposures to other currencies which are immaterial on an individual basis.

Note 20: Financial instruments and financial risk management (continued)

Note 20C(ii): Foreign currency risk management (continued)

Foreign currency sensitivity analysis

The following table demonstrates the impact on the consolidated entity's operating result of a 14% (2009: 12%) movement of the value of the Australian dollar relative to the basket of actual net exposures as at 30 June 2010, with all other variables held constant. It is assumed that the relevant change occurs as at the reporting date and the results presented are shown after taking into account the implementation of the Board's foreign currency exposure policy (that is, the sensitivity is calculated on the net exposure presented in the tables on the two previous pages).

	30 June 2010
	Impact on operating result
	\$'000
+ 14% movement	1,579,290
- 14% movement	(1,579,290)
	30 June 2009
	Impact on operating result
	\$'000
+ 12% movement	1,186,358
- 12% movement	(1,186,358)

Note 20: Financial instruments and financial risk management (continued)

Note 20C(iii): Public markets equity price risk

The Future Fund is exposed to equity price risks arising from public market equity investments. The equity price risk is the risk that the value of our equity portfolio will decrease as a result of changes in the levels of equity indices and the price of individual stocks. The Future Fund holds all of its equities at fair value through profit or loss.

The Fund's exposure to equity price risk at the reporting date was as follows:

	30 June 2010	30 June 2009
	\$'000	\$'000
Domestic listed equities and listed managed investment schemes	11,683,155	11,975,171
International listed equities and listed managed investment schemes	16,831,917	10,535,238
Total equity price risk exposure	28,515,072	22,510,409

Equity derivative contracts

The Fund had open positions in exchange traded equity futures contracts and equity option contracts as at 30 June 2010. The *Future Fund Act 2006* (as amended) governs the use of financial derivatives. Exchange traded equity futures are used to manage market exposures to equity price risk and to ensure that asset allocations remain within approved limits. Over the counter equity options are used to buy protection against a fall in equity markets. The Fund's counterparties for equity options include major banking firms and their affiliates. The Fund diversifies its exposure by utilising multiple counterparties, by considering each counterparty's credit rating, and by executing such contracts pursuant to master netting agreements. All transactions are undertaken using ISDAs approved by the Fund. The notional value of the open contracts and their fair value are set out below:

	Notional Value 2010 \$'000	Fair Market Value 2010 \$'000	Notional Value 2009 \$'000	Fair Market Value 2009 \$'000
Buy domestic equity futures contracts	457,313	(27,483)	61,246	(469)
Sell domestic equity futures contracts	–	–	(945,602)	13,882
Buy international equity futures contracts	577,364	(710)	45,628	(807)
Sell international equity futures contracts	–	–	(597,532)	40,385
Exchange traded international equity options	673	761	–	–
Over the counter international equity options	3,301,191	63,796	–	–
Total	4,336,541	36,364	(1,436,260)	52,991

Equity futures contract open positions are cash margined daily with the relevant futures clearing exchange. Whilst the above fair market value represents the value of the open contracts at the reporting date, these positions have been cash settled via postings to or from the associated margin account with the resulting gain or loss recorded in the statement of comprehensive income.

Note 20: Financial instruments and financial risk management (continued)

Note 20C(iii): Equity price risk (continued)

Equity price sensitivity analysis

The analysis below demonstrates the impact on the consolidated entity's operating result of the following movements:

- +/- 20% on Australian equities
- +/- 15% on International equities

The sensitivity analysis has been performed to assess the direct risk of holding equity instruments and associated derivatives. The analysis is undertaken on the base currency values of the underlying exposures. Currency risk sensitivity is considered separately in the currency sensitivity table presented above. The percentage change for each sub-class noted in the table below is measured with reference to each underlying security's forward looking beta, which is a measure of how the underlying security price would change relative to an absolute increase or decrease in the market portfolio which has a beta of 1.

	30 June 2010	30 June 2009
	Impact on operating result \$'000	Impact on operating result \$'000
20% increase in Australian equities	2,450,028	1,824,049
15% increase in International equities	3,578,783	1,881,845
Total	6,028,811	3,705,894
20% decrease in Australian equities	(2,450,022)	(1,817,649)
15% decrease in International equities	(2,655,251)	(1,881,009)
Total	(5,105,273)	(3,698,658)

Note 20: Financial instruments and financial risk management (continued)

Note 20C(iv): Other price risk (collective investment vehicles)

The Future Fund is exposed to other price risks arising from its investments in collective investment vehicles. The Fund mitigates this risk through diversification of its investments.

As noted in Note 20F, in the absence of active markets for a particular investment, judgement is required in determining fair value which introduces an increased element of uncertainty in the determination of that fair value. Collective investment vehicle pricing requires this judgement to be exercised in determining appropriate market reference transactions, pricing or earnings multiples, cash flow estimates and market discount rates.

Similarly, when estimating the potential sensitivity of the inputs into the fair values, there is judgement required as to how to determine what a reasonable change in underlying inputs might be in the next financial period. The Fund has adopted the use of proxy information to assist in determining these sensitivities and these are detailed below.

Private real estate proxy

The Fund has created a proxy index of publicly traded real estate investment trusts (REITs) that is appropriate for the geographical exposure of the portfolio.

Private equity proxy

The Fund has created a proxy after consideration of the investment strategy and geographical exposure of each private equity investment. For example, a venture capital strategy is proxied using micro cap equities in the appropriate geography.

Infrastructure proxy

The Fund utilises an appropriate index of publicly traded infrastructure companies as a proxy.

Alternative strategy funds

An appropriate market index of public traded assets or similar alternative strategy funds is used as a proxy.

Other price risk sensitivity analysis

The sensitivity analysis for other price risk using the proxies noted above is incorporated within the equity risk sensitivity analysis and interest rate sensitivity analysis presented earlier in Notes 20C(i) and 20C(iii).

Note 20: Financial instruments and financial risk management (continued)

Note 20D: Liquidity risk management

Liquidity risk is the risk that the Future Fund will not be able to meet its obligations as they fall due. The primary obligation of the Future Fund, being the payment of the Commonwealth Government's employee superannuation obligations, is not expected to be required to be met until the earlier of the balance of the Fund being greater than or equal to the target asset level or 1 July 2020.

Nonetheless, in the interim period, the Future Fund has sufficient funds available to meet operating expenses and other liabilities.

The following tables summarise the maturity profile of the Fund's financial liabilities, net and gross settled derivative financial liability instruments into relevant maturity groupings based on the remaining period at the reporting date to the contractual maturity date. The tables have been drawn up based on the contractual undiscounted cash flows.

As at 30 June 2010:

	Less than 3 months \$'000	3 months to 1 year \$'000	1 to 5 Years \$'000	> 5 Years \$'000	Total contractual cashflows \$'000	Carrying amount (assets)/ liabilities \$'000
2010						
Non-derivatives						
Unsettled purchases	1,073,304	–	–	–	1,073,304	1,073,304
Accounts payable	165,075	–	–	–	165,075	165,075
Total non-derivatives	1,238,379	–	–	–	1,238,379	1,238,379
Derivatives						
Net settled (interest rate swaps, credit default swaps, interest rate options)	1,579	1,364	167,024	59,099	229,066	229,066
Gross settled (forward foreign exchange contracts, cross currency swaps)						
– (inflow)	(12,464,870)	(20,381,019)	(502,098)	(249,911)	(33,597,898)	(33,597,898)
– outflow	12,955,429	21,718,292	510,929	256,752	35,441,402	35,441,402
Total derivatives	492,138	1,338,637	175,855	65,940	2,072,570	2,072,570

The Fund has posted cash with a futures broker to cover exchange traded futures positions as required under clearing house rules. As at 30 June 2010, the Fund had posted \$208 million in futures margins to cover open positions. This cash remains a financial asset of the Fund, however any alternate use of this cash is restricted.

Note 20: Financial instruments and financial risk management (continued)

Note 20D: Liquidity risk management (continued)

As at 30 June 2009:

	Less than 3 months	3 months to 1 year	1 to 5 Years	> 5 Years	Total contractual cashflows	Carrying amount (assets)/ liabilities
	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000
2009						
Non-derivatives						
Unsettled purchases	922,660	–	–	–	922,660	922,660
Accounts payable	49,647	–	–	–	49,647	49,647
Total non-derivatives	972,307	–	–	–	972,307	972,307
Derivatives						
Net settled (interest rate swaps, credit default swaps)	2	–	8,411	56,552	64,965	64,965
Gross settled (forward foreign exchange contracts)						
– (inflow)	(4,479,426)	(2,707,599)	(1,561,560)	–	(8,748,585)	(8,748,585)
– outflow	4,665,738	3,102,586	1,733,483	–	9,501,807	9,501,807
Total derivatives	186,314	394,987	180,334	56,552	818,187	818,187

Note 20: Financial instruments and financial risk management (continued)

Note 20E: Credit risk

Credit risk is the risk of loss that arises from a counterparty failing to meet their contractual commitments in full and on time, or from losses arising from the change in value of a traded financial instrument as a result of changes in credit risk on that instrument.

The Board sets limits on the credit ratings of debt investments. These limits are reflected in the underlying investment mandates and are monitored by the Agency with compliance reported to the Board.

The Future Fund's maximum exposures to credit risk at reporting date in relation to each class of recognised financial assets is the carrying amount of those assets as indicated in the statement of financial position.

The Fund had, at 30 June 2010, an exposure of greater than 10% of its net assets to interest bearing securities issued by domestic banks. Exposures to individual counterparties are separately identified in the table below.

Domestic interest bearing securities issued by:	\$'000
Commonwealth Bank of Australia	3,185,919
Westpac Banking Corporation	2,954,593
National Australia Bank Limited	2,284,360
Australia and New Zealand Banking Group Limited	2,030,977
Other domestic banks (2 banks* – refer credit exposure analysis below)	534,726
Non-bank issued	2,424
Total	10,992,999

*Includes domestic subsidiaries of foreign banks

The exposures presented above reconcile to Note 8 of the financial statements as follows:

Domestic interest bearing securities issued by:	\$'000
Bank bills – domestic	124,492
Negotiable certificates of deposit – domestic	5,605,026
Corporate debt securities – domestic	5,263,481
Total	10,992,999

Note 20: Financial instruments and financial risk management (continued)

Note 20E: Credit risk (continued)

Exposures as at 30 June 2009:

Domestic interest bearing securities issued by:	\$'000
Commonwealth Bank of Australia	6,355,499
Westpac Banking Corporation	6,429,213
National Australia Bank Limited	4,051,394
Australia and New Zealand Banking Group Limited	4,459,693
Other domestic banks (4 banks* – refer credit exposure analysis below)	1,260,122
Non-bank issued	7,893
Total	22,563,814

*Includes domestic subsidiaries of foreign banks

The exposures presented above reconcile to Note 8 of the financial statements as follows:

Domestic interest bearing securities issued by:	\$'000
Bank bills – domestic	730,447
Negotiable certificates of deposit – domestic	15,109,437
Corporate debt securities – domestic	6,723,930
Total	22,563,814

Exposures are measured at the fair value of the underlying securities which is equivalent to their carrying value in the statement of financial position. Any associated income which is outstanding has been included within the numbers presented. None of these accrued income amounts are past due.

Note 20: Financial instruments and financial risk management (continued)

Note 20E: Credit risk (continued)

Credit risk derivatives

The Fund's managers utilise credit default swaps to gain exposure to, and to hedge, credit risk. The Fund's counterparties for credit default swaps include major banking firms and their affiliates. The Fund diversifies its exposure by utilising multiple counterparties, by considering each counterparty's credit rating, and by executing such contracts pursuant to master netting agreements. All transactions are undertaken using ISDAs approved by the Fund. Managers are required to fully cash back all sold credit protection positions. Outstanding positions are marked to market and collateralisation of out of the money positions is required.

The notional value of the open credit default swap positions and their fair value are set out below:

	Notional Value	Fair Market Value	Notional Value	Fair Market Value
	2010	2010	2009	2009
	\$'000	\$'000	\$'000	\$'000
Buy Credit Protection	1,479,892	40,878	216,694	(1,062)
Sell Credit Protection	301,727	(13,274)	55,606	(22,045)
Total		27,604		(23,107)

Note 20: Financial instruments and financial risk management (continued)

Note 20E: Credit risk (continued)

Credit exposure by credit rating

The following table provides information regarding the credit risk exposures of the debt instruments held by the Future Fund according to the credit ratings of the underlying debt instruments.

	2010 \$'000	2009 \$'000
<i>Long-term rated securities</i>		
AAA	2,378,844	3,352,780
AA	9,005,260	8,733,592
A	1,181,611	631,551
BBB	1,040,855	494,305
Below Investment grade#	5,490,245	3,266,358
<i>Short term rated securities</i>		
A-1+/P-1	5,729,517	15,541,641
A-1	-	298,243
<i>Other</i>		
US Government Guaranteed	531,064	486,995
Total debt securities and cash held	25,357,396	32,805,465
Other non-debt financial assets	44,986,214	29,950,412
Total financial assets	70,343,610	62,755,877

The Fund has a number of mandates with managers specialising in managing distressed debt and corporate loans portfolios.

Credit risk associated with receivables is considered minimal. The main receivables balance is in relation to franking credits which are claimable from the Australian Taxation Office (ATO) annually in July each year. Other receivables balances are immaterial.

There are no overdue contractual receipts due from counterparties as at 30 June 2010 (30 June 2009: nil).

Note 20: Financial instruments and financial risk management (continued)

Note 20F: Fair values of financial assets and liabilities

The carrying amounts of the Fund's assets and liabilities at the end of each reporting period approximate their fair values.

Financial assets and liabilities held at fair value through profit or loss are measured initially at fair value excluding any transaction costs that are directly attributable to the acquisition or issue of the financial asset or financial liability. Transaction costs on financial assets and financial liabilities at fair value through profit or loss are expensed immediately. Subsequent to initial recognition, all instruments held at fair value through profit or loss are measured at fair value with changes in their fair value recognised in the statement of comprehensive income.

(i) Fair value in an active market

The fair value of financial assets and liabilities traded in active markets is based on their quoted market prices at the end of the reporting period without any deduction for estimated future selling costs.

The Fund values its investments in accordance with the accounting policies set out in Note 2. For the majority of its investments, the Fund relies on information provided by independent pricing services for the valuation of its investments.

The quoted market price used for financial assets held by the Fund is the current bid price; the appropriate quoted market price for financial liabilities is the current asking price.

A financial instrument is regarded as quoted in an active market if quoted prices are readily and regularly available from an exchange, dealer, broker, industry group, pricing service, or regulatory agency, and those prices represent actual and regularly occurring market transactions on an arm's length basis.

As a result of events in global markets in the past year and comparative period, liquidity in some investment markets decreased significantly. As a result, the volume of trading in some of the investments held by the Fund decreased significantly, and accordingly the valuation of those investments is subject to a greater uncertainty and requires greater judgement than would be the case in normal investment market conditions.

(ii) Fair value in an inactive or unquoted market

The fair value of financial assets and liabilities that are not traded in an active market is determined using valuation techniques employed by the managers the Board has engaged or by the Fund directly. These include the use of recent transactions to the extent these are available and are not distressed transactions, reference to the current fair value of a substantially similar other instrument, discounted cash flow techniques, option pricing models or any other valuation technique that provides an estimate of prices that could be obtained in actual market transactions.

Where discounted cash flow techniques are used, estimated future cash flows are based on best estimates and the discount rate used is a market rate at the balance date applicable for an instrument with similar terms and conditions.

Note 20: Financial instruments and financial risk management (continued)

Note 20F: Fair values of financial assets and liabilities (continued)

For other pricing models, inputs are based on market data at balance date. Fair values for unquoted equity investments are estimated, if possible, using applicable price/earnings ratios for similar listed companies adjusted to reflect the specific circumstances of the issuer.

The fair value of derivatives that are not exchange traded is estimated at the amount that the Fund would receive or pay to terminate the contract at the balance date taking into account current market conditions (volatility and appropriate yield curve). The fair value of a forward contract is determined as a net present value of estimated future cash flows, discounted at appropriate market rates as at the valuation date. The fair value of an option contract is determined by applying industry standard option pricing models.

Note 20G: Fair value hierarchy

The Fund has adopted the amendments to AASB 7, effective 1 July 2009. This requires the fund to classify fair value measurements using a fair value hierarchy that reflects the subjectivity of the inputs used in making the measurements. The following table provides an analysis of financial instruments held at 30 June 2010 that are measured subsequent to initial recognition at fair value, grouped into Levels 1 to 3 based on the degree to which the fair value is observable.

- > Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets or liabilities
- > Level 2 fair value measurements are those derived from inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices)
- > Level 3 fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs).

Investments whose values are based on quoted market prices in active markets, and therefore classified within level 1, include active listed equities and exchange traded derivatives.

Financial instruments that trade in markets that are not considered to be active but are valued based on quoted market prices, dealer quotations or alternative pricing sources supported by observable inputs are classified within level 2. These include both investment grade and non investment grade interest bearing securities and over the counter derivatives.

The Fund must appoint investment managers to invest the assets of the Fund under the Act. A significant proportion of these investments are made via pooled investment vehicles which in turn invest in a variety of underlying investments (and are classified as Level 3 investments). The diverse nature of the investments they make on the Fund's behalf means it is not possible to provide additional information in these financial statements regarding how inputs into the valuation of Level 3 investments might change nor the resultant impact on the statement of comprehensive income that such changes to valuation inputs might trigger.

As noted in Note 20C (iv) the Fund has used proxy investment exposures to provide sensitivity information surrounding the possible impact on the income of the Fund should equity or interest rate markets move up or down by a specified amount.

Note 20: Financial Instruments and Financial Risk Management (continued)

Note 20G: Fair value hierarchy (continued)

	Level 1 \$'000	Level 2 \$'000	Level 3 \$'000	Total \$'000
Financial assets at fair value through profit or loss:				
Interest bearing securities	4,375	20,727,980	1,600,620	22,332,975
Listed equities and listed managed investment schemes	28,228,963	50,899	235,210	28,515,072
Collective investment vehicles	–	–	14,198,020	14,198,020
Derivatives	761	1,204,135	2,978	1,207,874
Total	28,234,099	21,983,014	16,036,828	66,253,941
Financial liabilities at fair value:				
Derivatives	–	2,067,033	5,537	2,072,570
Total	–	2,067,033	5,537	2,072,570

The disclosure for collective investment vehicles presented in the above table shows all investments classified as level 3. The financial statements received from the managers provide additional information in relation to the underlying investments and on a look through basis the disclosure is as follows:

	Level 1 \$'000	Level 2 \$'000	Level 3 \$'000	Total \$'000
Collective investment vehicles	1,120,185	4,382,676	8,695,159	14,198,020

The following table presents the transfers between levels for the year ended 30 June 2010

	Level 1 \$'000	Level 2 \$'000	Level 3 \$'000
Transfers between levels 1 and 2	85,408	(85,408)	–
Transfers between levels 2 and 3	–	604,139	(604,139)

Note 20: Financial Instruments and Financial Risk Management (continued)

Note 20G: Fair value hierarchy (continued)

The following table presents the movement in level 3 instruments for the year ended 30 June 2010 by class of financial instrument.

	Interest bearing securities \$'000	Listed equities and listed managed investment schemes \$'000	Collective investment vehicles \$'000	Derivatives \$'000	Total \$'000
Financial assets at fair value through profit or loss:					
Opening balance	2,069,214	276,275	4,690,163	–	7,035,652
Purchases	580,687	122,941	8,355,831	1,976	9,061,435
Sales	(662,897)	(33,413)	–	–	(696,310)
Transfers into level 3	97,363	7,792	–	–	105,155
Gains and losses recognised in the statement of comprehensive income	54,719	31,779	1,152,026	1,002	1,239,526
Transfers out of level 3	(538,466)	(170,164)	–	–	(708,630)
Closing balance	1,600,620	235,210	14,198,020	2,978	16,036,828

	Interest bearing securities \$'000	Listed equities and listed managed investment schemes \$'000	Collective investment vehicles \$'000	Derivatives \$'000	Total \$'000
Financial liabilities at fair value through profit or loss:					
Opening balance	–	–	–	88	–
Purchases	–	–	–	250,000	250,000
Sales	–	–	–	(249,600)	(249,600)
Transfers into level 3	–	–	–	–	–
Gains and losses recognised in the statement of comprehensive income	–	–	–	(5,361)	(5,361)
Transfers out of level 3	–	–	–	(664)	(664)
Closing balance	–	–	–	(5,537)	(5,537)

Note 21: Events occurring after reporting date

There have been no significant events occurring after reporting date that would materially affect these financial statements.

Note 22: Parent Entity

The following table sets out information relating to the parent entity which comprises Future Fund Management Agency and the Board of Guardians:

	30 June 2010 \$'000	30 June 2009 \$'000
Total assets	70,321,734	62,590,191
Total liabilities	3,039,698	1,628,629
Total equity and amount attributable to the Government	67,282,036	60,961,562
Profit/(loss)	6,320,474	(3,319,357)
Total comprehensive income	6,320,474	(3,319,357)

The parent entity has committed to funding the subsidiary commitments as detailed in Note 8 for both the current and comparative years.

Note 23: Compensation and debt relief disclosures

No 'Act of Grace' payments were made during the reporting period (2009: nil).

No waivers of amounts owing to the government were made pursuant to subsection 34(1) of the *Financial Management and Accountability Act 1997* during the reporting period (2009: nil).

No payments were made under the 'Defective Administration Scheme' during the reporting period (2009: nil).

No payments were made under section 73 of the *Public Service Act 1999* during the reporting period (2009: nil).

No payments were made under ex-gratia programs during the reporting period (2009: nil).

Note 24: Special Accounts

Note 24A: Special Accounts: Future Fund Special Account

Legal Authority — *Future Fund Act 2006* (as amended), section 12.

Purpose — establishment and ongoing operation of the Future Fund.

Disclosures below are on a cash basis and consolidate departmental and administered items.

Future Fund Special Account	Period from 1 July 2009 to 30 June 2010 \$'000	Period from 1 July 2008 to 30 June 2009 \$'000
Balance carried from previous period	–	–
Bank interest amounts credited	–	–
Appropriations for reporting period	–	–
Other Receipts:		
GST credits	10,170	4,890
Amounts transferred from investment account ^(a)	278,477	84,064
Amounts credited to the special account	–	–
Total Credits	288,647	88,954
Available for payments	288,647	88,954
Payments made:		
Investments debited from the Special Account (FFA s17)	–	–
Payments made		
– Remuneration of Board of Guardians and Agency staff	16,947	13,168
– Suppliers	31,559	18,408
– Investment expenses	237,954	56,985
– Purchase of capital equipment and software	2,187	393
Total Debits	288,647	88,954
Balance carried forward to next year ^(b)	–	–

(a) The operations of the Future Fund are funded via the investment revenue generated.

(b) Excluding investments balances, see Note 24C.

Note 24B: Special accounts: Other Trust Moneys – Future Fund Management Agency Special Account

The Other Trust Moneys – Future Fund Management Agency Special Account is a Special Public Money account established for the purpose:

- a) Of disbursing amounts temporarily held on trust or otherwise for the benefit of a person other than the Commonwealth; and
- b) to repay amounts where an Act or other law requires or permits the repayment of an amount received.

The Special Account was established under s20 of the *Financial Management and Accountability Act 1997*. The Special Account has not been used during the current year or the comparative reporting period and has a nil balance as at 30 June 2010.

Note 24C: Special Accounts: Investment of Public Money

Disclosures below are on a cash basis, except for the transfer of Telstra shares.

Future Fund Special Account: Investment of Public Money under section 17 of the <i>Future Fund Act 2006</i> (as amended)	Period from 1 July 2009 to 30 June 2010 \$'000	Period from 1 July 2008 to 30 June 2009 \$'000
Opening balance	65,839,783	66,511,021
Investments made on transfer of funds from the Special Account	–	–
Realised investments reinvested	86,788,002	124,528,518
Telstra shares – non reciprocal transfer	–	140,741
Interest earned reinvested	1,138,855	2,202,422
Dividends received reinvested	1,081,086	1,140,984
Franking credits received reinvested	323,224	291,820
Foreign currency realised reinvested	3,200,798	(2,032,640)
Other income reinvested	6,042	–
Amounts transferred to operations ^(a)	(278,477)	(84,064)
Investments realised	(87,289,609)	(126,859,019)
Closing Balance	70,809,704	65,839,783

(a) The operations of the Future Fund are funded via the investment revenue generated.

Note 25: Reporting of outcomes

Note 25A: Net cost of outcome delivery

Outcome 1: Managing and growing publicly funded investments to meet future financial needs and contribute to the prosperity of future generations of Australians.

	Outcome 1 2010 \$'000	Outcome 1 2009 \$'000
<i>Expenses</i>		
Investment related expenses	307,387	106,618
Depreciation and amortisation	855	649
Agency and Board remuneration expenses	18,856	15,019
Other expenses	12,791	7,200
Total expenses	339,889	129,486
<i>Costs recovered from provision of goods and services to the non-government sector</i>		
Income		
Interest	71,274	105,548
Dividends, distributions and imputation credits	1,387,549	1,479,652
Realised and unrealised investment gains and losses	5,192,672	(4,774,747)
Other income	8,868	156
Total income	6,660,363	(3,189,391)
Net cost (contribution) of outcome	(6,320,474)	3,318,877

Note 25: Reporting of outcomes (continued)

Note 25B: Net cost of outcome delivery – Programs

The Future Fund Management Agency ('the Agency') has two programs: the management of the investment of the Future Fund and the management of the investment of the Building Australia Fund, Education Investment Fund and Health and Hospitals Fund.

Program 1.1 Management of the investment of the Future Fund.

The Agency supports the Board in investing to accumulate assets for the purpose of offsetting the unfunded superannuation liabilities of the Australian Government which will fall due on future generations. The net cost of this output delivery is presented above in Note 25A.

Program 1.2 Management of the investment of the Building Australia Fund, Education Investment Fund and Health and Hospitals Fund (the BAF, EIF and HHF)

Under the *Nation-building Funds Act 2008*, the role of the Agency was extended to include supporting the Board in the investment of the assets of the BAF, EIF and HHF (each a 'Fund'). The Agency charges a monthly fee to each Fund to reimburse the Agency for shared costs paid by the Agency, as agreed with the Department of Finance and Deregulation. This is shown as other income in the income statement. Direct costs to the BAF, EIF and HHF, such as investment management and custody fees, were charged directly to each Fund's Special Account and are not reported as part of these financial statements.

Appendices

Future Fund Investment Mandate Directions

Part 1 – Preliminary

1. Name of Directions

These Directions are the Future Fund Investment Mandate Directions 2006.

2. Commencement

These Directions commence on 22 May 2006.

3. Definitions

In these Directions:

Act means the *Future Fund Act 2006*.

Fund means the Future Fund.

Board means the Future Fund Board of Guardians.

4. Objective of these Directions

The Future Fund will make provision for unfunded superannuation liabilities that will become payable during a period when an ageing population is likely to place significant pressure on the Commonwealth's finances.

The objective of these directions is to give guidance to the Board in relation to its investment strategy for the Future Fund. The Future Fund Board of Guardians is required under section 18 of the Act to seek to maximise the return earned on the Fund over the long term, consistent with international best practice for institutional investment and subject to its obligations under the Act and any directions given by the responsible Ministers under subsection 18(1) or subclause 8(1) of Schedule 1 of the Act.

These Directions are given under subsection 18(1) of the Act to articulate the Government's expectations for how the Fund will be invested and managed by the Board.

Investments by the Future Fund will be confined to financial assets.

Part 2 – Directions

5. Benchmark return

The Board is to adopt an average return of at least the Consumer Price Index (CPI) + 4.5 to 5.5 per cent per annum over the long term as the benchmark return on the Fund.

During the initial transition period, as the Board develops a long-term strategic asset allocation, a return lower than the benchmark return is expected.

In targeting the benchmark return, the Board must determine an acceptable but not excessive level of risk for the Fund measured in terms such as the probability of losses in a particular year.

6. Limits for holdings of listed companies

The Board must establish a limit for holdings on any listed company in order to prevent a breach of the statutory limits imposed by sections 21 and 22 of the Act.

7. Telstra Corporation

The Board must not acquire a direct equity holding of voting shares in Telstra Corporation Limited except as a result of a transfer of financial assets by the responsible Ministers under clause 6 of Schedule 1 of the Act or a gift of financial assets under clause 7 of Schedule 1 of the Act.

8. Board must consider impacts from its investment strategy

In undertaking its investment activities, the Board must act in a way that:

- minimises the potential to effect any abnormal change in the volatility or efficient operation of Australian financial markets; and
- is unlikely to cause any diminution of the Australian Government's reputation in Australian and international financial markets.

9. Corporate Governance

The Board must have regard to international best practice for institutional investment in determining its approach to corporate governance principles, including in relation to its voting policy.

Future Fund Ministerial Directions – Telstra holding

1. Definitions

For the purposes of this direction:

ASX means the Australian Stock Exchange Limited;

Board means the Future Fund Board of Guardians;

Dispose of a Telstra Share means:

- (a) sell, transfer, create a trust over or interest (including any legal, beneficial or relevant interest (as defined in the *Corporations Act 2001*)) in, or alienate any right or power attached to, a Telstra Share or create, issue or sell a financial product convertible into, exchangeable for or representing the right to receive a Telstra Share; or
- (b) agree or undertake to do any of the foregoing, whether conditionally or unconditionally; or
- (c) do anything having the economic effect of any of the foregoing including entering into a derivative (as defined in the *Corporations Act 2001*) over Telstra Shares.

Telstra means Telstra Corporation Limited;

Telstra 3 Instalment Receipts means instalment receipts that:

- (a) relate to ordinary shares in Telstra; and
- (b) are issued in connection with the Telstra 3 Share Offer.

Telstra 3 Share Offer means the offer by the Commonwealth of ordinary shares in Telstra to retail and institutional investors, through an offer of instalment receipts relating to those shares (Telstra 3 Instalment Receipts) made in October and November 2006; and

Telstra Shares means ordinary shares in Telstra that are transferred to the Future Fund by the Commonwealth Government after the closure of the Telstra 3 Share Offer.

2. Ministerial Direction

2.1 Disposal of Telstra shares

Subject to paragraph 2.2 below, the Board must not Dispose of any Telstra Shares during the period from and including the date Telstra 3 Instalment Receipts are first listed on ASX to and including the date 2 years after that date (the 'Lock-up Period').

2.2 Exceptions

At any time during the Lock-up Period, the Board may Dispose of Telstra Shares:

- (a) only if requested by Telstra and agreed by the Board, as part of any Telstra initiated dividend reinvestment plan or share top-up plan; and
- (b) only if requested by Telstra and agreed by the Board, as part of any Telstra initiated capital management initiative, such as a buy-back or capital reduction (whether selective or based on equal access or of any other nature – for the avoidance of doubt, if any such initiative is based on equal access, Telstra will be taken to have requested the Board's participation); and
- (c) to a single investor, provided that:
 - (A) the parcel of Telstra Shares to which the Disposal relates is greater than 3% of Telstra's issued ordinary shares at the time of the Disposal; and
 - (B) the investor provides an enforceable undertaking on terms acceptable to the Board and the Commonwealth to be bound by similar lock-up provisions to those contained in this direction for at least the balance of the Lock-up Period (except that the undertaking will not contain an exception equivalent to this clause 2.2(c) but may contain an exception for a Disposal as a result of a bona fide exercise of security by financiers to the investor); and
 - (C) Telstra is advised prior to such Disposal; and
 - (D) the price per Telstra Share is no less than the Telstra 3 Share Offer institutional offer price; and
 - (E) the date of the disposal is at least six months following the initial listing of Telstra 3 Instalment Receipts on the ASX.

Building Australia Fund Investment Mandate Directions

Part 1 – Preliminary

1. Name of Directions

These Directions are the Building Australia Fund Investment Mandate Directions 2009.

2. Commencement

These Directions commence on the 15th day after they are given.

Note: Section 42 of the *Legislative Instruments Act 2003* (which deals with the disallowance of legislative instruments) does not apply to this instrument: see section 44 of that Act. Part 6 of that Act (which deals with the sunset of legislative instruments) does not apply to this instrument: see section 54 of that Act.

3. Definitions

In these Directions:

Act means the *Nation-building Funds Act 2008*.

Board means the Future Fund Board of Guardians.

Fund means the Building Australia Fund.

responsible Ministers has the same meaning as in the Act.

4. Object of these Directions

- (1) The Building Australia Fund is a financing source to enhance the Commonwealth's ability to make payments in relation to the creation or development of transport, communications, energy and water infrastructure, and eligible national broadband network matters.
- (2) The object of these Directions is to give guidance to the Board in relation to its investment strategy for the Fund. The Board is required by the Act to seek to maximise the return earned on the Fund, consistent with international best practice for institutional investment and subject to its obligations under the Act and any directions given by the responsible Ministers under the Act.
- (3) These Directions are given under subsection 35 (1) of the Act to articulate the Australian Government's expectations of how the Fund will be invested and managed by the Board.
- (4) The responsible Ministers may review these Directions, including the benchmark return, in consultation with the Board. The first review is expected to occur before 1 July 2010.

Part 2 – Directions

5. Benchmark return

- (1) The Board is to adopt a benchmark return on the Fund of the Australian three month bank bill swap rate + 0.3 per cent per annum, calculated on a rolling 12 month basis (net of fees).
- (2) In targeting this benchmark return, the Board should invest in such a way as to minimise the probability of capital losses over a 12 month horizon.

6. Board must consider impacts from its investment strategy

In undertaking its investment activities,

the Board must act in a way that:

- (a) minimises the potential to effect any abnormal change in the volatility or efficient operation of Australian financial markets; and
- (b) is unlikely to cause any diminution of the Australian Government's reputation in Australian and international financial markets.

Note

1. All legislative instruments and compilations are registered on the Federal Register of Legislative Instruments kept under the *Legislative Instruments Act 2003*. See <http://www.frli.gov.au>.

Education Investment Fund Investment Mandate Directions

Part 1 – Preliminary

1. Name of Directions

These Directions are the Education Investment Fund Investment Mandate Directions 2009.

2. Commencement

These Directions commence on the 15th day after they are given.

Note: Section 42 of the *Legislative Instruments Act 2003* (which deals with the disallowance of legislative instruments) does not apply to this instrument: see section 44 of that Act. Part 6 of that Act (which deals with the sunseting of legislative instruments) does not apply to this instrument: see section 54 of that Act.

3. Definitions

In these Directions:

Act means the *Nation-building Funds Act 2008*.

Board means the Future Fund Board of Guardians.

Fund means the Education Investment Fund.

responsible Ministers has the same meaning as in the Act.

4. Object of these Directions

- (1) The Education Investment Fund is a financing source to enhance the Commonwealth's ability to make payments in relation to the creation or development of higher education, research, vocational education and training and eligible education infrastructure, and to make transitional Higher Education Endowment Fund payments.
- (2) The object of these Directions is to give guidance to the Board in relation to its investment strategy for the Fund. The Board is required by the Act to seek to maximise the return earned on the Fund, consistent with international best practice for institutional investment and subject to its obligations under the Act and any directions given by the responsible Ministers under the Act.
- (3) These Directions are given under subsection 154 (1) of the Act to articulate the Australian Government's expectations of how the Fund will be invested and managed by the Board.
- (4) The responsible Ministers may review these Directions, including the benchmark return, in consultation with the Board. The first review is expected to occur before 1 July 2010.

Part 2 – Directions

5. Benchmark return

- (1) The Board is to adopt a benchmark return on the Fund of the Australian three month bank bill swap rate + 0.3 per cent per annum, calculated on a rolling 12 month basis (net of fees).
- (2) In targeting this benchmark return, the Board should invest in such a way as to minimise the probability of capital losses over a 12 month horizon.

6. Board must consider impacts from its investment strategy

In undertaking its investment activities,

the Board must act in a way that:

- (a) minimises the potential to effect any abnormal change in the volatility or efficient operation of Australian financial markets; and
- (b) is unlikely to cause any diminution of the Australian Government's reputation in Australian and international financial markets.

Note

1. All legislative instruments and compilations are registered on the Federal Register of Legislative Instruments kept under the *Legislative Instruments Act 2003*. See <http://www.frli.gov.au>.

Health and Hospitals Fund Investment Mandate Directions

Part 1 – Preliminary

1. Name of Directions

These Directions are the Health and Hospitals Fund Investment Mandate Directions 2009.

2. Commencement

These Directions commence on the 15th day after they are given.

Note: Section 42 of the *Legislative Instruments Act 2003* (which deals with the disallowance of legislative instruments) does not apply to this instrument: see section 44 of that Act. Part 6 of that Act (which deals with the sunset of legislative instruments) does not apply to this instrument: see section 54 of that Act.

3. Definitions

In these Directions:

Act means the *Nation-building Funds Act 2008*.

Board means the Future Fund Board of Guardians.

Fund means the Health and Hospitals Fund.

responsible Ministers has the same meaning as in the Act.

4. Object of these Directions

- (1) The Health and Hospitals Fund is a financing source to enhance the Commonwealth's ability to make payments in relation to the creation or development of health infrastructure.
- (2) The object of these Directions is to give guidance to the Board in relation to its investment strategy for the Fund. The Board is required by the Act to seek to maximise the return earned on the Fund, consistent with international best practice for institutional investment and subject to its obligations under the Act and any directions given by the responsible Ministers under the Act.
- (3) These Directions are given under subsection 229 (1) of the Act to articulate the Australian Government's expectations of how the Fund will be invested and managed by the Board.
- (4) The responsible Ministers may review these Directions, including the benchmark return, in consultation with the Board. The first review is expected to occur before 1 July 2010.

Part 2 – Directions

5. Benchmark return

- (1) The Board is to adopt a benchmark return on the Fund of the Australian three month bank bill swap rate + 0.3 per cent per annum, calculated on a rolling 12 month basis (net of fees).
- (2) In targeting this benchmark return, the Board should invest in such a way as to minimise the probability of capital losses over a 12 month horizon.

6. Board must consider impacts from its investment strategy

In undertaking its investment activities, the Board must act in a way that:

- (a) minimises the potential to effect any abnormal change in the volatility or efficient operation of Australian financial markets; and
- (b) is unlikely to cause any diminution of the Australian Government's reputation in Australian and international financial markets.

Note

1. All legislative instruments and compilations are registered on the Federal Register of Legislative Instruments kept under the *Legislative Instruments Act 2003*. See <http://www.frli.gov.au>.

Implementation of the Santiago Principles

The Santiago Principles are a voluntary set of principles and practices developed by the International Working Group of Sovereign Wealth Funds during 2008. The Principles identify a framework of generally accepted principles and practices that properly reflect appropriate governance and accountability arrangements as well as the conduct of investment practices by Sovereign Wealth Funds (SWFs) on a prudent and sound basis.

The International Forum of Sovereign Wealth Funds (IFSWF) has subsequently been formed and is a voluntary group of SWFs, which will meet, exchange

views on issues of common interest, and facilitate an understanding of the Santiago Principles and SWF activities. The Chair of the Future Fund, Mr David Murray is also Chair of the IFSWF. This document focuses primarily on the implementation of the Santiago Principles in the context of the Future Fund. This reflects the fact that the Nation-building Funds draw on the legal, institutional and investment and risk management framework of the Future Fund and that their principal distinguishing characteristic is their shorter-term focus.

Principle	Implementation and reference material
<p>1 The legal framework should be sound and support the SWF's effective operation and the achievement of its stated objectives:</p> <p>1.1 The legal framework should ensure the legal soundness of the SWF and its transactions</p> <p>1.2 The key features of the SWF's legal basis and structure, as well as the legal relationship between the SWF and other state bodies, should be publicly disclosed.</p>	<p>The legal framework for the Board of Guardians and the Agency, together with arrangements for the governance and operation of the public asset funds for which the Board of Guardians is responsible, are detailed in the <i>Future Fund Act 2006</i> and <i>Nation-Building Funds Act 2008</i>. The framework is designed specifically to establish the sound and effective operation of the Fund and achievement of its objectives.</p> <p>The legal basis and structure and the legal relationships between the Board, Agency and Government are detailed in the legislation which is publicly available.</p> <p>Additional detail and discussion of the basis and operation of the Board, Agency and the Funds themselves is available from the Board's annual report and website.</p> <p>www.futurefund.gov.au/about_the_future_fund/legislation www.futurefund.gov.au/investment/investment_mandate</p>
<p>2 The SWF's policy purpose should be being clearly defined and publicly disclosed.</p>	<p>The Future Fund was established to meet unfunded superannuation liabilities that will become payable during a period when an ageing population is likely to place significant pressure on Commonwealth finances. The Nation-building Funds were established to provide financing resources to meet the Australian Government's commitment to Australia's future through investment in critical areas of infrastructure such as transport, communications, energy, water, education, research and health.</p> <p>Detail on the policy purpose for each of the Funds is provided in the relevant legislation, annual reports and the organisation's website.</p> <p>www.futurefund.gov.au/about_the_future_fund/legislation www.futurefund.gov.au/investment/investment_mandate www.futurefund.gov.au/annual_reports</p>

Principle**Implementation and reference material**

3 Where the SWF has significant direct domestic macroeconomic implications, those activities should be closely coordinated with domestic fiscal and monetary authorities so as to ensure consistency with the overall macroeconomic policies.

The Australian Government is responsible for determining the timing and extent of withdrawals from the Future Fund and Nation-building Funds, subject to legislative constraints. The Australian Government is not permitted to access the Future Fund until the earlier of 2020 or when the investments exceed the target asset level, at which time any withdrawals will assist the Australian Government Budgetary position. Coordination with all relevant fiscal and monetary authorities will be undertaken at this time.

In establishing the Nation-building Funds the Australian Government made a commitment that spending proposals would be delivered in line with prevailing macroeconomic conditions. Spending from the Nation-building Funds is undertaken consistent with the legislated process and as part of the usual Budget process within the limits of the legislated General Drawing Rights Limit. Coordination with all relevant fiscal and monetary authorities, and relevant departments, is undertaken as part of this process.

The investment of the assets of the Funds is undertaken by the Board in accordance with the risk and return requirements of the Investment Mandates and has no macroeconomic implications.

www.futurefund.gov.au/about_the_future_fund/legislation

4 There should be clear and publicly disclosed policies, rules, procedures, or arrangements in relation to the SWF's approach to funding, withdrawal and spending operations.

The legislation publicly sets out the funding, withdrawal and spending arrangements and procedures for the Funds, including arrangements for Parliamentary oversight and public disclosure of funding, withdrawals and spending. The source of funding is publicly disclosed together with the approach to withdrawals and spending of monies.

4.1 The source of SWF funding should be publicly disclosed

www.futurefund.gov.au/about_the_future_fund/legislation

4.2 The general approach to withdrawals from the SWF and spending on behalf of the government should be disclosed.

www.finance.gov.au/investment-funds/future-fund/transfers.html

www.finance.gov.au/investment-funds/NBF/NBF_transfers.html

5 The relevant statistical data pertaining to the SWF should be reported on a timely basis to the owner, or otherwise as required, for inclusion where appropriate in macroeconomic data sets.

Statistical data is consolidated in national financial accounts, government financial statistics, the balance of payments and international investment position by the Australian Bureau of Statistics in accordance with its regular data collection and reporting arrangements. Data is also incorporated into the Government's budget statements.

Audited annual financial statements are tabled in Parliament and quarterly updates on the portfolio and released publicly.

www.abs.gov.au

http://www.futurefund.gov.au/investment/portfolio_updates

Principle

Implementation and reference material

6 The governance framework for the SWF should be sound and establish clear and effective division of roles and responsibilities in order to facilitate accountability and operational independence in the management of the SWF to pursue its objectives.

The roles and responsibilities of the Government, as asset owner, and the Board (supported by the Agency), as asset manager are detailed in the legislation.

Further detail is provided by the Investment Mandates and the Statement of Expectations and Statement of Intent exchanged between the Government and the Board and the Agency.

Internal policies, procedures and protocols have been established to further delineate roles and responsibilities at the operational level.

www.futurefund.gov.au/about_the_future_fund/legislation
www.futurefund.gov.au/__data/assets/pdf_file/0016/3571/SoE_-_Final.pdf
www.futurefund.gov.au/__data/assets/pdf_file/0017/3572/Sol_Final_300909.pdf

7 The owner should set the objectives of the SWF, appoint the members of its governing body(ies) in accordance with clearly defined procedures, and exercise oversight over the SWF's operations.

The objective for each Fund, the procedures for the appointment of the Board of Guardians by Government and arrangements for the exercise of oversight are detailed in the legislation.

www.futurefund.gov.au/about_the_future_fund/legislation

8 The governing body(ies) should act in the best interests of the SWF, and have a clear mandate and adequate authority and competency to carry out its functions.

The Board is bound by the legislation and Investment Mandates set by Government to pursue the investment objectives detailed in the legislation and to act in good faith. The legislation also provides the Board with the necessary powers to undertake its mandated activities and sets out the experience, expertise and credibility required of appointees to the Board.

www.futurefund.gov.au/about_the_future_fund/legislation
www.futurefund.gov.au/investment/investment_mandate

9 The operational management of the SWF should implement the SWF's strategies in an independent manner and in accordance with clearly defined responsibilities.

The Board is responsible for investing the assets of the Funds in accordance with the legislation and makes decisions independently of Government. The legislation establishes the Agency to provide support and advice to the Board and to assist in giving effect to the Board's decisions.

Clear internal policies, procedures and protocols have been established to further delineate roles and responsibilities at the operational level.

www.futurefund.gov.au/about_the_future_fund/legislation

10 The accountability framework for the SWF's operations should be clearly defined in the relevant legislation, charter, other constitutive documents, or management agreement.

Accountability arrangements, including the requirement for publication of an annual report and arrangements for the provision of reports and information to the responsible Minister, are detailed in the legislation.

Further accountability is also provided through the operation of the *Financial Management and Accountability Act 1997* governing the establishment and operation of Special Accounts for each Fund.

www.futurefund.gov.au/about_the_future_fund/legislation

Principle**Implementation and reference material**

11 An annual report and accompanying financial statements on the SWF's operations and performance should be prepared in a timely fashion and in accordance with recognised internal or national accounting standards in a consistent manner.

The annual report and financial statements, prepared in accordance with the Finance Minister's Orders made under the *Financial Management and Accountability Act 1997* including the Australian Accounting Standards of the Fund.

The legislation requires that the annual report and audited financial statements are presented to the responsible Minister as soon as practicable after the end of each financial year and tabled in Parliament within 15 sitting days of each House of Parliament.

www.futurefund.gov.au/about_the_future_fund/legislation
www.futurefund.gov.au/annual_reports

12 The SWF's operations and financial statements should be audited annually in accordance with recognised international or national auditing standards in a consistent manner.

Internal audit services are provided by an external firm reporting to the Board's Audit Committee. The Australian National Audit Office is responsible for an annual independent external audit conducted in accordance with the Australian National Audit Office Auditing Standards, which incorporate and Australian Auditing Standards.

www.futurefund.gov.au/about_the_future_fund/legislation
www.anao.gov.au

13 Professional and ethical standards should be clearly defined and made known to the members of the SWF's governing body(ies), management and staff.

The duties and obligations of members of the Board of Guardians are detailed in the legislation together with arrangements for the management of conflicts of interest. The legislation also includes details of the civil and criminal penalties applying for breach of specific duties and obligations. Persons are eligible for appointment to the Board only if the responsible Ministers are satisfied the person has substantial experience or expertise and professional credibility and significant standing in investing in financial assets, managing investments in financial assets or corporate governance.

Staff of the Agency are employed under the *Public Service Act 1999* and are bound by the Australian Public Service Values and Code of Conduct. Details of these obligations are included in internal policies and training activities.

www.futurefund.gov.au/about_the_future_fund/legislation
<http://www.apsc.gov.au/values/conductguidelines.htm>

14 Dealing with third parties for the purpose of the SWF's operational management should be based on economic and financial grounds, and follow clear rules and procedures.

The Board's approach to the engagement of third parties, including advisers and investment managers, is outlined in its Statement of Investment Policies available on the internet. Engagement of third parties is based on economic and financial grounds.

The purchase of goods and services by the Agency is consistent with the Commonwealth Procurement Guidelines and governed by clear internal policies and procedures to encourage value for money, open and effective competition and fair dealing and ethics.

www.futurefund.gov.au/investment/investment_policies

Principle**Implementation and reference material**

15 SWF operations and activities in host countries should be conducted in compliance with all applicable regulatory and disclosure requirements of the countries in which they operate.

The Board of Guardians ensures that all investment activities are undertaken in accordance with applicable regulatory and disclosures requirements. Detailed due diligence and reporting is in place to monitor compliance. The legislation requires the Board of Guardians to act in a way that is unlikely to cause any diminution of the Australian Government's reputation in international financial markets.

www.futurefund.gov.au/about_the_future_fund/legislation

16 The governance framework and objectives, as well as the manner in which the SWF's management is operationally independent from the owner, should be publicly disclosed.

The governance framework and objectives of the Board and the Agency are set out in the legislation and in public annual reports. The framework clearly establishes the independence and accountability arrangements for the Fund, the Board and the Agency.

www.futurefund.gov.au/about_the_future_fund/legislation

www.futurefund.gov.au/annual_reports

17 Relevant financial information regarding the SWF should be publicly disclosed to demonstrate its economic and financial orientation, so as to contribute to stability in internal financial markets and enhance trust in recipient countries.

An annual report and audited annual financial statements are tabled in Parliament and published via the website. The Board also issues public quarterly updates on performance and asset allocation.

www.futurefund.gov.au/annual_reports

www.futurefund.gov.au/investment/portfolio_updates

18 The SWF's investment policy should be clear and consistent with its defined objectives, risk tolerance, and investment strategy, as set by the owner or the governing body(ies), and be based on sound portfolio management principles.

The Board's Statement of Investment Policies, published on the internet as required by legislation, details its investment strategy and risk tolerance and its application of portfolio investment principles. Annual reports provide additional insight and discussion of the investment strategy.

18.1 The investment policy should guide the SWF's financial risk exposures and possible use of leverage.

These documents address matters relating to financial risk, leverage, the use of and extent of the activities and authority of internal/external managers as well as the process for their appointment and monitoring of their performance.

18.2 The investment policy should address the extent to which internal and/or external investment managers are used, the range of their activities and authority, and the process by which they are selected and their performance monitored.

The policies and practices detailed by these documents are consistent with the obligations contained in the legislation.

18.3 A description of the investment policy of the SWF should be publicly disclosed.

www.futurefund.gov.au/about_the_future_fund/legislation

www.futurefund.gov.au/investment/investment_policies

www.futurefund.gov.au/annual_reports

Principle**Implementation and reference material**

19 The SWF's investment decisions should aim to maximise risk-adjusted financial returns in a manner consistent with its investment policy, and based on economic and financial grounds.

19.1 If investment decisions are subject to other than economic and financial considerations, these should be clearly set out in the investment policy and be publicly disclosed.

19.2 The management of the SWF's assets should be consistent with what is generally accepted as sound asset management principles.

The Board's obligation to seek to maximise risk-adjusted financial returns is established in the legislation with return and risk parameters detailed through investment mandates created under the legislation. The Board is required to operate in a manner consistent with international best practice for institutional investment.

The limited set of restrictions on the Board's investment activities, such as limits on the size of stakes in Australian and foreign listed companies, are clearly expressed in the legislation. The Board's approach to consideration of environmental, social and governance matters in its investments is detailed in its Statement of Investment policies and reflects the Board's focus on acting as a prudent investor seeking to maximise risk-adjusted returns.

www.futurefund.gov.au/about_the_future_fund/legislation

20 The SWF should not seek or take advantage of privileged information or inappropriate influence by the broader government in competing with private entities.

The Board has and seeks no access to privileged information or inappropriate influence through the Government in competing with private entities. The statutory governance framework, duties and obligations of Board members and the Code of Conduct applying to Agency staff provide a solid framework to prevent access to and use of privileged information. Clear protocols and processes have been established for the Board and Agency to maintain this position.

www.futurefund.gov.au/about_the_future_fund/legislation

21 SWFs view shareholder ownership rights as a fundamental element of their equity investments' value. If an SWF chooses to exercise its ownership rights, it should do so in a manner that is consistent with its investment policy and protects the financial value of its investments. The SWF should publicly disclose its general approach to voting securities of listed entities, including the key factors guiding its exercise of ownership rights.

The Board is required to have regard to international best practice for institutional investment in determining its approach to corporate governance principles, including in relation to its voting policy.

The Board's approach to the exercise of ownership and voting rights is detailed in its Statement of Investment Policies. The annual report discusses the application of the Board's policy including reporting in aggregate of how voting rights have been exercised.

www.futurefund.gov.au/investment/investment_policies

www.futurefund.gov.au/investment/investment_mandate

Principle**Implementation and reference material**

22 The SWF should have a framework that identifies, assesses, and manages the risks of its operations.

22.1 The risk management framework should include reliable information and timely reporting systems, which should enable the adequate monitoring and management of relevant risks within acceptable parameters and levels, control and incentive mechanisms, codes of conduct, business continuity planning, and an independent audit function.

22.2 The general approach to the SWF's risk management framework should be publicly disclosed.

Consistent with the legislation, Investment Mandates and obligation to have regard to international best practice for institutional investment, the Board and Agency have established a framework for the identification, assessment and management of the risks of its operations, including appropriate reporting and monitoring arrangements. Policies and procedures are in place to support the risk management framework.

The approach to risk management is detailed in the Statement of Investment Policies and the annual report.

www.futurefund.gov.au/investment/investment_policies
www.futurefund.gov.au/annual_reports

23 The assets and investment performance (absolute and relative to benchmarks, if any) of the SWF should be measured and reported to the owner according to clearly defined principles or standards.

The assets and investment performance of the Funds, including performance against the benchmarks established in the Investment Mandate are reported to the responsible Ministers and publicly through the annual report and audited financial statements.

www.futurefund.gov.au/annual_reports

24 A process of regular review of the implementation of the GAPP should be engaged in by or on behalf of the SWF.

The first review of the implementation of the Santiago Principles was undertaken in 2009/10. Further reviews will be published annually with the annual report and via the website.

List of Requirements

The Requirements for Annual Reports approved by the Joint Committee of Public Accounts and Audit requires that Annual Reports include a List of Requirements to help readers identify whether an annual report contains all required information. The following table satisfies this requirement

Ref	Part of Report	Description	Requirement	Location in annual report
A.4		Letter of transmittal	Mandatory	p2
A.5		Table of contents	Mandatory	p1
A.5		Index	Mandatory	p133
A.5		Glossary	Mandatory	p132
A.5		Contact officer(s)	Mandatory	inside cover
A.5		Internet home page address and Internet address for report	Mandatory	inside cover
9.1	Review by Secretary	Review by departmental secretary	Mandatory	p6-9, 10-11
9.2		Summary of significant issues and developments	Suggested	p6-9
9.2		Overview of department's performance and financial results	Suggested	p6-9
9.2		Outlook for following year	Suggested	p6-9
9.3		Significant issues and developments – portfolio	Portfolio departments – suggested	p6-9
10	Departmental Overview	Overview description of department	Mandatory	p3
10.1		Role and functions	Mandatory	p3
10.1		Organisational structure	Mandatory	p30-37
10.1		Outcome and program structure	Mandatory	p131
10.2		Where outcome and program structures differ from PB Statements/PAES or other portfolio statements accompanying any other additional appropriation bills (other portfolio statements), details of variation and reasons for change	Mandatory	Not applicable
10.3		Portfolio structure	Portfolio departments – mandatory	p30-37
11.1	Report on Performance	Review of performance during the year in relation to programs and contribution to outcomes	Mandatory	p12-29
11.1		Actual performance in relation to deliverables and KPIs set out in PB Statements/PAES or other portfolio statements	Mandatory	p12-29
		Performance of purchaser/provider arrangements	If applicable, suggested	Not applicable
11.1		Where performance targets differ from the PBS/PAES, details of both former and new targets, and reasons for the change	Mandatory	Not applicable

Ref	Part of Report	Description	Requirement	Location in annual report
11.1		Narrative discussion and analysis of performance	Mandatory	p12-29
11.1		Trend information	Mandatory	p5
11.1		Significant changes in nature of principal functions/services	Suggested	Not applicable
11.1		Factors, events or trends influencing departmental performance	Suggested	p12-29
11.1		Contribution of risk management in achieving objectives	Suggested	p37, 42
11.1		Social justice and equity impacts	Suggested	Not applicable
11.2		Performance against service charter customer service standards, complaints data, and the department's response to complaints	If applicable, mandatory	Not applicable
11.3		Discussion and analysis of the department's financial performance	Mandatory	p6-9, 12-29
11.3		Discussion of any significant changes from the prior year or from budget.	Suggested	p12-29
11.4		Agency resource statement and summary resource tables by outcomes	Mandatory	p131
11.5		Developments since the end of the financial year that have affected or may significantly affect the department's operations or financial results in future	If applicable, mandatory	Not applicable
	Management Accountability			
12.1	Corporate Governance			
12.1		Statement of the main corporate governance practices in place	Mandatory	p30-42
12.1		Names of the senior executive and their responsibilities	Suggested	p34-37
12.1		Senior management committees and their roles	Suggested	p34, 45
12.1		Corporate and operational planning and associated performance reporting and review	Suggested	p10-11
12.1		Approach adopted to identifying areas of significant financial or operational risk	Suggested	p37-45
12.1		Agency heads are required to certify that their agency comply with the Commonwealth Fraud Control Guidelines.	Mandatory	p45
12.1		Policy and practices on the establishment and maintenance of appropriate ethical standards	Suggested	p11, 40
12.1		How nature and amount of remuneration for SES officers is determined	Suggested	p40-42, 85-86

Ref	Part of Report	Description	Requirement	Location in annual report
12.2	External Scrutiny	Significant developments in external scrutiny	Mandatory	p32
12.2		Judicial decisions and decisions of administrative tribunals	Mandatory	Not applicable
12.2		Reports by the Auditor-General, a Parliamentary Committee or the Commonwealth Ombudsman	Mandatory	Not applicable
12.3	Management of Human Resources	Assessment of effectiveness in managing and developing human resources to achieve departmental objectives	Mandatory	p40
12.3		Workforce planning, staff turnover and retention	Suggested	p40
12.3		Impact and features of enterprise or collective agreements, determinations, common law contracts and AWAs	Suggested	p40
12.3		Training and development undertaken and its impact	Suggested	p40
12.3		Occupational health and safety performance	Suggested	p40
12.3		Productivity gains	Suggested	Not applicable
12.3		Statistics on staffing	Mandatory	p40
12.3		Enterprise or collective agreements, determinations, common law contracts and AWAs	Mandatory	p40
12.3		Performance pay	Mandatory	p40-42
12.4	Assets management	Assessment of effectiveness of assets management	If applicable, mandatory	Not applicable
12.5	Purchasing	Assessment of purchasing against core policies and principles	Mandatory	p42

Ref	Part of Report	Description	Requirement	Location in annual report
12.6	Consultants	The annual report must include a summary statement detailing the number of new consultancy services contracts let during the year; the total actual expenditure on all new consultancy contracts let during the year (inclusive of GST); the number of ongoing consultancy contracts that were active in the reporting year; and the total actual expenditure in the reporting year on the ongoing consultancy contracts (inclusive of GST). The annual report must include a statement noting that information on contracts and consultancies is available through the AusTender website. (Additional information as in Attachment D to be available on the Internet or published as an appendix to the report. Information must be presented in accordance with the pro forma as set out in Attachment D.)	Mandatory	p42
12.7	Australian National Audit Office Access Clauses	Absence of provisions in contracts allowing access by the Auditor-General	Mandatory	Not applicable
12.8	Exempt contracts	Contracts exempt from the AusTender	Mandatory	Not applicable
12.9	Commonwealth Disability Strategy	Report on performance in implementing the Commonwealth Disability Strategy	Mandatory	p40
13	Financial Statements	Financial Statements	Mandatory	p46-112
	Other Information			
14.1		Occupational health and safety (section 74 of the <i>Occupational Health and Safety Act 1991</i>)	Mandatory	p40
14.1		Freedom of Information (subsection 8(1) of the <i>Freedom of Information Act 1982</i>)	Mandatory	p130
14.1		Advertising and Market Research (Section 311A of the <i>Commonwealth Electoral Act 1918</i>) and statement on advertising campaigns	Mandatory	p42
14.1		Ecologically sustainable development and environmental performance (Section 516A of the <i>Environment Protection and Biodiversity Conservation Act 1999</i>)	Mandatory	p42
14.2	Other	Grant programs	Mandatory	Not applicable
14.3		Correction of material errors in previous annual report	If applicable, mandatory	Not applicable
F		List of Requirements	Mandatory	p126-129

Freedom of information

This section addresses the requirements of Section 8 of the *Freedom of Information Act 1982* (FOI Act). Details of the operations and powers of the Board of Guardians and Agency are outlined elsewhere in this report and specified in the *Future Fund Act 2006* and in the *Nation-building Funds Act 2008*.

The Minister for Finance and Deregulation holds certain delegated powers under the Constitution and the *Financial Management and Accountability Act 1997* (and regulations to the Act) that have been delegated to the Chief Executive of the Agency.

Documents maintained by the Board and Agency include working files dealing with policy and administration in the investment of funds and documents on internal administration including personnel, financial and procedural matters.

The primary published document relating to the Board and Agency is the annual report, which is available on the organisation's website. Copies of the Investment Mandates for each fund and investment policies are also available online together with other information on the operations, structure and staffing of the organisation.

Applicants seeking access under the FOI Act should apply in writing to:

FOI Coordinator
Future Fund
Locked Bag 20010
Melbourne VIC 3001

An application of \$30, or a written request that the application fee be remitted pursuant to section 30A (1) of the FOI Act, should accompany requests.

Telephone inquiries should be directed to the Freedom of Information Coordinator on 03 8656 6400, between 9am and 5pm Monday to Friday (except for public holidays or public service holidays).

Authorised officers can make decisions in respect of requests for access to documents under section 23 of the FOI Act. In accordance with section 54 of the FOI Act an applicant may, within 30 days of receiving notification of a decision under the FOI Act, apply to the Chief Executive of the Agency seeking an internal review of a decision to refuse a request. The prescribed fee of \$40 should accompany this application.

Outcome and output framework

The outcome for the Agency is managing and growing public funded investments to meet future financial needs and contribute to the prosperity of future generations of Australians.

This breaks down into two outputs: management of the Future Fund and management of the Nation-building Funds.

Agency resource statement

	Actual Available Appropriations for 2009/10 \$'000	Payments Made 2009/10 \$'000	Balance Remaining
Special Accounts			
Opening balance			-
Non-Appropriation receipts to Special Accounts	288,647	288,647	-
Total Resourcing and Payments	288,647	288,647	-

The Future Fund does not receive any annual appropriations. Its outputs are funded, through the *Future Fund Act 2006*, as payments from the Future Fund Special Account. The Board invests amounts standing to the credit of the Future Fund Special Account, and the outputs are funded from the redemption of investments.

The receipts identified in the above table are sourced from the Future Fund Special Account: Investment of Public Money.

Resources for outcome

Outcome 1: Managing and growing publicly funded investments to meet future financial needs and contribute to the prosperity of future generations of Australians

	Budget 2009/10 \$'000	Actual Expenses 2009/10 \$'000	Variation \$'000
Program 1.1 Management of the investment of the Future Fund			
Advances from the Special Account	26,097	23,648	2,449
Total for Program 1.1	26,097	23,648	2,449
Program 1.2 Management of the investment of the Building Australia Fund, Education Investment Fund and Health and Hospitals Fund			
Advances from Special Account	781	943	(162)
Total for Program 1.2	781	943	(162)
Total for Outcome 1	26,878	24,591	2,287

Average staffing level (number) 65

Abbreviations

AASB	Australian Accounting Standards Board
AO	Officer of the Order of Australia
AM	Member of the Order of Australia
ANAO	Australian National Audit Office
ASIC	Australian Securities and Investments Commission
ATO	Australian Taxation Office
CPGs	Commonwealth Procurement Guidelines
CPI	Consumer Price Index
FFMA	Future Fund Management Agency
FMA Act	<i>Financial Management and Accountability Act 1997</i>
FMO	Finance Minister's Orders
FOI Act	<i>Freedom of Information Act 1982</i>
GST	Goods and Services Tax
HEEF	Higher Education Endowment Fund
PSA	<i>Public Service Act 1999</i>
RBA	Reserve Bank of Australia
VWAP	Volume Weighted Average Price

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