

Investment results

ARIA finished the 2006/07 year with over \$18 billion funds under management and over 325 578 members in the CSS, PSS and PSSap.

CSS and PSS Default Fund

The CSS Default Fund posted a net return of 16.5% and the PSS Default Fund posted a net return of 17.7%, the fourth consecutive year of double digit returns. This performance well exceeded the long-term target of at least 7% per annum.

The CSS has achieved an average performance over the past three years of 14.5% per annum, a five year average return of 12.0% and a 10 year average of 9.1% per annum.

For the PSS its three year average performance was 14.9% per annum, five year average return was 12.2% and for 10 years was 9.1% per annum.

CSS and PSS Cash Investment Option

The CSS Cash Investment Option posted a net return of 5.4%, which is in line with its strategic investment objective. The PSS Cash Investment Option also posted a net return of 5.4%, which is also in line with its objective.

PSSap

The PSSap's investment choice options all performed well in 2006/07. The Trustee Choice default fund achieved 16.7% which was well above its long-term target return of no less than 7% per annum.

The other three pre-mixed, diversified investment options also performed particularly well with the Aggressive Option returning 20.3%, followed by the Balanced Option 12.2% and the Conservative Option 9.3%.

Major events and developments

The reforms to superannuation announced by the government in the 2006/07 Budget have now come into effect. The 'Better Super' reforms involved significant changes to our scheme administrator's systems and communication to members in relation to the changes. ARIA and its administrator were pleased with the successful implementation of the changes.

Another key development for 2006/07 was the change to the CSS and PSS Earning Rate Policy allowing ARIA to distribute Fund earnings more equitably among members who leave the scheme and those who stay during a period of negative earnings. The next step in this process is to move to monthly allocation of Fund earnings, whether positive or negative. To do this, we need to allocate unallocated Fund earnings to members' accounts. We will commence this process during 2007/08.

Significant scheme changes were announced as part of the 2007/08 Budget. These will affect all members of the CSS and PSS once they are implemented (scheduled for 2008). ARIA will liaise with the government and other stakeholders on the impact of these proposals during 2007/08.

In the 2005/06 annual report we advised that there were errors in the published Exit Rates which ranged between 0.5% up to 5.5%. This resulted in an understatement of investment earnings for members taking their benefit in that year, for example taking a lump sum or certain pensions. All affected members

have been contacted and the majority of cases have now been processed. Due to the complexity involved in some calculations, as well as members not responding to requests for information, some cases remain to be processed. All additional benefit payments made to members who have been affected include interest for the period, through to the date of the payment.

ARIA's investment team changed in 2006/07 with the appointment of Ms Alison Tarditi as Chief Investment Officer (CIO) in June 2007, following the resignation of the previous CIO, Mr André Morony in late 2006. Mr Greg Bayles was also appointed as ARIA's alternative investments portfolio manager.

The executive team was also enhanced with the announcement that Mr Paul Watson would join ARIA as Deputy Chief Executive Officer late in July 2007.

Investment and corporate governance

ARIA is at the forefront of fiduciary, investment and corporate governance, recognising that poor environmental, corporate governance and social practices can lead to a decline in investment value as much as financial risk can.

ARIA continues to manage risk actively through the casting of proxy votes in the Australian and international companies in which it invests and also through Regnan, the Governance Advisory Service it assisted to create for the primary purpose of proactive engagement with investee companies.

Evolving from the former BT Governance Advisory Service (GAS), Regnan was established by ARIA and seven other major institutional investors in May 2007.

Regnan is Australia's only investment risk management service which focuses on an engagement process to meet the oversight needs of institutional investors. It addresses portfolio exposure to environmental, social and governance risks by directly engaging with companies and performing specialist research and analysis.

In December 2006 ARIA became a signatory to the United Nations Principles for Responsible Investment (PRI) and is actively committed to ensuring that all investment activities are undertaken consistently with these principles.

Following the positive results of these initiatives, ARIA will continue to act as a responsible corporate citizen and will embrace its proxy voting responsibilities and increase market and public awareness of governance issues to raise standards, minimising the financial risk to our members.

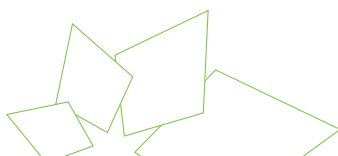
Administration

ARIA and its administrator, ComSuper will work together to improve member services. ARIA conducts regular reviews of the effectiveness of all aspects of its scheme administrator.

In 2006/07 our administrator has been focused on:

- > improving customer service for both members and employers
- > enhancing systems as a result of the 'Better Super' changes; and
- > implementing ARIA's Fund allocation project and related changes.

In the 2007/08 Budget, the Minister for Finance and Administration announced additional funding for ComSuper, over a number of years, to allow it to modernise IT systems and meet ongoing regulatory requirements.



Regulatory environment

This year has been marked by a number of significant regulatory and policy initiatives. Legislative amendments include:

- > The *Superannuation Legislation Amendment (Superannuation Safety and Other Measures) Act 2006* which amended the CSS Act to permit actual earnings (including negative earnings) to be applied to member accounts, providing ARIA with greater capacity to equitably distribute Fund earnings between members who leave the scheme and those who stay.
- > The 28th Amending Deed for the PSS (21 June 2007) which amended the PSS Rules to permit actual earnings (including negative earnings) to be applied to member accounts. This change was consistent with the changes made to the CSS Act.
- > The 1st Amending Deed for the PSSap (25 July 2006) which made a number of technical amendments in the areas of benefit payments, roll-overs and transfers and portability provisions, as well as amendments consequent on the establishment of ARIA.

Future directions

2007/08 will be another busy year for ARIA. We will continue to work with the Department of Finance and Administration and other key stakeholders to ensure that the Australian Government is able to provide its employees with affordable, well structured superannuation arrangements, with the aim of achieving consistently good returns.

There are a number of significant projects on the agenda for 2007/08 including the finalisation of fund allocation to members and the practical implementation of the major changes to CSS and PSS announced in the 2007 Budget.

We will collaborate with our administrator, ComSuper, to define the requirements for systems to replace those currently used for the CSS and PSS. These systems will service members and employers and so continue to meet their needs and requirements into the future.



Steve Gibbs
Chief Executive Officer