

**Australian Ethical Smaller Companies Trust (AEST)**  
ARSN 089 919 175

**Annual Financial Report for the year ended 30 June 2014**

# **Australian Ethical Smaller Companies Trust**

## **Annual Financial Report for the year ended 30 June 2014**

<b>Contents</b>	<b>Page</b>
<b>Directors' Report</b>	<b>1</b>
<b>Statement of Profit or Loss and Other Comprehensive Income</b>	<b>3</b>
<b>Statement of Financial Position</b>	<b>4</b>
<b>Statement of Changes in Equity</b>	<b>5</b>
<b>Statement of Cash Flows</b>	<b>6</b>
<b>Notes to the Financial Statements</b>	<b>7</b>
<b>Directors' Declaration</b>	<b>23</b>
<b>Lead Auditor's Independence Declaration</b>	<b>24</b>
<b>Independent Auditor's Report</b>	<b>25</b>

## Australian Ethical Smaller Companies Trust

### Directors' Report For the year ended 30 June 2014

Australian Ethical Investment Limited, the "Responsible Entity" of the Australian Ethical Smaller Companies Trust ("AEST" or "the Scheme") presents its directors' report together with the audited financial statements of the Scheme for the year ended 30 June 2014 and the accompanying independent auditor's report.

#### Responsible Entity

Australian Ethical Investment Limited (ABN 47 003 188 930) serves as the Responsible Entity for the Scheme. The registered office and principal place of business for the Responsible Entity is:

Registered office:  
Trevor Pearcey House (Block E)  
Traeger Court, 34 Thynne Street  
Bruce ACT 2617

Principal place of business:  
Level 8, 130 Pitt St  
Sydney,  
NSW 2000

The following persons were directors of Australian Ethical Investment Limited during the whole of the financial year and up to the date of this report unless otherwise indicated:

Phil Vernon  
Kate Greenhill  
Stephen Gibbs  
Mara Bun  
Tony Cole  
Stephen Newnham (ceased 26 July 2013)  
André Morony (ceased 20 November 2013)

#### Principal activities and state of affairs

The principal activity of the Scheme is to pool investors' savings to invest in diversified portfolios of securities, in accordance with the investment objectives and guidelines as set out in the current Product Disclosure Statement and within the provisions of the Scheme's constitution. The constitution of the Scheme authorises investments in a range of assets, which may include listed and unlisted Australian equity investments, with a bias towards smaller capitalisation stocks listed on the ASX. Investments are sought to pursue the goal of a just and sustainable society and the protection of the natural environment as well as providing unitholders (the Scheme investors) with a competitive financial return.

There were no significant changes in the nature of the Scheme's principal activities during the year and there were no significant changes in the Scheme's state of affairs.

#### Review of operations

##### Overview

The underlying fundamentals of the Scheme are consistent with those set out in the Scheme's Product Disclosure Statement dated 30 June 2014.

##### Results

Total return is the percentage change of a unitholder's financial interest in the Scheme assuming all distributions are reinvested in the Scheme. These returns are calculated in accordance with FSC Standard 6 Product Performance-Calculation of Return. The Scheme achieved a total return for the retail and wholesale class of 16.5% (2013: 22.4%) and 18.1% (2013: 24.0%) respectively for the financial year.

## Australian Ethical Smaller Companies Trust

### Directors' Report For the year ended 30 June 2014

#### Distributions paid and/or payable

Distributions paid and/or payable by the Scheme during the year are shown in the accompanying Statement of Profit or Loss and Other Comprehensive Income.

The Scheme paid interim distributions totalling 2.62 cents per unit (2013: 3.38 cents per unit) and year end distributions totalling 16.73 cents per unit (2013: 6.48 cents per unit).

#### Net Assets

The value of the Scheme's net assets attributable to unitholders as at 30 June 2014 was \$304,597,156 (30 June 2013: \$257,808,814).

#### **Likely developments**

The Responsible Entity continually reviews the Scheme and depending on that review may, during the course of the financial year, make decisions to change the offerings of products to investors. The Responsible Entity plans to continue to invest in line with the strategy set out in the Product Disclosure Statement.

#### **Events occurring after the reporting date**

The Australian and international markets remain relatively volatile, and this impacts the valuation of the Scheme's investment portfolio. As the investments are measured at their 30 June 2014 fair values in the financial report, any volatility in values subsequent to the balance date is not reflected in the Statement of Profit or Loss and Other Comprehensive Income or the Statement of Financial Position. However the volatility in value of investments has been reflected in the current unit price.

Except as outlined above, during the period between the end of the financial year and the date of this report, there were no items, transactions or events of a material and unusual nature likely in the opinion of the Responsible Entity, to affect significantly the operations of the Scheme, the results of those operations, or the state of affairs of the Scheme in future financial years.

#### **Indemnities and insurance premiums for the Responsible Entity and auditors**

No insurance premiums are paid for out of the assets of the Scheme for insurance cover provided to the Responsible Entity, its officers or auditor of the Scheme. Where the Responsible Entity acts in accordance with the Scheme's constitution and the law, it is generally entitled to an indemnity out of the assets of the Scheme against losses incurred while acting on behalf of the Scheme. The auditor of the Scheme is not indemnified out of the assets of the Scheme.

#### **Related party disclosures**

Fees paid to the Responsible Entity and its associates out of Scheme assets is shown in note 15 of the attached financial statements.

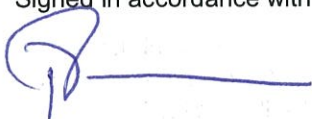
#### **Environmental regulation**

The operations of the Scheme are not subject to any particular or significant environmental regulations under Commonwealth, State or Territory legislation.

#### **Auditor's declaration**

The auditor's independence declaration is included on page 24 of the annual report and forms part of the Directors report for the financial year ended 30 June 2014.

Signed in accordance with a resolution of the Board of Directors of Australian Ethical Investment Limited.



Phil Vernon  
Managing Director  
Australian Ethical Investment Limited  
26 September 2014

**Australian Ethical Smaller Companies Trust**

**Statement of Profit or Loss and Other Comprehensive Income for the year ended 30 June 2014**

	Note	2014 \$	2013 \$
<b>Investment income</b>			
Interest income	4	484,310	575,104
Dividend income	5	9,180,564	8,405,102
Net change in fair value of financial assets	6	40,852,568	46,666,372
Other income		-	124,335
<b>Net investment income</b>		<u>50,517,442</u>	<u>55,770,913</u>
<b>Operating expenses</b>			
Management fees	15	5,403,229	4,408,411
Administration fees	15	817,053	564,474
Other Expenses		-	102,075
Amortisation	10	196,349	199,312
<b>Operating expenses before finance costs</b>		<u>6,416,631</u>	<u>5,274,272</u>
<b>Profit from operating activities</b>		44,100,811	50,496,641
<b>Finance costs</b>			
Distributions paid and payable to unitholders of the Scheme	12	(13,291,627)	(5,917,167)
<b>Change in net assets attributable to unitholders (total comprehensive income)</b>	3	<u>30,809,184</u>	<u>44,579,474</u>

The accompanying notes form part of these financial statements.

**Australian Ethical Smaller Companies Trust**

**Statement of Financial Position as at 30 June 2014**

	Note	2014 \$	2013 \$
<b>Assets</b>			
Cash and cash equivalents	7	23,581,100	23,292,420
Trade and other receivables	8	2,725,383	1,394,397
Financial assets held at fair value through profit and	9	293,043,351	237,062,969
Other assets	10	278,161	474,510
<b>Total assets</b>		<b>319,627,995</b>	<b>262,224,296</b>
 <b>Liabilities</b>			
Trade and other payables	11	3,072,313	456,565
Distribution payable	12	11,958,526	3,958,917
<b>Total liabilities</b>		<b>15,030,839</b>	<b>4,415,482</b>
 <b>Net assets attributable to unitholders</b>	 3	 <b>304,597,156</b>	 <b>257,808,814</b>
 Represented by:			
Net assets attributable to unitholders at redemption price		317,268,568	262,675,002
Amounts payable to unitholders of the scheme		(11,958,526)	(3,958,917)
Adjustments arising from different unit pricing and accounting valuation		(712,886)	(907,271)
 <b>Total net assets attributable to unitholders</b>	 3	 <b>304,597,156</b>	 <b>257,808,814</b>

The accompanying notes form part of these financial statements.

**Australian Ethical Smaller Companies Trust**

**Statement of Changes in Equity for the year ended 30 June 2014**

The Scheme's net assets attributable to unitholders are classified as a liability under AASB 132 '*Financial Instruments: Presentation*'. As such the Scheme has no equity and no items of changes in equity at the start and end of the year.

The accompanying notes form part of these financial statements.

**Australian Ethical Smaller Companies Trust**

**Statement of Cash Flows for the year ended 30 June 2014**

	2014 \$	2013 \$
<b>Cash flows from operating activities</b>		
Interest received	438,534	575,104
Dividends received	9,481,502	8,416,962
Other income received	-	217,617
Expenses paid	<u>(6,034,347)</u>	<u>(5,615,116)</u>
<b>Net cash provided by operating activities</b>	<b>14     3,885,689</b>	<b>3,594,567</b>
<b>Cash flows from investing activities</b>		
Proceeds from sale of investments	87,136,222	102,236,359
Purchase of investments	<u>(101,450,123)</u>	<u>(89,783,011)</u>
Purchase of capital projects	-	(61,283)
<b>Net cash (used in)/provided by investing activities</b>	<b>(14,313,901)</b>	<b>12,392,065</b>
<b>Cash flows from financing activities</b>		
Proceeds from issue of units	29,585,256	11,588,279
Payment of redemption of units	<u>(17,459,514)</u>	<u>(22,285,321)</u>
Distributions paid to unitholders	<u>(1,408,850)</u>	<u>(1,325,199)</u>
<b>Net cash provided by/(used in) financing activities</b>	<b>· 10,716,892</b>	<b>(12,022,241)</b>
Net increase in cash and cash equivalents	288,680	3,964,391
Cash and cash equivalents at 1 July	<u>23,292,420</u>	<u>19,328,029</u>
Cash and cash equivalents at 30 June	<b>7     23,581,100</b>	<b>23,292,420</b>

The accompanying notes form part of these financial statements.



## Australian Ethical Smaller Companies Trust

### Notes to the Financial Statements for the year ended 30 June 2014

#### Note 1 - Statement of significant accounting policies

The Australian Ethical Smaller Companies Trust ("AEST" or the "Scheme") is a registered managed investment scheme under the Corporations Act 2001. The Scheme was constituted on 2 November 1999. The Scheme will terminate on 1 November 2079 unless terminated earlier in accordance with the provisions of the Scheme constitution. The Scheme is domiciled in Australia and is a for profit entity. The financial statements of the Scheme are for the year ended 30 June 2014.

##### *Statement of compliance*

The financial statements are general purpose financial statements which have been prepared in accordance with Australian Accounting Standards (AASBs) adopted by the Australian Accounting Standards Board (AASB) and the Corporations Act 2001. The financial statements of the Scheme complies with International Financial Reporting Standards (IFRSs) and interpretations adopted by the International Accounting Standards Board (IASB).

The financial statements were approved by the Board of Directors of the Responsible Entity on 24 September 2016.

##### **Basis of preparation**

These financial statements are presented in Australian dollars and are prepared on the historical cost basis with the exception of financial assets designated at fair value through profit and loss and derivatives which are measured at fair value, and receivables and payables which are measured at amortised cost.

The preparation of financial statements in conformity with AASBs requires management to make judgments, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses and the disclosure of contingent assets and liabilities. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the result of which form the basis of making the judgments about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates. These accounting policies have been applied consistently.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised and in any future periods affected.

##### **Change in accounting policies**

The Scheme has adopted the following standards and amendments for the 30 June 2014 reporting period:

(a) AASB 13 *Fair Value Measurement* and AASB 2011-8 *Amendments to Australian Accounting Standards arising from AASB 13* (effective for accounting periods beginning on or after 1 January 2013)

AASB 13 aims to improve consistency and reduce complexity by providing a precise definition of fair value and a single source of fair value measurement and disclosure requirements for use across Australian Accounting Standards. The standard does not extend the use of fair value accounting but provides guidance on how it should be applied where its use is already required or permitted by other Australian Accounting Standards.

Previously the fair value of financial liabilities (including derivatives) was measured on the basis that the financial liability would be settled or extinguished with the counterparty. The adoption of AASB 13 has clarified that fair value is an exit price notion, and as such, the fair value of financial liabilities should be determined based on a transfer value to a third party market participant. As a result of this change, the fair value of derivative liabilities has changed on transition to AASB 13, largely due to incorporating credit risk into the valuation.

On adoption of the standard, the Scheme has not changed its valuation inputs for listed financial assets or liabilities and continues to utilise quoted bid and ask prices. There has been no impact to the net gains/(losses) on financial instruments held at fair value through profit or loss.

(b) AASB 2012-2 *Amendments to Australian Accounting Standards - Disclosures - Offsetting Financial Assets and Financial Liabilities* (effective for accounting periods beginning on or after 1 January 2013)

AASB 2012-2 requires additional disclosures to enable users of financial statements to evaluate the effect or the potential effects of netting arrangements, including rights of set-off associated with an entity's recognised financial assets and recognised financial liabilities, on the entity's financial position. The amendments did not have any impact on the Scheme's financial position or performance.

## Australian Ethical Smaller Companies Trust

### Notes to the Financial Statements for the year ended 30 June 2014

#### Note 1 - Statement of significant accounting policies - continued

(c) AASB 10 *Consolidated Financial Statements*, AASB 11 *Joint Arrangements*, AASB 12 *Disclosure of Interests in Other Entities*, AASB 127 (revised 2011) *Separate Financial Statements* and AASB 128 (revised 2011) *Investments in Associates and Joint Ventures* (effective for accounting periods beginning on or after 1 January 2013)

The Scheme has early adopted AASB 2013-5 *Amendments to Australian Accounting Standards - Investment Entities* (effective for accounting periods beginning on or after 1 January 2014) which makes amendments to AASB 10, AASB 12 and AASB 127 (the "Amendments").

AASB 10 *Consolidated financial statements* and Amendments to AASB 10:

The objective of AASB 10 is to establish principles for the presentation and preparation of consolidated financial statements. It sets out how to apply the principle of control to identify whether an investor controls an investee and therefore must consolidate the investee. It also sets out the accounting requirements for the preparation of consolidated financial statements. The amendments to AASB 10 define an investment entity and introduce an exemption from the consolidation requirements for investment entities. The adoption of these standards has had no impact on the Scheme.

##### *Investment entity*

The Scheme has multiple unrelated unitholders and holds multiple investments directly or indirectly. Ownership interests in the interfunding investments are in the form of units which are classified as debt in accordance with AASB 132 and which are exposed to variable returns from changes in the fair value of the Scheme's net assets. The Scheme has been deemed to meet the definition of an investment entity per AASB 10 as the following conditions exist:

- (i) The Scheme has obtained funds for the purpose of providing unitholders with investment management services;
  - (ii) The Scheme's business purpose, which is communicated directly to unitholders, is investing solely for returns from capital appreciation and investment income; and
  - (iii) The performance of investments made through the Scheme are measured and evaluated on a fair value basis.
- The Scheme meets the typical characteristics of an investment entity.

AASB 12 *Disclosure of interests in other entities* and Amendments to AASB 12:

The standard requires entities to disclose significant judgements and assumptions made in determining whether the entity controls, jointly controls, significantly influences or has some other interests in other entities. Entities will also be required to provide more disclosures around certain 'structured entities'. The amendments also introduce new disclosure requirements related to investment entities. Adoption of the standard has impacted certain disclosures in the Scheme's annual financial report, but has had no impact to the Scheme's financial position or results of operations.

AASB 127 (revised 2011) *Separate financial statements* and Amendments to AASB 127:

The objective of the standard is to prescribe the accounting and disclosure requirements when an entity prepares separate financial statements. The amendments require an investment entity as defined in AASB 10 to present separate financial statements as its only financial statements in the case where it measures all of its subsidiaries at fair value through profit or loss and to disclose that fact. The adoption of this standard has had no impact on the Scheme.

AASB 11 *Joint arrangements* and AASB 128 (revised 2011) *Investments in Associates and Joint Ventures* and related amendments have also been adopted, however, these standards have had no impact on the scheme.

There are no other standards, interpretations or amendments to existing standards that are effective for the first time for the financial year beginning 1 July 2013 that would be expected to have a material impact on the Scheme.

#### **Accounting policies**

##### **(a) Cash and cash equivalents**

Cash and cash equivalents comprise cash on hand, deposits held at call with financial institutions or highly liquid investments of original maturity of three months or less.

##### **(b) Financial instruments**

Financial instruments comprise of investments held at fair value through profit or loss, loans held at amortised cost, trade and other receivables, cash and cash equivalents and other payables.

## Australian Ethical Smaller Companies Trust

### Notes to the Financial Statements for the year ended 30 June 2014

#### Note 1 - Statement of significant accounting policies - continued

##### *Recognition and initial measurement*

A financial instrument is recognised when the Scheme becomes a party to the contractual provisions of the instrument. Regular way purchase and sales of financial assets are accounted for at trade date (i.e. the date the Scheme commits itself to purchase or sell the asset).

Financial assets and liabilities at fair value through profit or loss are recognised initially at fair value, with transaction costs recognised in the Statement of Profit or Loss and Other Comprehensive Income. Financial assets and liabilities not at fair value through profit or loss are initially recognised at fair value plus any directly attributable transaction costs.

##### *Derecognition*

The Scheme derecognises financial assets when the contractual rights to the cash flows from the financial assets expire or it transfers the financial assets and the transfer qualifies for derecognition in accordance with AASB 139 *Financial Instruments: Recognition and Measurement*.

A financial liability is derecognised when the obligation specified in the contract is discharged, cancelled or expired.

##### *Classification*

Financial assets and financial liabilities held at fair value through profit or loss are classified as either held for trading or are designated at fair value through profit or loss. Financial assets and liabilities held for trading include derivative financial instruments. Financial assets and liabilities designated at fair value through profit or loss include equity securities, investments in unit trusts and fixed interest securities.

##### *Measurement*

Subsequent to initial recognition, all instruments classified at fair value through profit or loss are measured at fair value with changes in their fair value recognised in the Statement of Profit or Loss and Other Comprehensive Income. All other financial instruments are carried at amortised cost using the effective interest rate method less any recognised impairment.

Financial liabilities arising from redeemable units issued by the Scheme are carried at the redemption amount representing the unitholders' rights to the residual interest in the Scheme's assets, effectively the fair value at the reporting date.

##### *Fair value measurement principles*

The Scheme can invest into a variety of assets, including cash, equities, fixed and floating rate interest securities, unit trusts and derivative contracts. Generally, valuation information is obtained from third party industry standard service providers to ensure that the most recent security prices are obtained. The prices used to value investments include, but are not limited to:

- independent prices obtained for each security;
- quoted 'bid' prices on long securities and quoted 'ask' prices on securities sold short;
- redemption prices published by the relevant Responsible Entity, for investments into unlisted unit trusts.

For certain investments, prices cannot be obtained from the above sources. In these instances, valuations obtained from service providers are estimated through the use of valuation models which are consistent with accepted industry practice and incorporate the best available information regarding assumptions that market participants would use when pricing the assets or liabilities. Irrespective of the method used by third party industry standard service providers to obtain valuations, prices achieved in actual transactions may be different.

##### *Impairment of financial assets held at amortised cost*

Financial assets other than those at fair value through profit or loss are assessed for indicators of impairment at the end of each reporting period. Financial assets are considered to be impaired when there is objective evidence that the estimated future cash flows are less than the carrying amount.

##### *Offsetting*

Financial assets and liabilities are offset and the net amount reported in the Statements of Financial Position when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

## Australian Ethical Smaller Companies Trust

### Notes to the Financial Statements for the year ended 30 June 2014

#### Note 1 - Statement of significant accounting policies - continued

##### *Derivative financial instruments*

In accordance with the Investment Mandate, the Scheme may invest in derivative financial instruments to gain or hedge exposure to equities, interest rates or foreign currencies. Derivative financial instruments are recognised initially at cost. Subsequent to initial recognition, derivative financial instruments are stated at fair value. The gain or loss on remeasurement to fair value is recognised immediately in the Statement of Profit or Loss and Other Comprehensive Income.

##### **(c) Trade and other receivables**

Receivables are carried at amortised cost and may include accrued income and other receivables such as Reduced Input Tax Credits (RITC).

##### **(d) Payables**

Payables are carried at amortised cost and may include amounts for unsettled purchases, accrued expenses and other payables such as GST and redemption monies owing by the Scheme. Unsettled purchases are amounts due to brokers for securities purchased that have not been paid at reporting date. Trades are recorded on trade date and normally settle within three business days. Accrued expenses include management fees payable.

##### **(e) Distributions paid and payable**

In accordance with the Constitution, the Scheme fully distributes its net income to unitholders. The distributions are determined by reference to the net taxable income of the Scheme. Distributable income includes capital gains arising from the disposal of investments. Unrealised gains and losses are transferred to net assets attributable to unitholders and are not assessable or distributable until realised. Realised capital losses are not distributed to unitholders but are retained to be offset against any future realised capital gains. Distributions paid and payable to unitholders are recognised in the Statement of Profit or Loss and Comprehensive Income as 'Finance costs'. Distributions paid are included in the Statement of Cash Flows as 'Net cash flows (used in)/ provided by financing activities'.

##### **(f) Change in net assets attributable to unitholders**

Change in net assets attributable to unitholders may consist of realised net capital losses and unrealised increments and decrements arising from fluctuations in the value of investments. They are included in the determination of distributable income when assessable for taxation purposes.

##### **(g) Revenue**

###### *Interest income*

Interest income is recognised in the Statement of Profit or Loss and Other Comprehensive Income as it accrues using the effective interest rate method. Interest income is recognised on a gross basis, including withholding tax, if any.

###### *Dividend income*

Dividend income relating to exchange-traded equity investments is recognised in the Statement of Profit or Loss and Other Comprehensive Income on the ex-dividend date. Income distributions from other managed investment schemes are recognised in the Statement of Comprehensive Income as dividend income on a present entitlement basis.

In some cases, the Scheme may receive or choose to receive dividends in the form of additional shares rather than cash. In such cases the Scheme recognises the dividend income for the amount of the dividend alternative with the corresponding debit treated as an additional investment.

##### **(h) Goods and Services Tax (GST)**

The Scheme qualifies for Reduced Input Tax Credits (RITC's) at a rate of between 55% to 75% depending on the service.

Revenues, expenses and assets are recognised net of the amount of GST, except where the amount of GST incurred is not recoverable from the Australian Tax Office (ATO). In these circumstances the GST is recognised as part of the cost of acquisition of the asset or as part of an item of the expense.

Receivables and payables in the Statement of Financial Position are shown inclusive of GST. The net amount of GST recoverable from the ATO is included in receivables in the Statement of Financial Position.

Cash flows are presented in the Statement of Cash Flows on a gross basis, except for the GST component of investing and financing activities, which are disclosed as operating cash flows.

## Australian Ethical Smaller Companies Trust

### Notes to the Financial Statements for the year ended 30 June 2014

#### Note 1 - Statement of significant accounting policies - continued

##### (i) Income tax

Under current income tax legislation the Scheme is not liable to pay income tax as the net income of the Scheme is assessable in the hands of the beneficiaries (the unitholders) who are 'presently entitled' to the income of the Scheme. There is no income of the Scheme to which the unitholders are not presently entitled and additionally, the Scheme's Constitution requires the distribution of the full amount of the net income of the Scheme to the unitholders each period.

As a result, deferred taxes have not been recognised in the financial statements in relation to differences between the carrying amounts of assets and liabilities and their respective tax bases, including taxes on capital gains which could arise in the event of a sale of investments for the amount at which they are stated in the financial statements. In the event that taxable gains are realised by the Scheme, these gains would be included in the taxable income that is assessable in the hands of the unitholders as noted above.

Realised capital losses are not distributed to unitholders but are retained within the Scheme to be offset against any realised capital gains. The benefit of any carried forward capital losses are also not recognised in the financial statements. If in any period realised capital gains exceed realised capital losses, including those carried forward from earlier periods and eligible for offset, the excess is included in taxable income that is assessable in the hands of unitholders in that period and is distributed to unitholders in accordance with the requirements of the Scheme's Constitution.

##### (j) Net assets attributable to unitholders

In accordance with AASB 132, unitholders' funds are classified as a financial liability and disclosed as such in the Statement of Financial Position, being referred to as 'Net assets attributable to unitholders'. The units can be put back to the Scheme at any time for cash equal to the proportionate share of the Scheme's net asset values. The value of redeemable units is measured at the redemption amount that is payable (based on the redemption unit price) at the Statement of Financial Position date if unitholders exercised their right to put the units back to the Scheme. Changes in the value of this financial liability are recognised in the Statement of Profit or Loss and Other Comprehensive Income.

##### (k) Expenses

All expenses, including management fees, are recognised in the profit or loss on an accruals basis.

##### (l) Foreign currency transactions and balances

Foreign currency transactions are translated to Australian currency at the rates of exchange ruling at the date of the transactions. Assets and liabilities denominated in foreign currency, are translated at the rates of exchange ruling at the reporting date. Unrealised foreign exchange gains or losses, arising on translation of assets and liabilities denominated in foreign currency at reporting date, are recognised as part of the 'Net change in fair value of investments' in the Statement of Profit or Loss and Comprehensive Income. Realised gains and losses on amounts denominated in foreign currencies are also brought to account as part of 'Net change in fair value of investments' in the Statement of Profit or Loss and Other Comprehensive Income and as part of 'Other income received' in the Statement of Cash Flows.

##### (m) Capitalised software

The amortisable amount of all fixed assets are amortised over their estimated useful lives to the entity commencing from the time the asset is held ready for use.

A straight line basis of amortisation has been adopted for capitalised software. The amortisation rates used for each class of assets are:

Software	3 - 5 years
----------	-------------

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each reporting date.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount.

Gains and losses on disposals are determined by comparing proceeds with the carrying amount. These gains and losses are included in the Statement of Profit or Loss and Other Comprehensive Income. When re-valued assets are sold, amounts included in the revaluation reserve relating to that asset are transferred to retained earnings.

## Australian Ethical Smaller Companies Trust

### Notes to the Financial Statements for the year ended 30 June 2014

#### Note 1 - Statement of significant accounting policies - continued

##### (n) Comparative figures

When required by Accounting Standards, comparative figures have been adjusted to conform to changes in presentation for the current financial year.

##### (o) Standards and interpretations in issue not yet adopted

Certain new accounting standards and interpretations have been published that are not mandatory for the 30 June 2014 reporting period and have not yet been early adopted by the Scheme. The assessment of the impact of these new standards (to the extent relevant to the Scheme) and interpretations is set out below:

*AASB 9 Financial Instruments (2009 or 2010 version), AASB 2009-11 Amendments to Australian Accounting Standards arising from AASB 9, AASB 2010-7 Amendments to Australian Accounting Standards arising from AASB 9 (December 2010), AASB 2012-6 Amendments to Australian Accounting Standards - Mandatory Effective Date of AASB 9 and Transition Disclosures and AASB 2013-9 Amendments to Australian Accounting Standards Conceptual Framework, Materiality and Financial Instruments (effective from 1 January 2017).*

AASB 9 Financial Instruments addresses the classification, measurement and derecognition of financial assets and financial liabilities. It has also now introduced revised rules around hedge accounting. The standard is available for early adoption but management does not expect this to have a significant impact on the recognition and measurement of the Scheme's financial instruments as they are carried at fair value through profit or loss. Further, the derecognition rules have not been changed from the previous requirements, and the Scheme does not apply hedge accounting.

The Scheme has not yet decided when to adopt AASB 9.

**Australian Ethical Smaller Companies Trust**

**Notes to the Financial Statements for the year ended 30 June 2014**

**Note 2 - Issued units**

Each unit represents a right to an individual share in the Scheme per the Constitution.

	2014	2013
	Units	Units
<i>Retail Class</i>		
On issue at beginning of year	130,083,076	135,509,135
Issued	11,513,312	5,436,543
Redeemed	(5,767,115)	(10,862,602)
On issue at year end	<u>135,829,273</u>	<u>130,083,076</u>

<i>Wholesale Class</i>		
On issue at beginning of year	16,128,558	14,813,224
Issued	5,390,361	3,598,967
Redeemed	(2,938,445)	(2,283,632)
On issue at year end	<u>18,580,474</u>	<u>16,128,558</u>

**Note 3 - Net assets attributable to unitholders**

The Scheme manages its net assets attributable to unitholders as capital, notwithstanding net assets attributable to unitholders are classified as a liability.

The objective of the Scheme is to provide unitholders with returns in accordance with the Product Disclosure Statement. The Scheme aims to deliver income and capital appreciation through investing in equities. The Scheme is not subject to any externally imposed capital requirements.

	2014	2013
	\$	\$
Opening balance	257,808,814	220,372,677
Issued	29,555,504	11,588,279
Distributions reinvested	3,883,168	3,553,705
Redeemed	(17,459,514)	(22,285,321)
Change in net assets attributable to unitholders	30,809,184	44,579,474
Total net assets attributable to unitholders	<u>304,597,156</u>	<u>257,808,814</u>

**Note 4 - Interest income**

Cash and cash equivalents	484,310	575,104
	<u>484,310</u>	<u>575,104</u>

**Note 5 - Dividend income**

Dividend income from securities designated at FVTPL	9,180,564	8,405,102
	<u>9,180,564</u>	<u>8,405,102</u>

**Note 6 - Gains/(losses) on Financial assets**

Unrealised gain arising on financial assets designated as at FVTPL:		
Equity investments and units trusts	31,065,040	35,703,357
Realised gain arising on the disposal of financial assets		
Gain on the disposal of investments	9,787,528	11,015,415
Net loss on the disposal of foreign currency options	-	(52,400)
	<u>9,787,528</u>	<u>10,963,015</u>
Net change in fair value of financial assets	<u>40,852,568</u>	<u>46,666,372</u>

**Australian Ethical Smaller Companies Trust**

**Notes to the Financial Statements for the year ended 30 June 2014**

**Note 7 - Cash and cash equivalents**

	2014	2013
	\$	\$
Cash at bank	23,581,100	23,292,420
	23,581,100	23,292,420
	23,581,100	23,292,420

Cash at bank earns interest at floating rates based on daily bank deposit rates. For the purposes of the Statement of Cash Flows, cash includes cash at bank and cash on deposit.

**Note 8 - Trade and other receivables**

Dividend receivable	879,906	1,180,844
Interest receivable	45,776	-
Investment sales	1,648,803	-
Applications receivable	26,809	56,561
Other receivables	124,089	156,992
	2,725,383	1,394,397
	2,725,383	1,394,397

**Note 9 - Financial assets at fair value through profit or loss**

Designated at fair value through profit or loss

Equities:		
Australian listed	247,130,401	208,050,813
International listed	29,613,682	10,597,452
Unlisted	1,805,060	856,326
	278,549,143	219,504,591
Stapled securities - Listed	14,494,208	17,558,378
	14,494,208	17,558,378
	293,043,351	237,062,969

The Scheme's accounting policy on fair value measurements is discussed in note 1(b).

**Note 10 - Other assets**

Capitalised project costs	278,161	474,510
	278,161	474,510
Capitalised project costs		
<i>At cost</i>		
Balance as at 1 July	868,413	807,130
Additions	-	61,283
Balance as at 30 June	868,413	868,413
<i>Accumulated amortisation and impairment</i>		
Balance as at 1 July	393,903	194,591
Depreciation	196,349	199,312
Balance as at 30 June	590,252	393,903

**Note 11 - Trade and other payables**

Investment purchases	2,462,716	-
Other payables	609,597	456,565
	3,072,313	456,565
	3,072,313	456,565



## Australian Ethical Smaller Companies Trust

### Notes to the Financial Statements for the year ended 30 June 2014

#### Note 12 - Distributions paid and payable

	2014	2013
	\$	\$
Distributions paid during the year	1,333,101	1,958,250
Distributions payable	11,958,526	3,958,917
	13,291,627	5,917,167

The Scheme paid interim distributions totalling 2.62 cents per unit (2013: 3.38 cents per unit) and year end distributions totalling 16.73 cents per unit (2013: 6.48 cents per unit).

#### Note 13 - Auditors' remuneration

Audit fees in relation to the Scheme are paid directly by the Responsible Entity. During the year the following fees were paid or payable by the Responsible Entity for services in relation to the audit of the Scheme.

Financial statements audit fees	20,200	17,000
Compliance plan audit	3,425	2,375
	23,625	19,375

#### Note 14 - Reconciliation of profit for the period to net cash provided by operating activities

Net profit from operating activities	44,100,811	50,496,641
Adjustments for:		
Net gains on disposal of investments	(9,787,528)	(11,015,415)
Net gains on revaluation of investments	(31,065,040)	(35,703,357)
Net losses on foreign exchange	-	52,400
Amortisation of project costs	196,349	199,312
Changes in assets and liabilities:		
decrease/(increase) in income and other receivables	288,065	(175,636)
Increase/(decrease) in other payables	153,032	(259,378)
Net cash provided by operating activities	3,885,689	3,594,567

#### *Non-cash financing and investing activities*

During the year income distributions totalling \$3,883,168 (2013: \$3,553,705) were reinvested by unitholders for additional units in the Scheme.

#### Note 15 - Related party disclosures

Australian Ethical Investment Limited (AEIL), as Responsible Entity of each Scheme, provides investment services for the Scheme in accordance with each Scheme's constitution. Transactions with the Responsible Entity are undertaken on commercial terms and conditions.

The Scheme does not employ personnel in its own right. However it is required to have an incorporated Responsible Entity to manage the activities of the Scheme and this is considered the key management personnel.

The following persons were directors of Australian Ethical Investment Limited during the whole of the financial year and up to the date of this report unless otherwise indicated:

Phil Vernon  
 Kate Greenhill  
 Stephen Gibbs  
 Mara Bun  
 Tony Cole  
 Stephen Newnham (ceased 26 July 2013)  
 André Morony (ceased 20 November 2013)

**Australian Ethical Smaller Companies Trust**

**Notes to the Financial Statements for the year ended 30 June 2014**

**Note 15 - Related party disclosures - continued**

There were no other persons with responsibility for planning, directing and controlling the activities of the Scheme, directly and indirectly during or since the end of the financial year.

During the year the following amounts were paid to the Responsible Entity in accordance with the Scheme's Constitution. Percentage rate of fees charged did not change from 30 June 2013.

	2014	2013
	\$	\$
Management fees (Retail 1.90% & Wholesale 0.95% of Net Assets)	5,403,229	4,408,411
Administration fees (Retail 0.305% of Net Assets & Wholesale nil)	817,053	564,474
Reimbursable expenses	-	3,031
	<b>6,220,282</b>	<b>4,975,916</b>

Fees payable to the Responsible Entity at 30 June 2014 were \$609,036 (2013: \$456,041).

Australian Ethical Superannuation Pty Ltd (ABN 43 079 259 733), a subsidiary of AEIL, is the Trustee of the Australian Ethical Retail Superannuation Fund (AERSF). Transactions with the AERSF are undertaken on commercial terms and conditions.

Transactions between AERSF and the Scheme during the financial year were:

AERSF purchase of units	13,831,242	5,213,641
AERSF sale of units	3,385,000	6,134,000
Value of units held by AERSF	151,768,355	141,830,941
Distribution payments to AERSF	2,390,510	893,233
Distribution payable to AERSF	5,808,164	1,830,077

	2014	2013
	Units	Units
Units purchased by AERSF	7,067,760	3,184,513
Units sold by AERSF	1,683,318	3,593,180

	2014	2013
	%	%
Percentage of units held by AERSF	49.78%	48.90%

Transactions between the Schemes where AEIL is the Responsible Entity during the financial year were:

	2014	2013
	\$	\$
Australian Ethical Balanced Trust purchase of units	101,468	-
Australian Ethical Balanced Trust sale of units	-	4,000,000
Value of units held by Australian Ethical Balanced Trust	26,711,575	23,851,085
Distribution payments to Australian Ethical Balanced Trust	446,513	167,574
Distribution payable to Australian Ethical Balanced Trust	1,022,250	345,046

	2014	2013
	Units	Units
Units purchased by Australian Ethical Balanced Trust	50,311	-
Units sold by Australian Ethical Balanced Trust	-	2,368,360

	2014	2013
	%	%
Percentage of units held by Australian Ethical Balanced Trust	8.76%	9.22%

## Australian Ethical Smaller Companies Trust

### Notes to the Financial Statements for the year ended 30 June 2014

#### Note 16 - Financial risk management and financial instruments

The Scheme is exposed to a variety of financial risks from investments in financial instruments, including operational risk, market risk, credit risk and liquidity risk.

This note presents information about the Scheme's exposure to each of the above risks, the Scheme's objectives, policies and processes for measuring and managing risks and the management of unitholder funds.

<b>(a) Categories of financial instruments</b>	<b>2014</b>	<b>2013</b>
<i>Financial assets</i>	<b>\$</b>	<b>\$</b>
Cash and cash equivalents	<b>23,581,100</b>	23,292,420
Investments designated at FVTPL	<b>293,043,351</b>	237,062,969
Trade and other receivables	<b>2,725,383</b>	1,394,397
	<b><u>319,349,834</u></b>	<u>261,749,786</u>
<i>Financial liabilities</i>		
Other financial liabilities		
Trade and other payables	<b>3,072,313</b>	456,565
Distribution payable	<b>11,958,526</b>	3,958,917
Amounts payable to unitholders	<b>304,597,156</b>	257,808,814
	<b><u>319,627,995</u></b>	<u>262,224,296</u>

#### **(b) Operational risk**

Operational risk is the risk of direct or indirect loss arising from a wide variety of causes associated with the Responsible Entity's processes, personnel, technology and infrastructure, and from external factors other than credit, market and liquidity risks such as those arising from legal and regulatory requirements and generally accepted standards of corporate behaviour. Operational risks arise from all of the Fund's operations.

The objective of the Responsible Entity of the Fund is to manage operational risk so as to balance the avoidance of financial losses and damage to its reputation with overall cost effectiveness and to avoid control procedures that restrict initiative and creativity.

#### **(c) Financial risk management objectives**

The Scheme is exposed to a number of risks due to the nature of its activities as further set out in its Product Disclosure Statement. These risks include market risk (including currency risk, interest rate risk and price risk), credit risk, and liquidity risk. The Scheme's objective in managing these risks is the protection and enhancement of unitholder value.

The Scheme's risk management policies are approved by the Responsible Entity and seek to minimise the potential adverse effects of these risks on the Scheme's financial performance. The risk management system is an ongoing process of identification, measurement, monitoring and controlling risk.

The Investment Committee's Charter requires it to oversight the processes which govern the investment of money of the Scheme for which Australian Ethical Investment Limited is the responsible entity. The Investment Committee bears primary responsibility for the oversight of processes for the management of the above financial risks. It meets on a regular basis to analyse financial risk exposure and to evaluate management strategies in the context of the most recent economic conditions and forecasts.

#### **(d)(i) Market risk**

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk comprises three types of risk: foreign exchange (currency risk), market interest rates (interest rate risk) and market prices (price risk). The Scheme manages this risk via outsourcing its investment management; the Investment Manager manages the financial risks relating to the operations of the Scheme in accordance with an investment mandate set out in accordance with the Scheme's Constitution and Product Disclosure Statement. The Scheme's investment mandate is to invest in a diversified portfolio of stocks listed on the ASX and it may also invest in derivative instruments such as futures and options. There has been no change to the Scheme's exposure to market risks or the manner in which it manages and measures the risk.

**Australian Ethical Smaller Companies Trust**

**Notes to the Financial Statements for the year ended 30 June 2014**

**Note 16 - Financial risk management and financial instruments - continued**

**(d)(ii) Foreign currency risk management**

The Scheme can invest in financial instruments and enter into transactions that are denominated in currencies other than its functional currency. Consequently, the Scheme is exposed to risk that the exchange rate of its currency relative to foreign currencies may change in a manner that has an adverse effect on the fair value or future cash flows of that portion of the Scheme's financial assets or liabilities denominated in currencies other than Australian dollar.

The Responsible Entity can use derivative financial instruments such as foreign currency options and forward contracts, to hedge the foreign currency risk exposures. The foreign currency exposure of the Scheme is reviewed regularly and updated as required. The use of derivative financial instruments is subject to policies and parameters set out in the Responsible Entities' Derivatives Risk Statement and Trust Investment Parameters. The Investment Committee is responsible for monitoring adherence to the Derivatives Risk Statement and the Trust Investment Parameters.

The carrying amounts of the Scheme's foreign currency denominated assets and monetary liabilities at the end of the reporting period are as follows:

	2014	2013
	\$	\$
NZD	<b>29,613,682</b>	10,597,452
	<b>29,613,682</b>	<b>10,597,452</b>

Management has performed a sensitivity analysis relating to the Scheme's exposure to currency risk at balance sheet date. This sensitivity analysis demonstrates the effect on the current year results and net assets attributable to unitholders which could result from a change in exchange rates by 5% (2013: 5%). In the analysis it is assumed that the amount of financial assets exposed to fluctuations in foreign exchange rates as at balance sheet date is representative of balances held throughout the financial year. No other flow on effects of fluctuations in foreign exchange rates have been taken into account.

At balance date, the effect on net assets attributable to unitholders and the change in net assets attributable as a result of changes in foreign currency rates with all other variables remaining constant would be as follows:

Currency	FX Exposure		
+5% AUD v's	All currencies	<b>1,480,684</b>	(529,873)
-5% AUD v's	All currencies	<b>(1,480,684)</b>	529,873

**(d)(iii) Interest rate risk management**

Interest rate risk represents the risk that the Scheme's financial performance will be adversely affected by fluctuations in interest rates.

The Scheme's exposures to interest rates on financial assets and financial liabilities are detailed in the liquidity risk management section of this note.

Management has performed a sensitivity analysis relating to the Scheme's exposure to interest rate risk at balance sheet date. This sensitivity analysis demonstrates the effect on the current year results and net assets attributable to unitholders which could result from a change in interest rates by 100 basis points (2013: 100 basis points). In the analysis it is assumed that the amount of financial assets exposed to fluctuations in interest rates as at balance sheet date is representative of balances held throughout the financial year. No other flow on effects of fluctuations in interest rates have been taken into account.

At balance date, the effect on profit and net assets attributable to unitholders, as a result of changes in the interest rate, with all other variables remaining constant would be as follows:

Increase in interest rate by 1%	<b>235,811</b>	232,924
Decrease in interest rate by 1%	<b>(235,811)</b>	(232,924)

## Australian Ethical Smaller Companies Trust

### Notes to the Financial Statements for the year ended 30 June 2014

#### Note 16 - Financial risk management and financial instruments - continued

##### (d)(iv) Price risk

Price risk is the risk that the total value of investments will fluctuate as a result of changes in market prices, whether caused by factors specific to an individual investment, its issuer or all factors affecting all instruments traded in the market. The Scheme has investments in equity instruments which exposes it to price risk. The investment manager manages the Scheme's market risk on a daily basis in accordance with the Scheme's investment objectives and policies, as detailed in the Product Disclosure Statement.

As the majority of the Scheme's financial instruments are carried at fair value with changes in fair value recognised in the income statement, all changes in market conditions will directly affect investment income.

Management has performed a sensitivity analysis relating to the Scheme's exposure to price risk at the balance sheet date. This sensitivity analysis demonstrates the effect on current year results and net assets attributable to unit holders which could result from a change in market prices of 10% (2013: 10%). In the analysis it is assumed that the amount of financial assets exposed to fluctuations in market prices as at the balance sheet date is representative of balances held throughout the financial year. No other flow on effects or fluctuations in fair value have been taken into account.

At balance date, the effect on net assets attributable to unitholders and the change in net assets attributable to unit holders as a result of changes in market prices with all other variables remaining constant would be as follows:

	2014	2013
	\$	\$
Increase in market prices by 10%	<b>29,304,335</b>	23,706,297
Decrease in market prices by 10%	<b>(29,304,335)</b>	(23,706,297)

##### (e) Credit risk management

Credit risk is the risk of financial loss from a counterparty failing to meet its contractual commitments. The Scheme is predominately exposed to credit risk through its deposits at banks and trade and other receivables. The Scheme's policy over credit risk is to minimise its exposure to counterparties, holding cash and cash equivalents at financial institutions with a credit rating of 'A' or higher and settling trade and other receivables on a monthly basis.

At the balance sheet date, all cash was held with National Australia Bank, which carries a Standard & Poor's rating of AA- at 30 June 2014 (2013: AA-). No financial assets carried at amortised cost were past due or impaired at 30 June 2014 (2013: nil).

The maximum credit risk exposure is represented by the respective carrying amounts of the relevant financial asset in the Statement of Financial Position.

The table below details the maximum exposure to credit risk for the assets held by the Scheme.

Cash and cash equivalents	23,581,100	23,292,420
Trade and other receivables	<b>2,725,383</b>	1,394,397
	<b><u>26,306,483</u></b>	<u>24,686,817</u>

**Australian Ethical Smaller Companies Trust**

**Notes to the Financial Statements for the year ended 30 June 2014**

**Note 16 - Financial risk management and financial instruments - continued**

**(f) Liquidity risk management**

Liquidity risk is the risk that the Scheme will encounter difficulty in realising assets or otherwise raising funds to meet commitments associated with financial instruments.

The Scheme is exposed to daily cash redemptions of redeemable units. Therefore, the approach to managing liquidity is for the Scheme to invest a significant portion of their funds in financial instruments which under normal market conditions are readily convertible into cash (for example, the Scheme's listed securities). As a result, there is a risk that the Scheme may not be able to liquidate all of these investments at their fair value in order to meet its liquidity requirements. In the event of significant redemptions, the Scheme has the ability to suspend redemptions until it can realise investments to meet the redemptions.

All payables of the Scheme are classed as normal operating obligations and are to be paid within three months of balance date.

**Financial instrument composition and maturity analysis**

	Weighted average interest rate %	2014				Total
		1-3 months	3 months to 1 year	1 to 5 years	5+ years	
		\$	\$	\$	\$	\$
Variable interest-bearing assets						
Cash and cash equivalents	2.40	23,581,100	-	-	-	23,581,100
Non-interest bearing						
Trade and other receivables	N/A	2,725,383	-	-	-	2,725,383
Financial assets	N/A	293,043,351	-	-	-	293,043,351
<b>Total financial assets</b>		<b>319,349,834</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>319,349,834</b>
Non-interest bearing						
Trade and other payables	N/A	3,072,313	-	-	-	3,072,313
Distribution payable	N/A	11,958,526	-	-	-	11,958,526
Amounts payable to unitholders	N/A	304,597,156	-	-	-	304,597,156
<b>Total financial liabilities</b>		<b>319,627,995</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>319,627,995</b>
	Weighted average interest rate %	2013				Total
		1-3 months	3 months to 1 year	1 to 5 years	5+ years	
		\$	\$	\$	\$	\$
Variable interest-bearing assets						
Cash and cash equivalents	2.90	23,292,420	-	-	-	23,292,420
Non-interest bearing						
Trade and other receivables	N/A	1,394,397	-	-	-	1,394,397
Financial assets	N/A	237,062,969	-	-	-	237,062,969
<b>Total financial assets</b>		<b>261,749,786</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>261,749,786</b>
Non-interest bearing						
Trade and other payables	N/A	456,565	-	-	-	456,565
Distribution payable	N/A	3,958,917	-	-	-	3,958,917
Amounts payable to unitholders	N/A	257,808,814	-	-	-	257,808,814
<b>Total financial liabilities</b>		<b>262,224,296</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>262,224,296</b>

**Australian Ethical Smaller Companies Trust**

**Notes to the Financial Statements for the year ended 30 June 2014**

**Note 16 - Financial risk management and financial instruments - continued**

**(g) Fair values**

The following table provides an analysis of financial instruments 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). This category includes instruments valued using quoted prices in active markets for similar instruments, quoted prices for identical or similar instruments in markets that are considered less than active or other valuation techniques for which all significant inputs are directly or indirectly observable from market data.

	2014			
	Level 1	Level 2	Level 3	TOTAL
	\$	\$	\$	\$
<b>Financial assets at fair value through profit or loss</b>				
Designated at fair value through profit or loss				
Equities				
Australian listed	247,130,401	-	-	247,130,401
International listed	29,613,682	-	-	29,613,682
Unlisted	-	-	1,805,060	1,805,060
Stapled securities				
Listed	14,494,208	-	-	14,494,208
<b>TOTAL</b>	<b>291,238,291</b>	<b>-</b>	<b>1,805,060</b>	<b>293,043,351</b>

	2013			
	Level 1	Level 2	Level 3	TOTAL
	\$	\$	\$	\$
<b>Financial assets at fair value through profit or loss</b>				
Designated at fair value through profit or loss				
Equities				
Australian listed	207,203,950	846,863	-	208,050,813
International listed	10,597,452	-	-	10,597,452
Unlisted	-	856,326	-	856,326
Stapled securities				
Listed	17,558,378	-	-	17,558,378
<b>TOTAL</b>	<b>235,359,780</b>	<b>1,703,189</b>	<b>-</b>	<b>237,062,969</b>

Investments classified within level 3 represent investment into unquoted equity securities. The valuation technique may use significant unobservable inputs at the underlying asset level. However, the scheme obtains fair value prices from the relevant companies without significant adjustments and does not calculate any unobservable inputs itself.

The following table shows a reconciliation from the beginning balances to the ending balances for fair value measurements in Level 3 of the fair value hierarchy.

	<b>Unlisted Equities</b>
<b>Opening balance at 1 July 2013</b>	-
Transfers into level 3	856,326
Purchases	1,099,753
Return of capital	(111,148)
Total gains or losses in profit or loss	(39,871)
	<u>1,805,060</u>

Total gains or losses for the period included in the Statement of Profit or Loss and Other Comprehensive Income attributable to changes in unrealised gains and losses relating assets and liabilities held at the end of the reporting period.

## Australian Ethical Smaller Companies Trust

### **Note 17 - Events subsequent to the reporting date**

The Australian and international markets remain relatively volatile, and this impacts the valuation of the Scheme's investment portfolio. As the investments are measured at their 30 June 2014 fair values in the financial report, any volatility in values subsequent to the balance date is not reflected in the Statement of Profit or Loss and Other Comprehensive Income or the Statement of Financial Position. However the volatility in value of investments has been reflected in the current unit price.

Except as outlined above, during the period between the end of the financial year and the date of this report, there were no items, transactions or events of a material and unusual nature likely in the opinion of the Responsible Entity, to affect significantly the operations of the Scheme, the results of those operations, or the state of affairs of the Scheme in future financial years.

### **Note 18 - Contingencies**

There are no contingent assets or liabilities as at 30 June 2014 (2013: Nil).



## Australian Ethical Smaller Companies Trust

### Directors' Declaration

In the opinion of the Directors of Australian Ethical Investment Limited, the Responsible Entity of the Australian Ethical Smaller Companies Trust (the "Scheme"):

(a) The annual financial statements and notes that are set out on pages 3 to 22 are in accordance with the Corporations Act 2001, including:

- i. Giving a true and fair view of the Scheme's financial position as at 30 June 2014 and of its performance for the financial year ended on that date; and
- ii. Complying with Australian Accounting Standards (including the Australian Accounting Interpretations) and Corporations Regulations 2001; and

(b) There are reasonable grounds to believe that the Scheme will be able to pay its debts when they become due and payable.

The Directors draw attention to Note 1 of the financial report which contains a statement of compliance with International Financial Reporting Standards.

Signed in accordance with a resolution of the Board of Directors of Australian Ethical Investment Limited.



Phil Vernon  
Managing Director  
Australian Ethical Investment Limited  
26 September 2014



*Lead Auditor's Independence Declaration under Section 307C of the Corporations Act 2001*

To: the directors of Australian Ethical Investment Limited, the Responsible Entity for the Australian Ethical Smaller Companies Trust:

I declare that, to the best of my knowledge and belief, in relation to the audit for the financial year ended 30 June 2014 there have been:

- (i) no contraventions of the auditor independence requirements as set out in the *Corporations Act 2001* in relation to the audit; and
- (ii) no contraventions of any applicable code of professional conduct in relation to the audit.

KPMG

Karen Hopkins  
*Partner*

Sydney  
26 September 2014



## **Independent auditor's report to the unitholders of the Australian Ethical Smaller Companies Trust**

### **Report on the financial report**

We have audited the accompanying financial report of Australian Ethical Smaller Companies Trust ('the Scheme'), which comprises the statement of financial position as at 30 June 2014, the statement of profit and loss and other comprehensive income, statement of changes in equity and statement of cash flows for the year ended on that date, notes 1 to 18 comprising a summary of significant accounting policies and other explanatory information, and the directors' declaration.

#### *Directors' responsibility for the financial report*

The directors of Australian Ethical Investment Limited ('the Responsible Entity') are responsible for the preparation of the financial report that gives a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001*, and for such internal control as the directors determine is necessary to enable the preparation of the financial report that is free from material misstatement, whether due to fraud or error. In note 1, the directors of the Responsible Entity also state, in accordance with Australian Accounting Standard AASB 101 *Presentation of Financial Statements*, that the financial statements comply with International Financial Reporting Standards.

#### *Auditor's responsibility*

Our responsibility is to express an opinion on the financial report based on our audit. We conducted our audit in accordance with Australian Auditing Standards. Those standards require that we comply with relevant ethical requirements relating to audit engagements and plan and perform the audit to obtain reasonable assurance whether the financial report is free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial report. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial report, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation of the financial report that gives a true and fair view 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 entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the financial report.

We performed the procedures to assess whether in all material respects the financial report presents fairly, in accordance with the *Corporations Act 2001* and Australian Accounting Standards, a true and fair view which is consistent with our understanding of the Scheme's financial position, and of its performance.



We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

*Independence*

In conducting our audit, we have complied with the independence requirements of the *Corporations Act 2001*.

*Auditor's opinion*

In our opinion:

- (a) the financial report of the Australian Ethical Smaller Companies Trust is in accordance with the *Corporations Act 2001*, including:
  - (i) giving a true and fair view of the Scheme's financial position as at 30 June 2014 and of its performance for the year ended on that date; and
  - (ii) complying with Australian Accounting Standards and the *Corporations Regulations 2001*.
- (b) the financial report also complies with International Financial Reporting Standards as disclosed in note 1.

KPMG

KPMG

Karen Hopkins  
*Partner*

Sydney  
26 September 2014