

How do the 'Good Practice Principles' apply in practice?

Overview of key unit pricing issues

Management issues in unit pricing

Unit pricing issue	Good practice guidance	Guide (page reference)
Effective risk management culture	<ul style="list-style-type: none"> ➤ The board and senior management should have a sufficient understanding of business processes and place a high priority on the unit pricing function. ➤ Ensure that everyone participating in unit pricing is appropriately trained. ➤ Document all policies and procedures. ➤ Implement formal reporting procedures on unit pricing matters, including regular identification and reporting of new risks. ➤ Implement regular, independent review of the inputs and outputs of unit pricing, as well as the related systems, procedures, methodologies and controls. 	21-29
Forward pricing or historic pricing	<ul style="list-style-type: none"> ➤ Forward pricing is preferred to historic pricing. ➤ Where historic pricing is used, controls should be in place to avoid arbitrage. 	30 and 32-33
Batching	<ul style="list-style-type: none"> ➤ If you use batching, you should batch and process on the day, or the day after, the price is calculated and make reasonable efforts to ensure that any return earned on unprocessed funds is attributed to the investor. 	33
Many pieces of information are used to calculate one unit price	<ul style="list-style-type: none"> ➤ Implement systems and procedures to check that data has not become unreliable, inaccurate or late. Each data item needs to be appropriately checked before it is fed into the unit pricing calculation. 	30-31 and 34
Transaction costs	<ul style="list-style-type: none"> ➤ To the extent that transaction costs are incurred as a result of application and redemption cashflows, people buying and selling units need to pay an allowance for those costs. ➤ The use of a single mid-price with no allowance for transaction costs is not consistent with good practice. ➤ Transaction costs must be applied consistently and equitably. The transaction costs methodology must be periodically reviewed and updated. ➤ Any profit from the application of the transaction cost policy must be returned to the fund. 	31-32 and 34-35

How do the 'Good Practice Principles' apply in practice?

Overview of key unit-pricing issues

Unit pricing issue	Good practice guidance	Guide (page reference)
Backdating (ie processing applications after the date of receipt)	<ul style="list-style-type: none"> ➤ Units must be issued and redeemed at the price, and in the timeframes, stated in the governing documents and in the product disclosure statement. ➤ Ensure that unitholders have not suffered loss as a result of any delay in processing. ➤ To the extent possible, design your procedures and allocate your resources so that delays are avoided and the use of backdating is minimised. 	32 and 35-37
Market disruption	<ul style="list-style-type: none"> ➤ Policies and procedures should deal with market disruption. 	37
Fund of fund structures	<ul style="list-style-type: none"> ➤ Build into your unit pricing cycle an allowance for the time needed to obtain unit prices from external product providers. ➤ In limited cases where there is no alternative, estimates may be required. ➤ When relying on the unit pricing systems of other product providers, you need to take steps to ensure that the service meets your requirements, eg regarding the timeliness of information and the reliability of the approach to unit pricing calculations. 	38 and 39
Performance fees	<ul style="list-style-type: none"> ➤ Carefully design and test your model for performance fee calculations, and periodically review its operation. ➤ Where an accrual can be estimated on a sound basis, this is likely to provide a more equitable outcome. ➤ Disclose your approach to calculating performance fees, including the effect on investors, the frequency of calculating the fee and any limitations on entering or exiting the fund due to the timing of performance fee calculations. 	38-39 and 40
Managing diversity in systems and products	<ul style="list-style-type: none"> ➤ The incidence of error is higher where a provider has many products operating under different rules or several administration platforms operating at once. Appropriate risk management strategies need to be implemented. ➤ Additional care and attention is required to effectively manage old (legacy) products or systems. 	45 and 46

How do the 'Good Practice Principles' apply in practice?

Overview of key unit-pricing issues

Unit pricing issue	Good practice guidance	Guide (page reference)
Managing changes in strategy and structure, product offerings and systems and staff	<ul style="list-style-type: none"> ➤ Simple change management processes should be implemented to approve, monitor and control the effect of change on unit pricing. 	45 and 47
Outsourcing unit pricing functions (eg asset valuation and fund accounting)	<ul style="list-style-type: none"> ➤ When a business activity is outsourced to a service provider, you are still accountable for the performance of that business activity. ➤ Outsourcing should be seen as a long-term commitment. ➤ Develop and implement outsourcing policies and procedures, including criteria to assess the capacity of service providers to meet your requirements. ➤ Understand the key elements of a service provider's unit pricing methodologies, policies, processes and controls. ➤ Develop service level agreements that cover certain matters specified in the Guide. ➤ Monitor the provision of outsourced services (eg through regular reporting requirements). 	48-55

Technical issues in unit-pricing

Unit-pricing issue	Good-practice guidance	Guide (page reference)
Determining asset values	<ul style="list-style-type: none"> ➤ Develop sound and justifiable documented policies for asset valuation for unit pricing, and review and update these periodically. ➤ Provide unbiased valuations. ➤ Use valuation methodologies that are be consistent with the governing rules of the product. ➤ Don't use estimates where actual values are available. Where there is no alternative but to use estimates, they must be developed on a sound and reasonable basis. Estimation policies need to be developed by people with appropriate expertise, tested periodically using actual data, and updated. 	56-62

How do the 'Good Practice Principles' apply in practice?

Overview of key unit-pricing issues

Unit-pricing issue	Good-practice guidance	Guide (page reference)
	<ul style="list-style-type: none"> ➤ Where values are not directly obtained from a market (ie non-exchange traded assets), you are responsible for understanding the valuation bases and ensuring they are appropriate, objectively reasonable, independently verifiable and internally consistent. ➤ You may seek third-party professional valuation advice, but you cannot delegate responsibility for determining the asset value. ➤ Price as frequently as you make it possible to buy or sell units in the fund. ➤ In principle, unit prices should only be struck with the same frequency that asset values are determined. Depending on the nature of the assets, you may need to use reasonable estimates of asset values. ➤ Determine the appropriate frequency for calculating hard prices, and for comparing hard and soft prices, based on the nature of the assets. ➤ Use reputable, professional, third-party valuers for periodic valuations of assets with recognised valuation methodologies such as property and infrastructure. ➤ Where an asset is valued infrequently (eg hedge fund assets, private equity, etc), daily or weekly prices cannot be struck between valuations unless there is a reasonable basis for estimating the unit price. Using estimates may be appropriate where illiquid assets comprise a small part of a large portfolio. ➤ Don't use long-term valuation models where assets are to be sold in the short term. ➤ In the case of foreign currency denominated assets, establish a policy to determine the appropriate exchange rate for valuations, if it is not already identified in the fund documentation. ➤ Transaction costs should not be included in asset values. 	
Determining tax treatments	<ul style="list-style-type: none"> ➤ A reasonable estimate of the tax provision must be used each time a unit price is struck. This estimate must be reconciled with the tax provisions in the accounts from time-to-time. 	63-71

How do the 'Good Practice Principles' apply in practice?

Overview of key unit-pricing issues

Unit-pricing issue	Good-practice guidance	Guide (page reference)
	<ul style="list-style-type: none"> ➤ Imputation credits should be included in the unit price as soon as information is available, to ensure that holders of a product at the time an amount accrues receive the benefit of that amount in the unit price. ➤ Future income tax benefits should be included in unit prices to the extent that they have value for present or future unitholders. ➤ Prepare reconciliations that compare the tax amounts used in unit pricing with the amounts, separately calculated, which are reported in financial statements and annual tax returns. Preparing reconciliations once a year, within three months of the due date for payment of tax, is the minimum acceptable frequency, and is appropriate only for funds with simple tax arrangements. For funds with more complex tax arrangements, reconciliations will generally be required quarterly or, at a minimum, six-monthly. 	
Determining the use of reserves	<ul style="list-style-type: none"> ➤ Only use reserves for an agreed purpose that has a reasonable basis. ➤ Develop sound and justifiable documented policies for the use of reserves, explaining the assumptions and why they are reasonable and appropriate. ➤ Clearly state the purpose of reserves, and policies governing their operation, in a form accessible to unitholders, together with information about amounts held in reserves. ➤ While it may be appropriate to use smoothing reserves with crediting rates, don't use smoothing reserves with unit pricing. 	72-75
Applying accounting standards	<ul style="list-style-type: none"> ➤ As a reporting entity, ensure that you comply with the Australian equivalents of IFRS, including (where necessary) by implementing changes to documents, implementing change in unit pricing practice, modifying computer systems and determining whether any new disclosures are required. ➤ Where financial statements show negative equity, you need to ensure that you make appropriate disclosures to unitholders to explain the significance of this equity position. 	76-79

How do the 'Good Practice Principles' apply in practice?

Overview of key unit-pricing issues

Consumer issues in unit pricing

Unit-pricing issue	Good-practice guidance	Guide (page reference)
Providing information about unit pricing	<ul style="list-style-type: none"> ➤ Develop sound and justifiable documented policies for providing information about unit pricing. ➤ Establish communication channels between work areas, including unit pricing, tax, accounting, product development, marketing, risk management and legal. ➤ Establish periodic, independent internal or external reviews to ensure ongoing consistency of documents and unit-pricing practice. ➤ Comply with the Good Disclosure Principles described in ASIC Policy Statement 168. 	80-86
Managing complaints	<ul style="list-style-type: none"> ➤ Consider management of complaints and other customer feedback as an essential part of risk management. ➤ Set up communication channels across organisational divisions to ensure that the causes of complaints are understood and addressed. ➤ Provide a copy of your complaints handling procedures to all relevant staff. 	87-89
Managing errors and compensation	<ul style="list-style-type: none"> ➤ If there are errors in unit pricing, unitholders do not receive the share of the value of the fund to which they are entitled. Therefore, you need to establish policies and procedures for managing unit pricing errors and addressing compensation issues. Your policies and procedures should address certain matters specified in the Guide. ➤ Communicate appropriately with unitholders (which may include unaffected unitholders) about the error and how and when the error will be fixed. ➤ Where unitholders have gained an advantage due to unit pricing error, you may choose to bear the cost, or you may seek to recover the amount from those unitholders. ➤ If an error occurs that adversely affects unitholders, you will need to compensate unitholders to return them to the financial position that would have existed had the error not occurred. 	90-98

How do the 'Good Practice Principles' apply in practice?

Overview of key unit-pricing issues

Unit-pricing issue	Good-practice guidance	Guide (page reference)
	<ul style="list-style-type: none"> ➤ Communicate with ASIC or APRA as soon as possible when a unit pricing error has been detected. The Guide outlines the information that will need to be provided. ➤ When determining whether compensation is payable, consider the impact on each individual unitholder of one or more unresolved errors. You need to: <ul style="list-style-type: none"> ➤ compare the value that would have accumulated had the unresolved error(s) not arisen with the value that accumulated in the presence of the error(s), from the date the error(s) started to the date the effect of the error(s) ceased; ➤ pay compensation if the difference is equal to or greater than 0.3 per cent (30 basis points) of the value that would have accumulated without the error; ➤ if the difference is less than 0.3 per cent, consider whether, in the circumstances, compensation should be paid. Where an error arises due to miscalculation of fees, it must be compensated in all cases. ➤ Importantly, in setting a 'materiality threshold' for compensating unitholders, the Guide does not adopt IFSA's approach (in Guidance Note 4) of setting a minimum dollar limit (eg \$20). According to the Guide, setting a dollar limit on loss to unitholders, below which compensation would not be paid, would discriminate between unitholders with larger and smaller investments. ➤ Unitholders do not usually bear the cost of compensation. However, where this is not the case, the costs to unitholders of receiving compensation may, in some cases, outweigh the benefits to those same unitholders. When determining compensation in the circumstances of your fund, you must take all relevant legal obligations into account and be able to demonstrate how you have addressed those obligations. 	