MFS PREMIUM INCOME FUND ARSN 090 687 577

ANNUAL REPORT 2006

MFS

INNOVATIVE INVESTMENT SOLUTIONS

www.mfsgroup.com.au

MFS Investment Management Limited
ABN 20 101 634 146, AFSL 246 553

Corporate Directory

Fund
MFS Premium Income Fund ARSN 090 687 577

Responsible Entity
MFS Investment Management Limited ABN 20 101 634 146
Australian Financial Services Licence No. 246553

Website
www.mfsgroup.com.au

Offices of MFSIM

New South Wales
Level 5, 56 Pitt Street
Royal Exchange Building
Sydney NSW 2000
Tel: +61 2 8259 7200
Fax: +61 2 9252 6201

Victoria
Level 11
200 Queen Street
Melbourne VIC 3001
Tel: +61 3 8602 2600
Fax: +61 3 9602 2832

Queensland
MFS House
5 Hicks Street
Southport QLD 4215
Tel: +61 7 5557 7700
Fax: +61 7 5591 8362

Legal Adviser
McCullough Robertson
Level 12
Central Plaza Two
66 Eagle Street
Brisbane QLD 4000

Auditor
KPMG
KPMG House
147 Collins Street
Melbourne VIC 3000

Registrar
Perpetual Nominees
Limited
MFS PIF
GPO Box 5136
Sydney NSW 2001
Tel: 1300 721 051

Table of contents

CEO letter

Dear Investor

On behalf of the Directors of MFS Investment Management Limited ('MFSIM'), the Responsible Entity of the MFS Premium Income Fund ('the Fund'), it is my pleasure to report another year of growth and consistent performance.

We are pleased to enclose the Financial Report for the year ended 30 June 2006 for the Fund and its controlled entities. These are the first full year accounts prepared in accordance with Australian equivalents to International Financial Reporting Standards ('AIFRS'). The implementation of AIFRS has resulted in a significantly longer set of notes to the accounts in order to satisfy all the additional disclosure requirements under the new standards.

During the year the Fund sold down its equity holding in the MFS Resort Asset Investment Fund ('MLR'), resulting in a holding of less than 50% as at 30 June 2006. However, as the Fund held greater than 50% of equity in the MLR up until early April 2006, thereby retaining control over MLR and the entities contained within, a consolidated income statement and statement of cash flows have been disclosed in the accounts for this period.

RESULTS FOR 2006

During the past financial year there have been a number of key achievements:

- 32% increase in Net Fund Growth;
- Balance of Net Funds over $700 million (as at 30 June 2006 the Fund had $704 million under management);
- Net Profit of $53,803,880 (an increase of 38% from previous year) of which 100% was distributed to unitholders; and
- Distributions were paid at targeted rates for all terms with an average return of 8.41% to unitholders.

We believe that the results are a testament to MFSIM's ability to select and professionally manage the assets of the Fund.

YEAR IN REVIEW

Over the last year the Fund has strategically developed into an Income Fund by diversifying its portfolio away from the a single asset investment sector [commercial mortgages] into a number of different capital stable, income yielding asset classes such as property trusts. This has resulted in a small portion of the income received from the Fund being tax advantaged for investors.

MFSIM received very strong acceptance at the unit holder meeting held on 23 June 2006 for the introduction of an innovative fee structure for the Fund. MFSIM has placed the interests of PIF investors first [ahead of MFSIM] by ensuring all obligations to investors are satisfied before payment of management fees.

In our view the revised remuneration model provides a benchmark for the funds management industry by truly aligning the interests of MFSIM with those of the investor. The way MFSIM now draws its fees is fundamentally linked to successful delivery of our targeted returns to investors.

In our view, it is a risk few in our industry are willing to take and is a testament to the confidence we have in our ability to deliver on our investors' expectations.

Furthermore, Investors in the Fund are now supported by a unique arrangement whereby MFS Limited will provide a $50 million support facility to MFSIM to assist with meeting investor redemptions and distributions.

We have also introduced a Loyalty Bonus program because we believe it's important for investors to be rewarded for staying with us. When investors rollover a 12 or 24 month investment for a further 12 or 24 month term, we will automatically reward you with an additional 0.1% pa on top of the current targeted rate of return. So, you are rewarded just for being a loyal customer and staying invested for another term.

UPDATE ON MFSIM

MFSIM manages over $800 million across a suite of income based investment products and it has been a year of growth for the MFSIM team. The team has expanded during the year and two key executive appointments have been made. Guy Hutchings was appointed as Chief Investment Officer (CIO) of MFSIM in July. Guy came from Tower Australia Limited where he was the CIO for over $3.5 billion of funds under management. He brings a wealth of knowledge and experience to the team with over 20 years experience in the funds management industry.

In addition, Grant Harris recently joined the MFSIM team as the new Fund Manager for the Fund. Grant has over 7 years experience as a quantitative analyst and investment researcher. Grant has extensive experience in building model portfolios and setting fund asset allocations.

Further to the two senior appointments, MFSIM has continued to recruit quality staff to the asset management and performance teams, especially in the non-mortgage sectors, thereby boosting experience and knowledge in this area.

OUTLOOK FOR THE FUTURE

The investment environment remains positive particularly where investors are looking for strong performance that a fund such as the MFS Premium Income Fund can potentially offer by way of yield, capital protection and investment diversification.

MFSIM expects a continuation of positive performance from the Fund in 2006 and on behalf of my fellow colleagues I thank you for your continued support.

Should you have any queries, please contact Client Services on 131 MFS, (131 637) or email mail@mfsgroup.com.au.

Yours sincerely

STEVE KYLING
CHIEF EXECUTIVE OFFICER
MFS INVESTMENT MANAGEMENT LIMITED

Directors' report

The Directors of MFS Investment Management Limited, the Responsible Entity of MFS Premium Income Fund (the "Trust"), present their report together with the financial report of the consolidated entity, being the Trust and its controlled entities for the year ended 30 June 2006 and the auditor's report thereon.

Responsible Entity

The Responsible Entity of MFS Premium Income Fund is MFS Investment Management Limited.

The directors of MFS Investment Management Limited during or since the end of the financial year are:

Michael Christodoulou King, LLB
Executive Director
Age 42

Director since 8 August 2002.

Michael is the co-founder of the MFS Group and has extensive experience in financial services, asset management, debt recovery, mortgagee property sales and commercial property litigation. Michael is a director of MFS Limited (appointed 4 February 2004), MFS Living and Leisure Group (appointed 8 August 2002), HFA Holdings Limited (since 5 August 2002) and was a director of Village Life Limited from 28 June 2006 to 31 August 2006.

Michael Gordon Hiscock B.Bus,
CFP F.Fin
Independent Non-Executive Chairman
Age 46

Director since 15 May 2003.

Michael has extensive experience in the financial planning and investment advisory industry spanning more than 20 years. He is a director of Avenue Capital Management Ltd and continues to provide advice to a broad range of clients. Michael holds a Bachelor of Business (Majoring in Accounting), is a Certified Financial Planner and a Fellow of the Financial Services Institute of Australasia. Michael is a director of MFS Limited (appointed 4 February 2004) and was a director of MFS Living and Leisure Group between 15 May 2003 and 24 March 2005.

Paul Joseph Manka, MBA
CFP Asia
Independent Non-Executive Director
Age 45

Director since 15 May 2003.

Paul holds a Masters in Business Administration (MGSM), is a Certified Financial Planner and a Fellow of the Financial Services Institute of Australasia. Paul has held a range of positions within the financial services sector, including various board and management positions, and continues to provide financial advice to a broad range of clients. Paul has been a director of MFS Limited since February 2004, HFA Holdings Limited since 1 September 2005 and was a director of MFS Living & Leisure Group between February 2004 and March 2005.

Craig Robert White
B.Bus, SA Fin
Executive Director
Age 33

Director since 31 August 2005.

Craig has over 10 years experience in accounting and financial services, including positions with Bank of New York – London, Union Bank of Switzerland and Suncorp. He is the Chief Executive Officer of the MFS Diversified Group and Deputy CEO of MFS Limited. Craig was a director of Village Life Limited from 28 June 2006 to 31 August 2006, and was a director of MFS Living and Leisure Group between 31 August 2005 and 15 May 2006.

Philip William Adams
Dip. Law
Executive Director
Age 51

Resigned 28 November 2005 (Director since 15 July 1999).

Philip is the co-founder of the MFS Group. Philip has extensive experience in the banking, finance and property industries. Philip has also worked extensively for a public listed property company specialising in property syndications. Philip is a director of MFS Limited (appointed 4 February 2004) and was a director of MFS Living and Leisure Group between 8 August 2002 and 28 November 2005.

Directors' report

Spencer Martin Young
B.Eng, MBA (Harvard)
Independent Non-Executive Director
Age 45

Resigned 6 October 2005 (Director since 7 October 1999).

Spencer has extensive investment and management experience domestically and internationally across property, private equity and venture capital investing. Spencer is a director of HFA Asset Management Limited (since listing in May 2006), was a director of MFS Limited from February 2004 to November 2005 and was a director of MFS Living and Leisure Group between 15 May 2003 and 24 March 2005.

The registered office of MFS Investment Management Limited and the Trust is MFS House, 5 Hicks Street, Southport, Queensland.

Company Secretary
Kim Kercher
CA, B.Bus(Acc), Grad Dip Applied Corp Gov, ACIS

Kim was appointed Company Secretary of the Responsible Entity on 31 August 2005. Kim is the Chief Governance Officer of MFS Limited, and also acts as Company Secretary of the ultimate parent entity and a number of subsidiaries within the group. Prior to joining MFS, Kim was a manager with KPMG specialising in assurance and advisory services, and has more than 15 years experience in accounting, compliance, regulatory and financial reporting.

David Anderson
FCA, B.Com, IP, MICM, CFA

David was appointed Company Secretary of the Responsible Entity on 18 April 2002. David is the Chief Financial Officer of MFS Limited, and joined after 20 years in the accounting profession practising in Australia, Europe, Asia and the South Pacific. David is an ex partner of KPMG Australia where his clients included major banks and financial institutions.

Principal activities
The Trust is a registered managed investment scheme domiciled in Australia.

The Trust's principal activity for the year was the receipt of unitholders' funds and investment of unitholders' funds in registered first mortgages, equity & debt instruments and cash.

The Trust did not have any employees during the year.

There has been no significant change in the nature of those activities during the year.

Review and results of operations

Operating result

The Consolidated net profit before finance costs for the year ended 30 June 2006 was $62,939,679 (2005: $38,973,778). The Trust's net profit before finance costs for the year ended 30 June 2006 was $53,803,880 (2005: $38,973,778).

Distributions

Distributions paid or payable by the Consolidated Entity in respect to the financial year total $54,251,240 (2005: $38,973,778). Distributions paid or payable by the Trust in respect to the financial year total $53,803,880 (2005: $38,973,778). This represents an average return of 8.41% (2005: 8.45%) on funds invested by unitholders.

unitholders' funds

The Trust issued 465,784,843 units during the financial year (2005: 291,228,613) while 296,125,422 units were redeemed (2005: 134,582,937), resulting in a balance of 704,795,104 units on issue as at 30 June 2006 (2005: 535,135,683).

The Trust had total assets valued at $711,587,387 as at 30 June 2006 (2005: $540,318,973). The basis for valuation of the Consolidated Entity's assets is disclosed in Note 1 to the financial statements.

State of affairs

The Trust continued to invest primarily in mortgage loans and equity & debt instruments during the year ended 30 June 2006, and continues to offer investors a diversified investment profile and a variety of investment terms ranging from 6 months to 24 months.

The asset allocation of the Trust as at 30 June 2006 was as follows:

Commercial Loans	45%
Managed Investment Schemes	27%
Alternative Investments	15%
Cash Investments	8%
Fixed Interest Investments	5%

A new remuneration structure for the Responsible Entity, MFS Investment Management Limited was voted in favour on 23 June 2006. The structure is designed to align the interests of the Responsible Entity with those of the unitholders whereby MFS Investment Management Limited will only be paid its monthly management fee entitlement after all current distributions, expenses and redemptions of the Trust have been satisfied. As part of the structure, the parent entity of the Responsible Entity, MFS Limited will provide a support mechanism to unitholders allowing the Trust to call upon MFS to support such payments.

In the opinion of the Responsible Entity there were no other significant changes in the state of affairs of the Trust that occurred during the financial year.

Directors' report

Environmental regulation

The Consolidated Entity's operations are not subject to any particular or significant environmental regulations under Commonwealth, State or Territory law in relation to its investment properties.

Rounding off

The Consolidated Entity is of a kind referred to in ASIC Class Order 98/100 dated 10 July 1998 and in accordance with that Class Order, amounts in the financial report and Directors' report have been rounded off to the nearest thousand dollars, unless otherwise stated.

Likely developments

The Responsible Entity does not propose any changes to the existing business of the Trust.

The Trust will pursue a policy of maintaining returns through selective investment decision making.

Further information about likely developments in the operations of the Trust and the expected results of those operations in future financial years has not been included in this report because disclosure of the information would be likely to result in unreasonable prejudice to the Trust.

Events subsequent to balance date

There has not arisen in the interval between the end of the financial year, and the date of this report any item, transaction or event of a material and unusual nature likely, in the opinion of the Responsible Entity, to affect significantly the operations of the Trust, the results of those operations, or the state of affairs of the Trust, in future financial years.

Interests of the Responsible Entity

The Responsible Entity and its associates held the following units in the Trust at year-end.

2006 Related Party	Investments held by related party $	Investments during the year $	Repayments during the year $	Distribution paid during the year $
MFS Wholesale Premium Income Fund	61,077,053	63,685,140	35,026,589	3,773,339
MFS L&L Management Limited	-	-	100,000	993
Michael C King Superannuation Fund	38,726	3,142	-	3,142

2005 Related Party	Investments held by related party $	Investments during the year $	Repayments during the year $	Distribution paid during the year $
MFS Wholesale Premium Income Fund	32,418,502	49,434,107	17,015,605	1,236,682
MFS L&L Management Limited	100,000	100,000	-	2,209
Michael C King Superannuation Fund	35,584	35,584	-	1,884

Responsible Entity's remuneration

On 23 June 2006 unitholders voted in favour of an amendment to the Constitution regarding the remuneration structure of the Responsible Entity, MFS Investment Management Limited. Up to the date of change the Trust was required to pay a management fee of 1% per annum (plus GST) of the total assets of the fund.

Under the new remuneration structure, MFS Investment Management Limited is entitled to receive, all surplus funds generated by the Trust only after all current distribution, redemption and expense obligations have been satisfied at the end of each month.

The following fees were paid or payable to the Responsible Entity and its associates during the financial year:

	2006 $	2005 $
· Management Fees for the year received directly from MFS Premium Income Fund.	7,773,534	4,811,478
· Other expenses included administration expenses incurred by the Responsible Entity, which are reimbursed to the Responsible Entity or associated entities in accordance with the provisions of the Constitution.	3,231,695*	162,695

** Following the introduction of the new management fee structure (i.e. Surplus after all Trust expenses, distributions and redemptions obligations are met) there is an increase in the value of the Trust expenses paid and reimbursed to the Responsible Entity this year.*

It is important to note that the overall cost of operating the Trust (i.e. Total Trust expenses, including insurance and management fees) for the year was the same as the previous year (2.35% - based on weighted average unit holder value). The increase in reimbursement of Trust expenses to the Responsible Entity has not resulted in an increase in total cost to the investor.

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

The lead auditor's independence declaration is set out on page 6 and forms part of the Directors' report for the year ended 30 June 2006.

Indemnities and insurance premiums of Officers or Auditors

Under the Trust's constitution the Responsible Entity, including its officers and employees, is indemnified out of the Trust's assets for any loss, damage, expense or other liability incurred by it in performing or exercising any of its powers, duties or rights in relation to the Trust.

The Trust has not indemnified any auditor of the Trust.

No insurance premiums are paid out of the Trust's assets in relation to insurance cover for the Responsible Entity, its officers and employees, the Compliance Committee or the auditors of the Trust.

Signed in accordance with a resolution of the Directors of the Responsible Entity, MFS Investment Management Limited.

	3/10/06
Director	Date

Auditor's declaration

LEAD AUDITOR'S INDEPENDENCE DECLARATION UNDER SECTION 307C OF THE CORPORATIONS ACT 2001

To: the Directors of the Responsible Entity, MFS Investment Management Limited:

I declare that, to the best of my knowledge and belief, in relation to the audit for the financial period ended 30 June 2006 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

D M Waters
Partner

Melbourne

Date: 11 October 2006

Financial statements

MFS

Income Statements for the financial year ended 30 June 2006

		Consolidated		Trust	
	Note	2006 $'000	2005 $'000	2006 $'000	2005 $'000
Revenue					
Interest income	3(a)	51,288	45,552	51,282	45,552
Investment income	3(b)	10,411	2,489	13,457	2,489
Investment property income		36,301	-	-	-
Loan and other fees	3(c)	750	1,817	750	1,817
Realised profit on sale of investments		3,243	-	3,243	-
Net change in fair value of investments		10,261	-	75	-
Total revenue		112,254	49,858	68,807	49,858
Expenses					
Audit fees	4	111	30	29	30
Advertising & marketing fees		3,490	1,691	1,784	1,691
Bad debts		-	241	-	241
Consulting, compliance, accounting & legal fees		3,760	486	1,635	486
Commission		1,324	-	1,324	-
Cost of stock sold		1,602	-	-	-
Custodian & registry fees		1,132	1,256	1,107	1,256
Depreciation		436	-	-	-
Employee expenses		11,024	-	-	-
Finance costs (excluding distributions)		2,192	-	-	-
Insurance		1,350	2,369	1,350	2,369
Investment property expenses		10,732	-	-	-
Management fees		7,829	4,811	7,774	4,811
Other costs		4,332	-	-	-
		49,314	10,884	15,003	10,884
Net profit before distributions		62,940	38,974	53,804	38,974
Distribution expense to unitholders	6	54,251	38,974	53,804	38,974
Contribution to net assets attributable to unitholders		8,687	-	-	-

Reconciliation of net assets attributable to unitholders		
Transfer to unitholders' funds	6,507	-
Transfer to minority interest	2,180	-
	8,687	-

The Income Statements are to be read in conjunction with the notes to the financial statement.

Financial statements

Statement of Changes in Equity for the year ended 30 June 2006

Under previous GAAP unitholders' funds were classified as equity. As outlined in note 23, under AIFRS unitholders' funds are classified as a liability. Consequently, under AIFRS, there have been no changes in the equity in the relevant periods. A reconciliation of movements in unitholders funds is included in note 5.

The Statement of Changes in Equity is to be read in conjunction with the notes to the financial statements.

Balance Sheets as at 30 June 2006

	Note	Consolidated 2006 $'000	Consolidated 2005 $'000	Trust 2006 $'000	Trust 2005 $'000
Assets					
Current assets					
Cash and cash equivalents		48,974	37,029	48,974	33,320
Inventory	7	-	299	-	-
Mortgage loans	8	266,753	268,602	266,753	268,602
Investments	9(a)	202,542	152,035	202,542	192,035
Trade and other receivables	10	2,587	8,334	2,587	852
Total current assets		520,856	466,299	520,856	494,809
Non-current assets					
Mortgage loans	8	61,018	45,510	61,018	45,510
Property, plant and equipment	11	-	1,406	-	-
Investment property	12	-	77,084	-	-
Investments	9(b)	129,713	-	129,713	-
Total non-current assets		190,731	124,000	190,731	45,510
Total Assets		711,587	590,299	711,587	540,319
Liabilities					
Current liabilities					
Trade and other payables	13	2,185	11,233	2,185	2,002
Distribution payable	6	4,607	3,181	4,607	3,181
Employee Benefits	14	-	204	-	-
Interest bearing loans and borrowings	15(a)	-	4,464	-	-
Total current liabilities		6,792	19,082	6,792	5,183
Non-current liabilities					
Interest bearing loans and borrowings	15(b)	-	36,081	-	-
		-	36,081	-	-
Total Liabilities (excluding net assets attributable to unitholders)		6,792	55,163	6,792	5,183
Net Assets attributable to unitholders - Liability	5	704,795	535,136	704,795	535,136
Represented by:					
Total Net Assets attributable to unitholders		704,795	535,136	704,795	535,136

The Balance Sheets are to be read in conjunction with the notes to the financial statements.

Statements of Cash Flows for the financial year ended 30 June 2006

	Note	Consolidated		Trust	
		2006 $'000	2005 $'000	2006 $'000	2005 $'000
Cash flows from operating activities					
Interest, fees and investment income received		41,599	28,012	44,423	28,012
Other cash payments in the course of business		(49,068)	(11,586)	(16,464)	(11,586)
Investment property income received		33,218	-	-	-
Net cash provided by/(used in) operating activities	19(a)	25,749	16,426	27,959	16,426
Cash flows from investing activities					
Mortgage loan advances		(195,584)	(161,785)	(195,584)	(161,785)
Mortgage loan repayments		161,263	183,864	161,263	183,863
Purchase of investments in managed investment schemes		(161,420)	(67,534)	(165,210)	(67,534)
Redemption of investments in managed investment schemes		61,768	264	61,768	264
Payments for controlled entities net of cash acquired		-	3,708	-	-
Short-term advance repaid		-	15,000	-	15,000
Investment properties purchased		(2,335)	-	-	-
Loan to related entity		(1,623)	-	-	-
Fixed interest securities purchased		(53,573)	-	(53,573)	-
Fixed interest securities redeemed		26,173	-	26,173	-
Promissory & unsecured notes purchased		(27,295)	(146,579)	(27,295)	(146,579)
Promissory & unsecured notes redeemed		44,295	124,579	44,295	124,579
Other investments purchased		(65,282)	(77,888)	(65,282)	(77,888)
Other investments repaid		83,859	16,499	83,860	16,499
Net cash provided by/(used in) investing activities		(129,754)	(109,872)	(129,585)	(113,581)
Cash flows from financing activities					
Proceeds from borrowings		13,580	-	-	-
Repayment of borrowings		(9,185)	-	-	-
Transaction costs relating to issue		(5,336)	-	-	-
Applications for units		385,826	291,229	385,826	291,229
Redemptions of units		(216,166)	(134,583)	(216,166)	(134,583)
Distributions paid		(52,652)	(37,186)	(52,380)	(37,186)
Net cash provided by/(used in) financing activities		116,067	119,460	117,280	119,460
Net increase in cash held		12,062	26,014	15,654	22,305
Cash at the beginning of the financial year		37,029	11,015	33,320	11,015
Less: Cash of deconsolidated entities		(117)	-	-	-
Cash at the end of the period	19(b)	48,974	37,029	48,974	33,320

The Statements of Cash Flows are to be read in conjunction with the notes to the financial statements.

Notes to the Consolidated Financial Statements for the year ended 30 June 2006

1. Statement of accounting policies

MFS Premium Income Fund (the "Trust") is domiciled in Australia. The consolidated financial report of the Trust for the year ended 30 June 2006 comprises the results from the Trust and its subsidiaries (together referred to as the "consolidated entity").

The financial report was authorised for issue by the directors of the Responsible Entity on ?? September 2006.

The significant accounting policies which have been adopted in the preparation of this consolidated financial report are outlined below.

(a) Statement of Compliance

The consolidated financial report is a general purpose financial report which has been prepared in accordance with Australian Accounting Standards adopted by the Australian Accounting Standards Board ("AASB"), the Corporations Act 2001 and the Trust's Constitution.

International Financial Reporting Standards ("IFRS") form the basis of Australian Accounting Standards adopted by the AASB, being Australian equivalents to IFRS ("AIFRS"). The financial report complies with IFRS and interpretations adopted by the International Accounting Standard Board.

This is the Trust's first financial report prepared in accordance with Australian Accounting Standards, being AIFRS and AASB 1 First-Time Adoption of Australian Equivalents to International Financial Reporting Standards has been applied. An explanation of how the transition to AIFRS has affected the reported financial position, financial performance and cash flows of the entity is provided in note 23. This note includes reconciliations of equity and profit or loss for comparative periods reported under Australian Generally Accepted Accounting Principles ("previous GAAP") to those reported for those periods under AIFRS.

(b) Basis of preparation

The financial report is presented in Australian dollars.

This consolidated financial report has elected to early adopt the following accounting standards and amendments:

AASB standard/ amendment	Affected standard(s)	
AASB 2005-1	AASB 139	Financial Instruments: Recognition and Measurement
AASB 2005-4	AASB 1	First-time adoption of Australian Equivalents to International Financial Reporting Standards
	AASB 139	Financial Instruments: Recognition and Measurement
	AASB 132	Financial Instruments: Disclosure and Presentation
AASB 2005-6	AASB 3	Business Combinations
AASB 2006-2	AASB 1	First-time adoption of Australian Equivalents to International Financial Reporting Standards

Notes to the Consolidated Financial Statements for the year ended 30 June 2006

1. Statement of accounting policies (continued)

The following standards and amendments were available for early adoption but have not been applied in this consolidated financial report:

AASB amendment	Affected standard(s)	Nature of change in accounting policy	Application date of standard*
New standard	AASB 7 Financial Instruments: Disclosure (August 2005)	Replacing the presentation requirements of financial instruments in AASB 132. No impact is anticipated on the financial results of the consolidated entity; however additional disclosure requirements such as sensitivity analyses are quite extensive.	1 Jan 07
AASB 2005-10	AASB 1 First-time adoption of Australian Equivalents to International Financial Reporting Standards AASB 101 Presentation of Financial Statements AASB 114 Segment Reporting AASB 132 Financial Instruments: Disclosure and Presentation AASB 139 Financial Instruments: Recognition and Measurement	Consequential amendments arising from the release of AASB 7 Financial Instruments: Disclosure (August 2005). No impact is anticipated on the financial result of the consolidated entity.	1 Jan 07

** Application date is for the annual reporting periods beginning on or after the date shown in the above table.*

It is anticipated that AASB 7 and AASB 2005-10 will be adopted in the financial report ending 30 June 2007.

The annual financial report is prepared on the basis of fair value measurement of assets and liabilities except where otherwise stated.

The preparation of a financial report in conformity with Australian Accounting Standards requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

(b) Basis of preparation (continued)

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

Judgements made by management in the application of Australian Accounting Standards that have a significant effect on the financial report and estimates with a significant risk of material adjustment in the next year are discussed in note 2. The accounting policies set out below have been applied consistently to all periods presented in the consolidated financial report and in preparing an opening AIFRS balance sheet at 1 July 2004 for the purposes of the transition to Australian Accounting Standards – AIFRS.

The accounting policies have been applied consistently throughout the entity for the purposes of the consolidated financial report.

(c) Basis of consolidation

Subsidiaries

Subsidiaries are entities controlled by the Trust. Control exists when the Trust has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that presently are exercisable or convertible are taken into account. The financial statements of subsidiaries are included in the consolidated financial report from the date that control commences until the date that control ceases.

Transactions eliminated on consolidation

Intragroup balances, and any unrealised gains and losses or income and expenses arising from intragroup transactions, are eliminated in preparing the consolidated financial statements.

Unrealised gains arising from transactions with associates and jointly controlled entities are eliminated to the extent of the consolidated entity's interest in the entity with adjustments made to the "Investments accounted for using the equity method" and "Share of profit of associates accounted for using the equity method" accounts.

Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

Changes in ownership interest

Loss of control, no joint control or significant influence

When control ceases, a gain or loss is recognised as the difference between net sales proceeds, if any, and the consolidated carrying amount (including post-acquisition share of profits, goodwill and equity). Any remaining investment is then accounted for in accordance with AASB 139 Financial Instruments: Recognition and Measurement (refer Accounting Policy 1(i)).

Notes to the Consolidated Financial Statements for the year ended 30 June 2006

1. Statement of accounting policies (continued)

Loss of control, joint control or significant influence retained

When control ceases but significant influence or joint control is retained, the carrying amount at the date of change in status of the investment is measured at fair value accordance with AASB 139 Financial Instruments: Recognition and Measurement, with changes in fair value recognised in the profit and loss in the period of change.

Retention of control

When some or all of the ownership interest is sold, but control is retained, the gain or loss on sale is recognised as the difference between the net sales proceeds, if any, and consolidated carrying amount portion adjusted for the net pre-acquisition profits, goodwill and equity relating to the portion sold.

(d) Revenue recognition

Interest income

Interest income and expense is recognised in the income statement as it accrues, using the original effective interest rate of the instrument calculated at the acquisition or origination date. Interest income includes the amortisation of any discount or premium, transaction costs or other differences between the initial carrying amount of an interest-bearing instrument and its amount at maturity calculated on an effective interest rate basis.

Interest income is recognised on a gross basis, including withholding tax, if any.

Investment and distribution income

Income from Debt units or Preferential units where the income is effectively of a fixed nature is recognised as it accrues.

Income from managed investment schemes and fixed securities is recognised on an accruals basis and is thus accounted for in the period to which the income relates.

Revenue from distributions from controlled entities is recognised by the Trust when declared by the controlled entities.

Revenue from managed investments schemes where the Responsible Entity is a controlled entity of MFS Limited (the ultimate parent entity of the entity's Responsible Entity) is recognised on an accruals basis.

Revenue from dividends and distributions from other investments is recognised at the earlier of declaration or receipt.

Dividends received out of pre-acquisition reserves are eliminated against the carrying amount of the investment and not recognised in revenue.

Realised profit and loss on sale

The gain or loss on disposal of current investment assets are recognised as revenue or expense at the date that control of the asset passes to the buyer, usually the settlement date of the contract note.

The gain or loss on disposal is calculated as the difference between the carrying amount of the asset at the time of disposal and the net proceeds on disposal (including incidental costs).

(d) Revenue recognition (continued)

Investment property income

Accommodation services

Revenue from holiday lettings is recognised when the services have been provided to the customer.

Sale of goods

Revenue from the sale of goods is recognised when ownership of the goods has been passed to the buyer.

Loan and other fees

Loan fees include exit fees on loans and are recognised at the earlier of receipt or when the quantum and receipt of the fees is considered virtually certain. Where fees relate to a loan which is still outstanding at balance date, the fees are recognised as income on an accruals basis.

All other fees are recognised as income on an accruals basis.

(e) Expenses

All expenses, including management fees and custodian fees, are recognised on an accruals basis.

(f) Depreciation

With the exception of investment property which is not depreciated, property, plant and equipment is depreciated on a straight-line basis over the estimated useful life of the asset.

(g) Investment properties

Investment properties comprise investment interests in land and buildings (including integral plant and equipment) held for the purpose of letting to produce rental income or for capital appreciation or both. These investment properties typically include the freehold title to the "manager's unit" in a resort complex, together with the management letting rights. The management letting rights are usually tied to the manager's unit, and the owner is restricted from selling one without the other.

Investment properties are initially recognised at cost, including any directly attributable expenditure including legal fees, valuation fees, stamp duty and taxes and other transaction costs.

Investment properties are subsequently recognised at fair value, with values being reassessed at least twice yearly, including as at 30 June and 31 December each year. The assessment of fair value may be determined by an independent professional valuer, or may be assessed internally by re-modelling the previous independent valuation with updated financial data on occupancies, room rates and expenses.

Valuations are prepared by considering the expected net cash flows that will be generated from the ownership of the properties and associated letting rights, and by applying a "years purchase" multiple which reflects the specific risks inherent in the net cash flows. The multiples used, are based on recommendations from independent professional valuers, having regard to economic

Notes to the Consolidated Financial Statements for the year ended 30 June 2006

(g) Investment properties (continued)

and market conditions, including prices at which other properties and letting rights have changed hands in recent times. The multiples currently applied vary from 4.0 to 5.4 years, depending on the location and nature of the property.

Any gain or loss arising from a change in fair value is recognised in the income statement.

If an investment property becomes owner-occupied, then it is reclassified as property, plant and equipment and its fair value at the date of reclassification becomes its cost for accounting purposes.

When an item of property, plant and equipment is transferred to investment property following a change in its use, any difference arising at the date of transfer between the carrying amount of the item immediately prior to transfer and its fair value is recognised directly in net assets attributable to unitholders if it is a gain. Upon disposal of the item the gain is transferred to net assets attributable to unitholders. Any loss arising in this manner is recognised immediately in the income statement.

(h) Property, plant and equipment

Property that is being constructed or developed for future use as investment property is classified as property, plant and equipment, and stated at cost until construction or development is complete, at which time it is reclassified as investment property.

Plant and equipment that are not considered to be integral to an investment property are recognised separately on the balance sheet.

Property, plant and equipment are stated at cost, or deemed cost, less accumulated depreciation and impairment losses.

(i) Investments

Investments in Controlled Entities

Investments in controlled entities are carried at the lower of cost and recoverable amount.

Investments in equity instruments

Investments held for trading are classified as current assets and are stated at fair value, with any resultant gain or loss recognised in the income statement.

Investments classified as available-for-sale are recorded as current assets and are stated at fair value, with any resultant gain or loss recognised in unitholder's funds.

Investments held to maturity are classified as non-current if the investment does not mature within twelve months of balance date. Investments held to maturity are valued at cost and are subject to a test for impairment (refer note 1(l)).

Financial instruments classified as held for trading or available-for-sale investments are recognised/derecognised by the consolidated entity on the date it commits to purchase/sell the investments. Securities held to maturity are recognised/derecognised on the day they are transferred to/by the consolidated entity.

(i) Investments (continued)

Other financial investments held by the consolidated entity are designated at fair value through profit and loss upon initial recognition. These include financial assets that are not held for trading purposes and which may be sold. These include investments in fixed interest securities, equity instruments and units in unlisted managed investment schemes. The fair value through profit or loss classification is in accordance with AASB 2005-4 Amendments to Australian Accounting Standards. The fair value through profit or loss classification is used for the majority of the financial assets held by the Consolidated Entity and the liabilities arising from the units on issue must be fair valued. Therefore not fair valuing the financial assets used in calculating the fair value of the liability would result in an accounting mismatch.

Fair value measurement principles

The fair value of investments is based on the last quoted sale price as at the close of business on reporting date without any deduction for estimated future selling costs.

Investments for which market quotations are not readily available are valued at the net fair value determined by the Responsible Entity. Alternative methods used include, the net asset value per share based on the last audited financial statements of the entity, valuation based on the last sale price or, the redemption price as at reporting date.

(j) Mortgage loans

Mortgage loans held by the consolidated entity are classified as loans and are stated at amortised cost, with any impairment loss, if any recognised directly in the income statement (refer note 1(l)). The carrying amount of the mortgage loans represents principal less repayments, plus any compound interest. Interest is calculated using the effective interest method.

(k) Trade and other receivables

Financial assets that are classified as loans and receivables include mortgage loans and accounts receivable and are carried at amortised cost using the effective interest rate (where relevant), less impairment loss identified (see accounting note 1(l)).

(l) Impairment

Financial assets that are stated at cost or amortised cost are reviewed at each balance sheet date to determine whether there is objective evidence of impairment. If any such indication exists, an impairment loss is recognised in the income statement as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate.

The carrying amount of the entity's assets, other than financial assets noted in the preceding paragraph, are reviewed at each balance date to determine whether there is any indication of impairment. If any such indication exists, the assets recoverable amount is estimated.

An impairment loss is recognised whenever the carrying amount of an asset or its cash generating unit exceeds its recoverable amount.

Notes to the Consolidated Financial Statements for the year ended 30 June 2006

(l) Impairment (continued)

If in a subsequent period, the amount of an impairment loss recognised decreases and the decrease can be linked objectively to an event occurring after the write-down, the write-down is reversed through the income statement.

An impairment loss in respect of a receivable carried at amortised cost is reversed if the subsequent increase in recoverable amount can be related objectively to an event occurring after the impairment loss was recognised.

Calculation of recoverable amount

The recoverable amount of the consolidated entity's receivables carried at amortised cost is calculated as the present value of estimated future cash flows, discounted at the original effective interest rate (i.e., the effective interest rate computed at initial recognition of these financial assets). Receivables with a short duration are not discounted.

Impairment of receivables is not recognised until objective evidence is available that a loss event has occurred. Significant receivables are individually assessed for impairment. Receivables that are not assessed as impaired are placed into portfolios of assets with similar risk profiles and a collective assessment of impairment is performed. Non-significant receivables are not individually assessed. Instead, impairment testing is performed by placing non-significant receivables in portfolios of similar risk profiles, based on objective evidence from historical experience adjusted for any effects of conditions existing at each balance date.

An impairment loss in respect of a receivable carried at amortised cost is reversed if the subsequent increase in recoverable amount can be related objectively to an event occurring after the impairment loss was recognised.

An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

(m) Cash and cash equivalents

Cash comprises current deposits with banks. Cash equivalents are short-term highly liquid investments that are readily convertible to known amounts of cash, are subject to an insignificant risk of changes in value, and are held for the purpose of meeting short-term cash commitments rather than for investment or other purposes.

(n) Inventories

Inventories are carried at the lower of cost and net realisable value. Costs are assigned on a first-in-first out basis and include direct materials, direct labour and an appropriate proportion of variable and fixed overhead expenses.

(o) Trade and other payables

Financial liabilities that are not at fair value through profit or loss include accounts payable which are measured at amortised cost. Trade payables are recognised for amounts to be paid in the future for goods or services received. Trade accounts payable are normally settled within 60 days.

(p) Provisions

Employee benefits

Liabilities for employee benefits for wages and salaries and annual leave represent the present obligations resulting from employees' services provided to reporting date, calculated at undiscounted amounts based on wage and salary rates the consolidated entity expects to pay as at reporting date including related on-costs, such as, workers compensation insurance and payroll tax.

(q) Interest bearing liabilities

Bank loans are recognised initially at their fair value, adjusted for attributable transaction costs, subject to set-off arrangements. Subsequent to initial recognition, the bank loans are stated at amortised cost with any difference between cost and redemption value being recognised in the income statement over the period of the borrowings on an effective interest basis. Interest expense is accrued at the contracted rate.

(r) Distributions and income tax

Under current income tax legislation, the Trust is not subject to income tax, provided that the taxable income is fully distributed to unitholders.

Realised capital losses are not distributed to unitholders but are retained in the Trust to be offset against any future realised capital gains.

(s) Changes in net assets attributable to unitholders

Non-distributable income, which may comprise unrealised changes in the fair value of investments, net capital losses, tax-deferred income, accrued income not yet assessable and non-deductible expenses are reflected in the profit and loss as change in net assets attributable to unitholders.

These items are included in the determination of distributable income in the period for which they are assessable or deductible for taxation purposes.

(t) Issue costs

Costs incurred, that are directly in connection with the issue of units, are netted against the funds raised.

(u) Goods and services tax

Revenues, expenses and assets are recognised net of the amount of goods and services tax (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 expense. Receivables and payables are stated with the amount of GST included. The net amount of GST recoverable from, or payable to, the ATO is included as a current asset or liability in the balance sheet.

Cash flows are included in the statement of cash flows on a gross basis. The GST components of cash flows arising from investing and financing activities which are recoverable from, or payable to, the ATO are classified as operating cash flows.

Notes to the Consolidated Financial Statements for the year ended 30 June 2006

(v) Finance costs

Distributions paid and payable on units are recognised in the income statement on an accruals basis as finance costs.

(w) Units issued to unitholders

Financial liabilities arising from the redeemable units issued by the Trust are carried at the redemption amount representing the investors' right to a residual interest in the Trust's assets, approximating fair value at reporting date. The ordinary units issued by the Trust satisfy the definition of "redeemable" units and are therefore recorded as a financial liability.

2. Accounting estimates and judgements

The majority of the Trust's financial instruments are carried at fair value on the Balance Sheet. For the listed securities a quoted market price is readily available. However, financial instruments such as unlisted units in managed investment schemes, unquoted securities and other equity units are valued using valuation techniques. These fair value estimates are subjective in nature and involve uncertainties and matters of significant judgement and therefore, cannot be determined with precision. The major methods and assumptions used in estimating the fair values of financial instruments were disclosed in notes 1(g) and 1(i).

For other financial instruments, including receivables, payables and accrued expenses, the carrying amounts approximate fair value due to their short-term nature.

3. Revenue

(a) Interest income

	2006			2005		
Consolidated	**Monthly average balance $'000**	**Interest income $'000**	**Average rate %**	**Monthly average balance $'000**	**Interest income $'000**	**Average rate %**
Cash and cash equivalents	80,845	4,355	5.38	48,464	2,517	5.19
Mortgage loans	312,347	35,458	11.35	315,439	36,362	11.53
Promissory & unsecured notes	15,583	1,999	12.82	26,918	3,068	11.40
Fixed interest securities	19,805	1,368	6.90	-	-	-
Other investments	73,502	8,108	11.03	38,198	3,605	9.44
		51,288			45,552	
Trust						
Cash and cash equivalents	79,716	4,349	5.46	48,464	2,517	5.19
Mortgage loans	312,347	35,458	11.35	315,439	36,362	11.53
Promissory & unsecured notes	15,583	1,999	12.82	26,918	3,068	11.40
Fixed interest securities	19,805	1,368	6.90	-	-	-
Other investments	73,502	8,108	11.03	38,198	3,605	9.44
		51,282			45,552	

3. Revenue (continued)

(b) Investment income in managed investment schemes

Consolidated	2006 Monthly average balance $'000	2006 Interest income $'000	2006 Average rate %	2005 Monthly average balance $'000	2005 Interest income $'000	2005 Average rate %
Unrelated managed investment schemes	50,993	4,961	9.72	-	-	-
Related managed investment schemes	43,388	5,450	12.56	27,231	2,489	9.14
		10,411			2,489	
Trust						
Unrelated managed investment schemes	50,993	4,961	9.72	-	-	-
Related managed investment schemes	74,823	8,496	11.35	27,231	2,489	9.14
		13,457			2,489	

(c) Loan and other fees

	Consolidated 2006 $'000	Consolidated 2005 $'000	Trust 2006 $'000	Trust 2005 $'000
Fees mortgage loans	510	1,817	510	1,817
Investor penalties	15	-	15	-
Rebateable commission	190	-	190	-
Guarantor fee	35	-	35	-
	750	1,817	750	1,817

4. Scheme expenses

	Consolidated 2006 $	Consolidated 2005 $	Trust 2006 $	Trust 2005 $
Auditors' remuneration				
Audit and review of the financial report:				
- KPMG	18,263	15,573	18,263	15,573
- PKF	75,230	-	-	-
Other regulatory audit services – KPMG	6,650	9,500	6,650	9,500
Other services – KPMG	11,167	4,500	4,500	4,500
	111,310	29,573	29,413	29,573

Notes to the Consolidated Financial Statements for the year ended 30 June 2006

5. Net assets attributable to unitholders - liability

Consolidated	For the year ended		For the year ended	
	30-Jun-06 Units '000	30-Jun-06 $'000	30-Jun-05 Units '000	30-Jun-05 $'000
Opening balance	535,136	535,136	378,490	378,490
Applications				
- Cash	447,840	447,840	277,662	277,662
- Reinvestments	17,944	17,944	13,567	13,567
Redemptions	(296,125)	(296,125)	(134,583)	(134,583)
Undistributed profit	6,507	6,507	-	-
Impact of deconsolidation of consolidated entity	(6,507)	(6,507)	-	-
Closing balance	704,795	704,795	535,136	535,136
Trust				
Opening balance	535,136	535,136	378,490	378,490
Applications				
- Cash	447,840	447,840	277,662	277,662
- Reinvestments	17,944	17,944	13,567	13,567
Redemptions	(296,125)	(296,125)	(134,583)	(134,583)
Closing balance	704,795	704,795	535,136	535,136

Under the Trust's constitution, each unit represents a right to the underlying assets of the Trust.

Under previous GAAP the consolidated entity classified unitholders' funds as equity. In accordance with AIFRS unitholders' funds are now classified as a liability.

6. Unitholder distributions

	Consolidated		Trust	
	2006 $'000	2005 $'000	2006 $'000	2005 $'000
During the reporting period distributions paid or payable:				
- Distributions paid/reinvested	49,469	35,793	49,197	35,793
- Distributions payable by PIF	4,607	3,181	4,607	3,181
- Distributions paid by controlled entities	175	-	-	-
	54,251	38,974	53,804	38,974

7. Inventory

	Consolidated		Trust	
	2006 $'000	2005 $'000	2006 $'000	2005 $'000
Finished goods at cost	-	299	-	-

8. Mortgage loans

	Consolidated		Trust	
	2006 $'000	2005 $'000	2006 $'000	2005 $'000
Current				
Mortgage loans	266,753	268,602	266,753	268,602
Non-current				
Mortgage loans	61,018	45,510	61,018	45,510
Total mortgage loans	327,771	314,112	327,771	314,112

Mortgage loans are secured by registered mortgages. The recoverability of mortgage loans is supported by valuations completed by registered valuers for mortgage security purposes and loan to valuation ratios not exceeding 66.67%.

As at 30 June 2006, there were 5 loans past due for repayment (2005: 9 loans) with a total principal balance of $46,513,600 (2005: $43,030,431). The directors do not expect any loss to be incurred in relation to these loans.

Subject to MFS Investment Management Limited operating within the lending policy stipulated in the insurance policy, Underwriters, Lloyd's of London, have indemnified MFS Investment Management Limited and the Trust should the proceeds of a forced sale of mortgaged property impair the repayment of the mortgage. The maximum loss covered by the policy is 66.67% of each mortgage amount or $3,000,000 whichever is the lesser.

Notes to the Consolidated Financial Statements for the year ended 30 June 2006

9. Investments

	Consolidated		Trust	
	2006 $'000	2005 $'000	2006 $'000	2005 $'000
(a) Current				
Managed investment schemes				
Debt units in a related managed investment scheme				
- MFS Optimiser One	21,304	26,073	21,304	26,073
	21,304	26,073	21,304	26,073
Managed investment schemes				
Equity units in a related managed investment schemes				
- MFS Optimiser One	3,680	-	3,680	-
- MFS Mirage Preferential Units	-	20,000	-	20,000
- MFS Diversified Trust	14,621	-	14,621	-
- MFS Resort Asset Income Trust	22,683	-	22,683	39,600
- MFS Resort Asset Equity Trust	229	-	229	400
	41,213	20,000	41,213	60,000
Promissory & unsecured notes				
MFS Pacific Finance Limited	-	5,000	-	5,000
MFS Group Notes	-	22,000	-	22,000
Other unrelated investments	10,000	-	10,000	-
	10,000	27,000	10,000	27,000
Fixed interest securities				
Fixed securities	26,247	-	26,247	-
	26,247	-	26,247	-
Other investments				
Loans in a related trust				
- MFS PECS Trust	1,015	-	1,015	-
- MFS 200 Queen Street Property Trust	12,336	-	12,336	-
Loans to other external parties	90,427	78,962	90,427	78,962
	103,778	78,962	103,778	78,962
Total current investments	**202,542**	**152,035**	**202,542**	**192,035**
(b) Non-current				
Managed investment schemes				
Equity units in unrelated managed investment schemes	129,713	-	129,713	-
Total investments	**332,255**	**152,035**	**332,255**	**192,035**

10. Receivables

	Consolidated		Trust	
	2006 $'000	2005 $'000	2006 $'000	2005 $'000
Trade Debtors	110	6,769	110	-
Interest receivable	2,298	1,239	2,298	802
GST receivable	179	326	179	50
	2,587	8,334	2,587	852

11. Property, plant and equipment

Plant and equipment	-	1,406	-	-

No depreciation was charged during 2005 as the consolidated entity was formed on 30 June 2005.

Property, plant and equipment recorded at acquired cost equivalent to fair value.

12. Investment property Management Letting Rights

Opening balance at 1 July	77,084	-	-	-
Additions/(disposals)	(77,084)	77,084	-	-
Net gain from fair value adjustment	-	-	-	-
	-	77,084	-	-

Investment properties are stated at fair values, which have been determined based on valuations performed by Herron Todd White Valuers (Gold Coast) Pty Ltd.

13. Payables

Accounts payable	107	3,084	107	921
Accrued expenses	2,055	1,056	2,055	1,056
Withholding tax payable	23	25	23	25
Unsecured loans	-	7,068	-	-
	2,185	11,233	2,185	2,002

14. Employee Benefits

Liability for annual leave	-	204	-	-
Number of employees at year end	-	380	-	-

Notes to the Consolidated Financial Statements for the year ended 30 June 2006

15. Interest bearing liabilities

	Consolidated		Trust	
	2006 $'000	2005 $'000	2006 $'000	2005 $'000
(a) Current				
Bank bills secured	-	4,464	-	-
(b) Non-current				
Bank bills secured	-	36,081	-	-
Total secured liabilities	-	40,545	-	-
Financing arrangements				
Bank bills	-	40,545	-	-
	-	40,545	-	-
Facilities utilised at balance date				
Bank bills	-	40,545	-	-
	-	40,545	-	-
Facilities not utilised at balance date				
Bank bills	-	-	-	-

Commercial bill facilities are secured by first registered mortgages over all buildings, first registered mortgage debentures over BreakFree Resorts Pty Ltd, Breakfree Holidays Pty Ltd, Breakfree Resorts (NSW) Pty Ltd and Breakfree Ltd and deed of consent/charge over all management and letting rights. The weighted average interest rate for 2005 is 5.9%.

16. Related parties

Responsible Entity

The Responsible Entity of MFS Premium Income Fund during the financial year was MFS Investment Management Limited (ABN 20 101 634 146) whose immediate and ultimate holding companies are MFS Property Ltd (ABN 62 101 069 381) and MFS Limited (ABN 90 107 863 436) respectively.

Custodian

The custodian of the trust is Perpetual Nominees Limited (ACN 000 733 700). Custodian fees have been paid by the Trust.

Directors

The names of the persons who were directors of the Responsible Entity during the financial year are as follow:

Name	Period of directorship
Mr Philip William Adams	Appointed 15 July 1999
	Resigned 28 November 2005
Mr Spencer Martin Young	Appointed 7 October 1999
	Resigned 6 October 2005
Mr Michael Christodoulou King	Appointed 8 August 2002
Mr Michael Gordon Hiscock	Appointed 15 May 2003
Mr Paul Joseph Manka	Appointed 15 May 2003
Mr Craig Robert White	Appointed 31 August 2005

Remuneration of key management personnel of the Responsible Entity

The directors have not received any remuneration from the Responsible Entity, the Trust, or any of the entities formerly controlled by the Trust.

Under the new remuneration structure, MFS Investment Management Limited is entitled to receive:

- All surplus funds generated by the Trust only after all current distribution, redemption and expense obligations have been satisfied at the end of each month.
- Reimbursement of Trust expenses incurred by MFS Investment Management Limited on behalf of the Trust.

Notes to the Consolidated Financial Statements for the year ended 30 June 2006

16. Related parties (continued)

Transactions with related parties are set out below:

	Trust	
	2006 $	2005 $
Total fees paid or payable:		
· Management Fees for the year	7,773,534	4,811,478
· Other expenses included administration expenses incurred by the Responsible Entity, which are reimbursed to the Responsible Entity in accordance with the provisions of the Constitution.	3,231,695*	162,695
· MFS Princes Street Property Trust guarantee fee	22	-
· MFS Administration Pty Ltd	110,479	-

The aggregate amounts payable to related parties at balance date are as follows:

· Responsible Entity	1,216,280	460,090
· MFS Administration Pty Ltd	55,630	-

These amounts are included in accounts payable and accrued expenses.

** Following the introduction of the new management fee structure (i.e. Surplus after all Trust expenses, distributions and redemptions obligations are met) there is an increase in the value of the Trust expenses paid and reimbursed to the Responsible Entity this year.*

It is important to note that the overall cost of operating the Trust (i.e. Total Trust expenses, including insurance and management fees) for the year was the same as the previous year (2.35% - based on weighted average unit holder value). The increase in reimbursement of Trust expenses to the Responsible Entity has not resulted in an increase in total cost to the investor.

16. Related parties (continued)

Related party investments held by the Trust

Set out below are details of the Trust's investments with related parties managed by the Responsible Entity or its associates.

All transactions with related parties are conducted on normal commercial terms and conditions.

2006 Trust **Related Party**	**Interest held in related Trust as as 30 June 2006** **$**	**Investments during the year** **$**	**Repayments during the year** **$**	**Contribution investment Income** **$**
Loan to MFS Living and Leisure Trust	-	52,145	4,841,355	487,798
Loan to MFS Bale Port Douglas	-	20,036,114	42,158,501	2,191,013
Loan to MFS 200 Queen Street Property Trust	12,335,728	12,075,740	-	259,988
Investments in related parties				
MFS Group Notes	-	7,000,000	29,000,000	1,396,356
MFS Pacific Finance Ltd unsecured notes 231,315		-	13,000,000	18,000,000
Equity units in MFS Optimiser One	3,679,871	11,310,714	7,630,843	723,546
Equity units in MFS Diversified Trust	15,038,461	15,038,461	-	422,394
Equity units in MFS PECS Trust	5,000	5,000	-	-
Equity Units in MFS Resort Asset Investment Fund	20,642,000	3,790,000	23,148,000	3,379,297
	41,219,029	47,319,914	77,363,458	6,152,908
Loans to related parties				
Debt units in MFS Optimiser One (formerly MFS Diversified Property Securities Trust)	21,304,103	6,536,806	11,305,714	1,614,267
Loan to MFS PECS Trust	1,010,000	1,010,000	-	18,402
Debt units in MFS Mirage Investment Trust	-	-	20,000,000	2,356,164
	22,314,103	7,546,806	31,305,714	3,988,833

Notes to the Consolidated Financial Statements for the year ended 30 June 2006

16. Related parties (continued)

2005 Trust Related Party	Interest held in related Trust as as 30 June 2005 Units	Investments during the year $	Repayments during the year $	Contribution to investment income $
Investments in related parties				
MFS Group Notes	22,000,000	62,000,000	40,000,000	2,520,927
MFS Securities & Underwriting	-	55,597,449	55,597,449	502,014
MFS Pacific Finance Ltd unsecured notes	5,000,000	5,000,000	-	45,205
Equity Units in MFS Resort Asset Investment Fund	40,000,000	40,000,000	-	-
	67,000,000	162,597,449	95,597,449	3,068,146
Loans to related parties				
Loan to MFS LIST	-	-	350,000	5,425
Loan to MFS Living and Leisure Trust	4,789,210	4,789,210	600,000	618,528
Loan to MFS Diversified Trust	-	-	4,000,000	89,753
Loan to MFS Bale Port Douglas	19,931,374	19,931,374	-	269,814
Debt units in MFS Optimiser One (formerly MFS Diversified Property Securities Trust)	26,073,011	2,534,000	264,000	2,091,370
Debt units in MFS Mirage Investment Trust	20,000,000	20,000,000	-	339,726
	70,793,595	47,254,584	5,214,000	3,414,616

Related party investments held in the Trust

2006 Trust Related Party	Investment held by related party $	Investments during the year $	Repayments during the year $	Distribution paid during the year $
MFS Wholesale Premium Income Fund	61,077,053	63,685,140	35,026,589	3,773,339
MFS L&L Management Limited	-	-	100,000	993
Michael C King Superannuation Fund	38,726	3,142	-	3,142
2005 Trust				
Related party				
MFS Wholesale Premium Income Fund	32,418,502	49,434,107	17,015,605	1,236,682
MFS L&L Management Limited	100,000	100,000	-	2,209
Michael C King Superannuation Fund	35,584	35,584	-	1,884

17. Segment information

A segment is a distinguishable component of the Consolidated Entity that is engaged either in a business segment or based on the Consolidated Entity's asset classes within a particular geographical segment based on the geographical location of the assets, which is subject to risks and rewards that are different from those of other segments.

The net operating profit for the period of $62,939,679 (2005: $38,973,778) for the Consolidated Entity included contributions from the secured mortgage finance operations and the Resorts Trusts which operates in the resort management letting rights business in Australia. Resorts are located across key leisure destinations including Gold Coast, Sunshine Coast, Far North Queensland and Northern NSW.

The Trust operates predominantly in the property investment industry within Australia. The Trust's operations and customers are located predominantly in Australia. The Trust provides mortgage secured finance to its customers.

The secured mortgage finance operations net profit for the period was $53,803,880 (2005: $38,973,778) and gross assets were $711,587,387 (2005: $540,318,973). The gross liabilities, excluding unitholders' funds, were $6,792,283 (2005: $5,183,290).

18. Contingent assets and liabilities

The Trust did not have any material contingent asset and liabilities as at 30 June 2006 (2005: nil).

19. Notes to the statement of cash flows

(a) Reconciliation of net cash provided by operating activities to net profit

	Consolidated		Trust	
	2006 $'000	2005 $'000	2006 $'000	2005 $'000
Net profit	62,940	38,974	53,804	38,974
Non-cash flows				
- Depreciation	436	-	-	-
- Gain on investment	(10,261)	-	-	-
- Capitalised interest and insurance	(20,445)	(19,763)	(20,445)	(19,763)
- Unrealised (profit)/loss	-	-	(75)	-
Changes in assets and liabilities during the financial year:				
- Decrease/(increase) in receivables	(6,480)	(2,344)	(5,510)	(2,344)
- Decrease/(increase) in inventory	3	-	-	-
- (Decrease)/increase in payables	2,237	171	185	171
- (Decrease)/increase in provisions	66	-	-	-
- Decrease/(increase) in intangible	(2,747)	-	-	-
- (Decrease)/increase in interest received in advance	-	(612)	-	(612)
Net cash provided by operating activities	25,749	16,426	27,959	16,426

Notes to the Consolidated Financial Statements for the year ended 30 June 2006

19. Notes to the statement of cash flows (continued)

(b) Reconciliation of cash

For the purposes of the statement of cash flows, cash includes cash on hand and at bank, and short-term deposits. Cash as at the end of the financial year as shown in the statement of cash flows is reconciled to the related items in the statement of financial position as follows:

Cash and cash equivalents	48,974	37,029	48,974	37,029

(c) Reinvestment of distribution

During the financial year, the Trust issued 17,944,145 units (2005: 13,566,412) as a result of reinvestment of distributions by members totalling $17,944,145 (2005: $13,566,412).

20. Additional financial instruments disclosure

(a) Interest rate risk

Interest rate risk exposures

The Trust and consolidated entity's exposure to interest rate risk and the effective weighted average interest rate for classes of financial assets and financial liabilities is set out below.

	Note	Weighted average interest rate	Floating interest rate	Fixed interest rate maturing within 12 months	Fixed interest rate maturing 1 - 5 years	Total
2006 Consolidated		%	$'000	$'000	$'000	$'000
Financial Assets						
Cash and cash equivalents		5.38	48,974	-	-	48,974
Mortgage loans	8	11.35	-	266,753	61,018	327,770
Related managed investment schemes	9	11.35	-	39,605	22,913	62,518
Unrelated managed investment schemes	9	9.72	-	-	129,713	129,713
Promissory notes & unsecured notes	9	12.82	-	10,000	-	10,000
Fixed interest securities	9	6.90	-	26,247	-	26,247
Other investments	9	11.03	-	103,778	-	103,778
			48,974	446,382	213,644	709,000
2005 Consolidated						
Financial Assets						
Cash and cash equivalents		5.19	37,029	-	-	37,029
Mortgage loans	8	11.53	-	274,021	41,496	315,517
Related managed investment schemes	9	9.14	-	46,073	-	46,073
Promissory notes & unsecured notes	9	11.40	-	27,000	-	27,000
Other investments	9	9.44	-	78,796	-	78,796
			37,029	425,890	41,496	504,415

20. Additional financial instruments disclosure (continued)

(b) Credit risk exposure

Credit risk represents the loss that would be recognised if counterparties failed to perform as contracted. The total credit risk for recognised items is limited to the amount carried on the statement of financial position.

The Consolidated entity minimises credit risk by:

- undertaking credit assessment procedures on prospective borrowers
- obtaining independent valuations for all loans
- maintaining loan to valuation ratios generally not exceeding 66.67%
- the insurance policy referred to in Note 8.

As at 30 June 2006, the Trust's investments in mortgage loans related to 40 borrowers (2005: 58), with borrowings ranging from approximately $1.2m to $48.2m (2005: approximately $0.3m to $36.2m).

The percentage of loans secured by mortgages over properties were divided across the following geographical regions as follows:

Trust	**2006**	**2005**
	%	%
Queensland – metropolitan areas	4.30	4.02
Queensland – other areas	34.85	38.00
New South Wales – metropolitan areas	12.69	7.61
New South Wales – other areas	17.68	29.97
Victoria – metropolitan areas	21.46	15.55
Victoria – other areas	2.11	4.39
South Australia	-	0.46
New Zealand	6.91	-
	100.00	100.00

Notes to the Consolidated Financial Statements for the year ended 30 June 2006

20. Additional financial instruments disclosure (continued)

(c) Fair values of financial assets and liabilities

The Trust is exposed to market pricing risk on investments in listed property trusts. Risk is mitigated by maintaining a diversified portfolio. The Trust does not need ready access to substantial amounts of liquid funds, is under no pressure to sell investments, and is therefore not exposed to short term fluctuations in market prices of listed investments. Investments in other unlisted schemes are usually traded based on net asset backing.

	Carrying Amount	Fair Value	Carrying Amount	Fair Value
	2006	**2006**	**2005**	**2005**
Consolidated	**$'000**	**$'000**	**$'000**	**$'000**
Cash and cash equivalents	48,974	48,974	37,029	37,029
Investments	332,255	332,255	152,035	152,035
Trade and other receivables	2,587	2,587	8,334	8,334
Investment properties	-	-	77,084	77,084
Mortagage loans	327,771	327,771	314,112	314,112
Trade and other payables	(2,185)	(2,185)	(11,233)	(11,233)
Interest bearing liabilities	-	-	(40,545)	(40,545)
	709,402	709,402	536,816	536,816
Trust				
Cash and cash equivalents	48,974	48,974	33,320	33,320
Investments	332,255	332,255	192,035	192,035
Trade and other receivables	2,587	2,587	852	852
Mortagage loans	327,771	327,771	314,112	314,112
Trade and other payables	(2,185)	(2,185)	(2,002)	(2,002)
	709,402	709,402	538,317	538,317

Estimation of fair values

The following summarises the major methods and assumptions used in estimating the fair values of financial instruments reflected in the tables: -

Equity Investments

Fair value is based on quoted market prices at the balance sheet date without any deduction for transaction costs.

Investment properties

Refer to note 12 for details of how investment properties are valued.

Interest bearing loans and borrowings

Fair value is calculated based on discounted expected future principal and interest cash flows.

20. Additional financial instruments disclosure (continued)

Other receivables and payables

For other receivables and payables with a remaining life of less than one year, the national amount is deemed to reflect fair value. All other receivables/payables are discounted to determine the fair value.

(d) Liquidity risk

The liquidity risk associated with the need to satisfy unitholders' requests for redemptions is mitigated by maintaining cash funds to satisfy the usual levels of demand.

21. Events subsequent to balance date

There have not been any transactions or events of a material and unusual nature likely, in the opinion of the Responsible Entity, to affect significantly the operations of the Trust, the results of those operations, or the state of affairs of the Trust.

Notes to the Consolidated Financial Statements for the year ended 30 June 2006

22. Deconsolidation of controlled entities

On 30 June 2005 the Trust acquired 100% of the units in MFS Resort Asset Income Trust and MFS Resort Asset Equity Trust ("Resort Trusts"). The financial accounts of the Resort Trusts were consolidated by the Trust and appear in this report as part of the comparative figures (refer note 1(c)).

It was the intention at the time of acquisition to sell down the interest in the Resort Trusts and to retain a non-controlling holding. On the 13th April 2006, units in the Resort Trust were sold down and the Trust ceased to control the Resort Trusts. The Resort Trust ceased to be consolidated at that date. Disposal of interest in the Resort Trust resulted in a profit on disposal of $3,110,000 during the financial year. Set out below is the consolidated balance sheet of the Resort Trusts at date of deconsolidation.

	MFS Resort Asset Income Trust & MFS Resort Asset Equity Trust Consolidated Balance Sheet on Deconsolidation $'000
Assets	
Current assets	
Cash and cash equivalents	117
Inventory	296
Trade and other receivables	12,401
Total current assets	12,814
Non-current assets	
Property, plant and equipment	1,243
Investment property	94,353
Total non-current assets	95,596
Total Assets	108,410
Liabilities	
Current liabilities	
Trade and other payables	3,837
Provisions	667
Interest bearing loans and borrowings	7,933
Total current liabilities	12,437
Non-current liabilities	
Interest bearing loans and borrowings	41,224
	41,224
Total liabilities (excluding net assets attributable to unitholders)	53,661
Net assets attributable to unitholders - liability	54,749

23. Explanation of transition to AIFRS

As stated in note 1(a), these are the Consolidated entity's first annual financial statements prepared in accordance with AIFRS.

(a) Application of AASB 132 and AASB 139 – Classification of unitholder funds

The adoption of AASB 132 and 139 has resulted in the Consolidated Entity recognising financial liabilities at fair value and more particularly in the classification of unitholder funds as a liability whereas under previous GAAP they were considered as equity. The reconciliation of opening balances at 1 July 2004 and 1 July 2005 is set out below.

At 1 July 2004	**Previous GAAP**	**Impact of change in accounting policy**	**AIFRS**
	$'000	**$'000**	**$'000**
Unitholders funds – equity	378,490	(378,490)	-
Net assets attributable to unitholders - liability	-	378,490	378,490
	378,490	-	378,490

At 1 July 2005	**Previous GAAP**	**Impact of change in accounting policy**	**AIFRS**
	$'000	**$'000**	**$'000**
Unitholders funds – equity	535,136	(535,136)	-
Net assets attributable to unitholders - liability	-	535,136	535,136
	535,136	-	535,136

The transitional provisions will not have any effect in future reporting periods.

Notes to the Consolidated Financial Statements for the year ended 30 June 2006

23. Explanation of transition to AIFRS (continued)

(b) Application of AASB 132 and AASB 139 – classification of unitholders distribution

As a result of the reclassification of unitholders' funds as a liability, changes in net assets attributable to unitholders' funds, which, under previous GAAP, were referred to as transfers to unitholders and distributions to unitholders are now recognised as a financing cost, reducing net profit of the Trust in the income statement to nil. AASB 132 does however permit an income statement presentation which reconciles changes in net assets attributable to unitholders, rather than a nil profit. The comparative reconciliation of unitholders distribution at 30 June 2005 is set out below.

2005	**Previous GAAP**	**Impact of change in accounting policy**	**AIFRS**
	$	**$**	**$**
	$'000	**$'000**	**$'000**
Total revenue	49,858		49,858
Total expenses before finance costs	10,884		10,884
Net profit before finance costs	38,974		38,974
Distribution expense to unitholders	-	38,974	38,974
Contribution to net assets attributable to unitholders	-	-	-
Net profit	38,974		-
Net profit comprises:			
Transfer to unitholder funds	-		-
Distributions paid and payable	38,974	(38,974)	-
	38,974		-

(c) Application of AASB 140 – Investment property

Following the introduction of AASB 140 Investment Property, the Responsible Entity of MFS Resort Asset Income Trust and MFS Resort Asset Equity Trust ("Resort Trusts") reconsidered the nature of the investment in managers units and associated letting rights and determined that it is most appropriate to treat these assets as investment properties. This has resulted in amendments to the balance sheets of the Consolidated entity as at 30 June 2005 to include investment property of $77,084,009, to remove intangible assets of $60,494,996 and to reduce property, plant and equipment by $16,589,013. The comparative reconciliation of investment property at 1 July 2005 is set out below.

At 1 July 2005	**Previous GAAP**	**Impact of change in accounting policy**	**AIFRS**
	$'000	**$'000**	**$'000**
Intangible assets	60,495	(60,495)	-
Property, plant and equipment	17,995	(16,589)	1,406
Investment property	-	77,084	77,084
	78,490	-	78,490

Directors' declaration

MFS
INNOVATIVE INVESTMENT SOLUTIONS

In the opinion of the Directors of MFS Investment Management Limited, the Responsible Entity of MFS Premium Income Fund ("the Trust"):

(a) the financial statements and notes, set out on pages 7 to 38, are in accordance with the Corporations Act 2001, including:

(i) giving a true and fair view of the financial position of the Trust and the Consolidated Entity as at 30 June 2006 and of their performance, as represented by the results of their operations and their cash flows for the year ended on that date; and

(ii) complying with Accounting Standards in Australia and the Corporations Regulations 2001; and

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

Signed in accordance with a resolution of the Directors of the Responsible Entity, MFS Investment Management Limited.

	3/10/06
Director	Date

Independent audit report to the unitholders of MFS Premium Income Fund and its Controlled Entities

Scope

We have audited the financial report of MFS Premium Income Fund ("the Trust") and its Controlled Entities ("the Consolidated Entity") for the financial year ended 30 June 2006, consisting of the income statements, statements of changes in equity, balance sheets, statements of cash flows, accompanying notes 1 to 23, and the directors' declaration set out on pages 7 to 39. The directors of the responsible entity, MFS Investment Management Limited (the "Responsible Entity"), are responsible for the preparation of the financial report including the relevant reconciling information regarding the adjustments required under Australian Accounting Standards AASB 1 First-time Adoption of Australian Equivalents to International Financial Reporting Standards. We have conducted an independent audit of this financial report in order to express an opinion on it to the unitholders.

Our audit has been conducted in accordance with Australian Auditing Standards to provide reasonable assurance whether the financial report is free of material misstatement. Our procedures included examination, on a test basis, of evidence supporting the amounts and other disclosures in the financial report, and the evaluation of accounting policies and significant accounting estimates. These procedures have been undertaken to form an opinion whether, in all material respects, the financial report is presented fairly in accordance with Australian Accounting Standards and other mandatory professional reporting requirements in Australia and statutory requirements so as to present a view which is consistent with our understanding of the Trust's and the Consolidated Entity's financial position, and performance as represented by the results of their operations and their cash flows.

The audit option expressed in this report has been formed on the above basis.

Audit Opinion

In our opinion, the financial report of MFS Premium Income Fund and its Controlled Entities for the year ended 30 June 2006 is in accordance with:

(a) the Corporations Act 2001, including:

- (i) giving a true and fair view of the Trust's and the Consolidated Entity's financial position as at 30 June 2006 and of their performance for the financial year ended on that date; and
- (ii) complying with Australian Accounting Standards and the Corporations Regulations 2001; and

(b) other mandatory professional reporting requirements in Australia.

KPMG

D M Waters
Partner

Place: Melbourne Date: 11 October 2006


MFS065281

MFS
INNOVATIVE INVESTMENT SOLUTIONS

Client Services 131 MFS (131 637)
www.mfsgroup.com.au

New South Wales
Level 5, 56 Pitt St
Royal Exchange Building
Sydney NSW 2000
Australia
Mailing Address
PO Box R1693
Royal Exchange
NSW 1225

Queensland
MFS House
5 Hicks Street
Southport QLD 4215
Australia
Mailing Address
PO Box 10414
Southport
QLD 4215

Victoria
Level 11
200 Queen Street
Melbourne VIC 3001
Australia
Mailing Address
GPO Box 1402
Melbourne
VIC 3001

New Zealand
Level 10
175 Queen Street
Auckland
New Zealand
Mailing Address
PO Box 105716
Auckland Central
New Zealand