

Monday, 2 March 2015

Mr Maan Beydoun
Senior Specialist
Investment Managers and Superannuation
Australian Securities and Investments Commission

Email: feeandcostdisclosure@asic.gov.au

By email only

Dear Maan

FSC comments on the December 2014 draft of ASIC Regulatory Guide 97 *Disclosing fees and costs in PDSs and periodic statements*

1. We thank ASIC for providing FSC with the opportunity to comment on the December 2014 draft ASIC Regulatory Guide 97 *Disclosing fees and costs in PDSs and periodic statements (Draft RG 97)*. We refer to our 22 October 2014 submission on a draft of the fee and cost Class Order, which has now been finalised as ASIC Class Order 14/1252. Many of our comments which we made in our October 2014 submission on the draft Class Order apply to this submission and therefore this 2 March 2015 submission should be considered along with the FSC's 22 October 2014 submission (which for convenience is enclosed).
2. We welcome ASIC clarifying various areas of indirect costs disclosure, including the double counting aspects of the fee disclosure regime and the consumer advisory warning addressed in CO 14/1252 (the **Class Order**). We also thank ASIC for engaging with industry on areas in which industry has sought more guidance from ASIC, such as in relation to the application of the fee and cost disclosure regime to interposed vehicles. The fee regime is now so complex that any attempt to refine and clarify may be interpreted in various ways leading to numerous requests for further refinement and clarity. At a holistic level, we feel that the fee and cost disclosure regime is an area of the disclosure regime needing a review for simplicity, clarity and consistency – that is perhaps an objective beyond the Class Order and the Draft RG 97.

Executive Summary and Themes

3. The fee and cost disclosure regime in the regulations is complex. As issuers transition into the Class Order changes, further questions may arise in which case we may approach ASIC in future on fee and cost disclosure matters.
4. The different treatment for superannuation and managed investments will lead to inconsistent disclosure and further complexity in what is otherwise a very complex regime by virtue of legislation and regulations being refined over time. The status quo (including as

constituted by the Class Order) is not ideal for consumer clarity because of the different treatment between superannuation and managed investments. We acknowledge that legislation refined the superannuation fee regime. While it is not possible to provide the solution in this submission, we consider that the superannuation fee disclosure regime should be broadly consistent with the current managed investments fee regime.

5. The phrase “may reasonably estimate” is problematic. It introduces subjectivity and uncertainty to the calculation of indirect cost. It therefore consequentially would not likely aid consistency and comparability. We observe the Class Order applies this where a trustee does not know the underlying fees/costs and could not reasonably know (i.e. could not be said to ought reasonably know the underlying fees/costs). Hence further guidance in RG 97 is sought, specifically, as to when ASIC considers it not inappropriate for a trustee/responsible entity to not “estimate” because it is not “reasonable” to estimate, such as due to lack of reliability or specificity of information provided by third parties, the lack of willingness of a third party (such as offshore) to provide more detailed information, and so on.
6. ASIC should give guidance on how the Class Order definition of “indirect costs” – particularly sub-paragraph (1)(a)(ii) – addresses the need to apportion a trustee’s or responsible entity’s indirect share of costs in a co-ownership situation. On one interpretation, the literal wording of the definition leads to absurd results where the indirect interest held by the top level product (i.e. the product in which the retail client is invested), in the interposed vehicle, is only a partial interest.
7. It is also important that RG 97 be obviously consistent with other ASIC policy positions on platform disclosure. We suggest that the wording of RG 97 be clarified to make it obviously consistent with ASIC’s disclosure policy in CO 06/636 (superannuation platforms) and CO 13/763 (IDPS).
8. This submission broadly covers:
 - (a) our request for a reasonable transition period (reiterating our 22 October 2014 submission, including the costs data provided in that submission);
 - (b) notes the need for some materiality threshold in light of ASIC’s “reasonable estimate” test in relation to costs which are not (by definition) actually known to the trustee or responsible entity;
 - (c) responds to various of the specific ASIC questions set out in ASIC’s document *Review of Regulatory Guide 97 – Disclosing fees and costs in PDSs and periodic statements (12 December 2014)*; and
 - (d) finally contains additional general miscellaneous comments on the Draft RG 97 (and Class Order) in relation to:

- (i) Investments via a life policy (as it relates particularly to superannuation);
- (ii) Quantification of transactional costs for inclusion in ICR;
- (iii) Disclosure of “indirect fees” in periodic statements; and
- (iv) Costs versus fees;
- (v) Platforms and disclosure of fees and costs under section 1012IA;
- (vi) (related to (v) above), Consistency of the Class Order with ASIC policy on platform costs disclosure; and
- (vii) Minor drafting points on Class Order 14/1252.

Reiterating our previous comments on the need for a reasonable transition period – Existing PDSs v New PDSs

9. We refer to paragraphs 88 to 93 of our 22 October 2014 submission in relation to a reasonable transition period in respect of what is now Class Order 14/1252. In our view Class Order 14/1252 provides a transition which is not sufficient, including because Draft RG 97 is not final and ASIC’s guidance in the finalised RG 97 will set out how to apply the Class Order. Our October 2014 submission included some cost information – in the region of \$8 million in aggregate – for a sample of our members in relation to “out of cycle” PDS rolls. Our October 2014 submission requested a start date in relation to compliance with the Class Order of 1 July 2015 for superannuation PDSs *issued* on or after 1 July 2015 and 1 July 2016 for managed investment PDSs *issued* on or after 1 July 2016. ASIC’s Class Order requires all PDSs, including PDSs already on issue, to be updated in 10 months (namely 1 January 2016) even though ASIC has not yet finalised its draft RG 97 on applying the Class Order.
10. We request that ASIC apply the following transition period, assuming RG 97 is updated by 30 June 2015:
- (a) **New Super and New MIS PDSs:** For superannuation and managed investment PDSs first *issued* (that is dated) on or after 1 January 2016 (unless the ASIC Class Order relating to section 29QC applies to PDSs first issued later than 1 January 2016), such PDSs must comply with Class Order 14/1252 on issue. However, if any Class Order or guidance relating to section 29QC (see ASIC consultation in relation to section 29QC) provides for a later start date, then the fee and cost Class Order 14/1252 should apply to New Super and New MIS PDSs first issued after any later start date of any section 29QC related Class Order. *[It is absolutely essential as a matter of red tape reduction, per Government policy, that ASIC’s fee and cost disclosure Class Order 14/1252 and ASIC’s proposed section 29QC Class Order not generate two separate PDS rolls.]*

(b) **Existing Super and Existing MIS PDSs:** For existing stock of PDSs (that is first issued prior to 1 July 2016), the PDSs must be updated for the Class Order by 1 January 2017 (unless the ASIC Class Order relating to section 29QC applies to PDSs first issued later than 1 July 2016). However, if any Class Order or guidance relating to section 29QC (see ASIC consultation in relation to section 29QC) provides for a later start date, then the fee and cost Class Order 14/1252 should apply to Existing Super and Existing MIS PDSs first issued prior to any later start date of any section 29QC related Class Order. *[It is essential as a matter of red tape reduction, per Government policy, that ASIC's fee and cost disclosure Class Order 14/1252 and ASIC's proposed section 29QC Class Order not generate two separate PDS rolls.]*

11. We request that if RG 97 is not updated by 30 June 2015, then a reasonable transition period would be extended commensurately. Following the transition period, we ask ASIC to provide a facilitative compliance approach given the fundamental policy changes, particularly the changes made by the Class Order to the managed investment fees and disclosure regime – changes not made by the Stronger Super Reforms.
12. We also request that ASIC provide a ‘no action’ position for a reasonable period with respect to clarification provided by Draft RG 97 consistent with the commencement of the ASIC Class Order to enable industry to appropriately consider the guidance in RG 97 once finalised.

Materiality threshold in light of ASIC’s “reasonable estimate” test

13. To the extent that the Class Order is designed to provide comfort to trustees that a reasonable estimate may be used (even where costs are not known) and trustees are not required to expend disproportionate time and resources ascertaining unknown costs, this is welcome and appropriate.
14. While it is difficult to be prescriptive on materiality guidance, we consider that it is essential that ASIC state in its updated RG 97 that the key is on “reasonable” estimate and that trustees are not expected to expend significant resources and system changes to “chase down” non-material levels of cost, fees or expense down the investment chain. APRA Reporting Standards have a materiality level (for example, see Reporting Standard 532.0). Similarly we request ASIC to recognise expressly in RG 97 materiality in the application of ASIC’s fee and cost disclosure regime, which in any event we think is recognised implicitly (if not expressly) by the use of the phrase “reasonable”. This is important because in some cases, where a trustee enquires of an intermediary, the extent to which information will be provided (or detailed information provided) will depend on the circumstances. Clearly trustees will exercise their duties in requesting the information where reasonable.
15. Broadly, FSC considers the Draft RG 97 is unclear as to the following matters and therefore we request further guidance in RG 97 on the following:

- (a) *Examples of costs reducing returns to investors.* Although there is a reasonableness test attached to the requirement to estimate indirect costs, the concept of amounts that directly or indirectly reduce returns or reduce the amount or value of income or property at any level of the investment structure is potentially excessively demanding and potentially captures a vast expanse of costs and expenses for which it will be difficult to obtain an estimate or a reliable estimate;
- (b) *How far are issuers required to “drill down” and enquire via a chain of externally managed vehicles (having regard to the reasonableness test);*
- (c) *What is not required in relation to the reasonable estimate requirement (and this is particularly important):* FSC seeks guidance from ASIC in the updated RG 97 as to the level of inquiry beyond which trustees are **not** expected to go, given that there is a cost impact to trustees and therefore potentially fund member costs in seeking to estimate costs which are not actually known and which may be so insignificant as to not justify the cost of estimation (of a cost which is not actually known or is otherwise unable to be readily obtained). We suggest that the search, system, process and procedure costs of ascertaining fees or costs which are not material (where otherwise not actually known by the issuer/trustee) will in certain cases not be justified from a costs of estimation perspective. We seek principles-based ASIC guidance in RG 97 as to when the trustee could reasonably form the view, on the grounds of information actually available, that the additional fee or cost in underlying vehicles is likely to be non-material and the cost of estimating such additional fee or cost is likely to exceed the benefit of disclosure of the additional fee or cost. We accept that reasonable judgement calls will be required on these matters but we seek ASIC guidance as to when in ASIC’s view a trustee is not expected to ascertain or estimate unknown costs in the context of “reasonable estimates” of costs not actually known to the trustee.
16. To elaborate on the point in paragraph 15(c) above, below is a hypothetical example of an Australian managed fund that invests in global equities and has operational cash accounts in various currencies and countries that incur daily transaction fees and costs charged by third party financial institutions. This is an example of the difficulty of estimating fees and costs which are not actually known to the responsible entity, and it is possible/likely that such expenses (sought to be estimated) are not material levels of expense for the managed fund. In this example, the transaction fees and costs are:
- (a) often calculated with reference to the number of transactions and balances of such cash accounts in which balances change constantly as a result of purchases, sales and dividends in relation to the equities being bought and sold (i.e. the fees and costs are activity-based and therefore subject to market conditions and therefore difficult to estimate);
- (b) incurred daily, but may not be charged until a later date (e.g. at month end);

- (c) subject to foreign exchange rate movements with respect to the Australian dollar; and
- (d) there is likely to be a time lag before this information is made available to the Australian responsible entity.

This is just one example of how it is very difficult to estimate fees and costs not actually known to the responsible entity/trustee.

Specific ASIC questions in ASIC Review of Regulatory Guide 97 – Disclosing fees and costs in PDSs and periodic statements (12 December 2014)

Interposed Vehicle

ASIC Question: B1Q1 Do you consider the guidance provided on the interposed vehicles to be sufficient to properly explain when a body, trust, partnership or other structure would be an interposed vehicle?

17. The guidance provided on what is an interposed vehicle is complex and requires careful reading. This is probably a function of the complexity of the definition of interposed vehicle, which is itself likely a function of the difficulty of delineating between an investment and a vehicle to achieve investment. Nonetheless, feedback from FSC members is that the definition of interposed vehicle is complex (and also so is the guidance on interposed vehicle). We consider that provision of Examples may further assist in an understanding of the definition (please see below).
18. We believe it would be beneficial if the specific reasoning of the conclusions of each of the Examples in RG 97 is articulated in RG 97 so the same reasoning can be applied by industry to similar situations with confidence.
19. We seek further examples (or flexibility, see below in relation to look-through and life policies) in RG 97, including examples relating to *superannuation entities investing via a life policy*, and examples relating to the different outcomes which can arise depending on whether an entity is *listed* or *unlisted* (e.g. the costs of a listed property trust need not be included in indirect costs but the costs of an unlisted property trust do need to be included if the unlisted property trust is not named in the PDS).
20. In relation to *superannuation entities and life policies*, we request that the final version of RG 97 be amended to allow flexibility for a superannuation trustee (investing via a life policy) to disclose fees that are charged in a life company in the relevant fee category (i.e. administration, investment fees etc.) rather than the amounts all being disclosed by the superannuation trustee as indirect costs. Further information on *superannuation entities and life policies* is included in paragraphs 82 to 84 of this submission.

21. We also seek ASIC's confirmation, by way of examples in RG 97 if necessary, that:
- (a) (***superannuation investing in a life policy***): Where a superannuation entity invests via a life policy then the life policy is an interposed vehicle in all cases and not just for *Example 4: Cash investment option*; and
 - (b) (***superannuation wrap platform***): Financial products offered via a superannuation wrap platform are not caught by the definition of an interposed vehicle for the same reasons as given in *Example 7: Investor directed portfolio services*.
22. The more examples provided in RG 97 the more likely that consistency will be achieved. We applaud that ASIC has provided some Examples in Draft RG 97 but we consider that given the complexity and breadth of the fee and cost disclosure regime, more examples are required in RG 97 to assist consistency, comparability and certainty.
23. Paragraph 97.26 of Draft RG 97 could be more clearly worded to accurately reflect the Class Order. The paragraph should mention the listing criterion in paragraph (a)(ii)(A) of the definition of "interposed vehicle" in the Class Order.
24. The wording of paragraph 97.28 could be re-arranged to make the meaning clearer i.e.:
- On the other hand, if the PDS describes the asset allocation for the investment option (e.g. a balanced option or a product) to include an investment in a ~~vehicle trust, body or partnership~~ of a particular type, (e.g. a hedge fund or private equity fund), that is predominantly in the business of investing in securities or financial products, ~~(e.g. hedge funds or private equity funds)~~, then this vehicle ~~these funds~~ would be an interposed vehicles and ~~their~~ its costs would need to be considered when calculating the investment option or product's indirect costs.*
25. We suggest for clarity and digestibility of RG 97 that each example in RG 97.33 be cross-referenced to the appropriate limb of the Class Order definition of "interposed vehicle".
26. Comments on particular examples in Draft RG 97.33 are:
- (a) **Example 2** concludes that the reason why the hedge funds are interposed vehicles is "because they provide exposure to other assets". However, referring to the Class Order, the more direct reason would seem to be that the "other hedge funds" (in Example 2) "predominantly carry on a business of investment in securities" per paragraph (a)(i) of the definition of "interposed vehicle" in the Class Order. (Example 2 states nothing about what the top level managed investment scheme PDS says so we cannot assume anything about how paragraph (a)(ii)(B) of the definition of "interposed vehicle" in the Class Order applies.)

- (b) In **Example 3** it could be clarified that this example would not apply in the case of a s1012IA custodial arrangement (see later in this submission for our comments on platforms).
- (c) **Example 5** is incorrect; it should say "... and does not predominantly invests in securities or financial products". [FSC acknowledges ASIC is already aware of this error and will correct the Example.]
- (d) **Example 6** refers to a superannuation trustee disclosing "*in the PDS of an investment option*"; which PDS is this referring to? There will be a PDS for a superannuation product, and that PDS may make disclosure about investment options available through the product. For a superannuation platform to which s1012IA applies there will be a PDS for the underlying accessible financial product, either prepared by the superannuation trustee or by the underlying issuer of the accessible financial product depending on what option under CO 06/636 is pursued (FSC understands the more common position in industry is that the PDS for the underlying accessible financial product would be prepared by the underlying issuer of the accessible financial product). We request that ASIC consider refining Example 6 to ensure absolute clarity as to which PDS is being referred to (given the use of superannuation platforms and the various PDSs which may exist referable to an offer of an accessible financial product on a superannuation platform).
27. We also seek some examples in relation to the application of the interposed vehicle definition to life company statutory funds including sub-funds. These funds can ordinarily be expected to be conduits for downstream investments.

ASIC Question: B1Q2 Are there additional examples that you consider should be included in RG 97 which would assist in clarifying or explaining the interposed vehicle definition and its application?

28. Please see our response to ASIC Question B1Q1. We also seek more examples in RG 97 on applying the framework to a chain of interposed entities. Diagrams may assist in clarity.
29. The examples provided by ASIC are all one layer examples and contemplate only whether a vehicle invested in directly by the relevant trustee or responsible entity is an interposed vehicle or not. The indirect cost disclosure requirement contemplates infinite look-through, if each subsequent vehicle is an 'interposed entity' for the purposes of the Class Order.
30. An example of this may be where a superannuation trustee invests in a managed fund, which in turn invests in other managed funds and alternative investment funds. Based on ASIC's guidance the superannuation trustee would be required to report on indirect costs in respect of both the managed fund, the underlying managed funds and any alternative investments fund and any other vehicles in which those underlying funds invest. We consider that an illustrative example provided by ASIC in RG 97 would be useful.

31. We also believe that there is uncertainty arising from the wording of paragraph (1)(a) of the “101A Indirect costs” definition in the Class Order and that ASIC should either amend it or give guidance about its interpretation to avoid potentially absurd results in certain cases. To explain further:
32. Paragraph (1)(a) provides for several factual permutations. One of these permutations is that indirect costs includes:

“any amount that: (a). reduces the amount or value of ... (ii) the income of or property attributable to an interposed vehicle ...”

33. One application of these words leads to absurd results. To illustrate with a simple example which assumes the following:
- (a) A retail managed investment scheme (**the MIS**) is a 25% shareholder in an unlisted investment company (**the interposed vehicle**) that predominantly carries on business of investing in securities;
 - (b) There are three other shareholders holding the remaining 75% of the interposed vehicle;
 - (c) All shares in the interposed vehicle carry equal rights to participate in the profits of the vehicle and its net assets on a wind-up;
 - (d) The gross income of the interposed vehicle is \$200; and
 - (e) The interposed vehicle incurs costs of \$100 which are deducted from the gross income (of \$200), leaving net income of the interposed vehicle for distribution of \$100; i.e. a 50% costs-income ratio.

Based on the assumptions in (a) to (e) above and applying the Class Order, then:

- (f) If all the gross income of the vehicle were to be distributed then, as a 25% shareholder, the MIS would be entitled to 25% of the gross income i.e. \$50; not of course the entire \$200.
- (g) As the interposed vehicle (based on the assumption in paragraph (e) above) incurs costs of \$100 which are deducted from the gross income, this leaves net income of the interposed vehicle for distribution of \$100; i.e. a 50% costs-income ratio.
- (h) The MIS’s share of net income would be \$25. That is, the MIS’s share of the income of the interposed vehicle has been reduced by 50% or by \$25 because of the interposed vehicle’s costs.

- (i) On a literal reading of the wording of paragraph (1)(a) of the “101A Indirect costs” definition, arguably it is the total \$100 cost figure which is the “amount that reduces the income attributable to the interposed vehicle”, and therefore, arguably, \$100 is the amount that the MIS responsible entity must include in its indirect costs calculation.
- (j) Applying one of many possible literal interpretations of the Class Order, this leads to the absurd result that the MIS indirect costs would include an amount of \$100 even though the MIS’s indirect share of those costs was only \$25.
34. A possible interpretation of the literal wording of the Class Order gives rise to this result because sub-paragraph (1)(a)(ii) of the definition of “Indirect costs” does not expressly provide for any proportionate attribution of the costs of the interposed vehicle to reflect the proportion of those costs that affect the return to the next entity up the investment chain.
35. ASIC should either amend the definition of “Indirect costs” in the Class Order or provide guidance in RG 97 to ensure that costs of the interposed vehicle are attributed proportionately up the investment chain. This should focus on the reduction in the return to the investor. That is, the wording of (1)(a)(ii) of the definition of “Indirect costs” in the Class Order should not focus on the total amount of the reduction in the income or property of the interposed vehicle; instead it should focus on the amount by which the reduction in the income or property of the interposed vehicle has reduced the return on the investment in that interposed vehicle made with “the property attributable to the product or option” (i.e. the headline retail product or retail product investment option). I.e. an amount being that proportion of the reduction in the return, income or property of the interposed vehicle that reasonably represents the investor’s share (in our example, the MIS’s share) of the costs.
36. The example above illustrates a closely-related problem – how to account for the investment interests of co-investors. In the above example the other shareholders are entitled to a distribution of the remaining \$75 of net income. Arguably, on one possible interpretation of the Class Order, this \$75 income distribution to other shareholders is “an amount that reduces the amount or value of the property attributable to the interposed vehicle” and therefore the MIS responsible entity should include this \$75 in the indirect costs calculation for the MIS PDS. We do not consider that result is intended by the Class Order but our members have noted the variety of interpretations open on a literal reading of the Class Order. We consider that a simple amendment of the Class Order or a clarification in RG 97 should remove all doubt so as to permit a proportionate allocation of costs.
37. Nevertheless, this (counter-intuitive) interpretation might possibly be seen as supported by paragraph RG 97.44 of Draft RG 97. Although that paragraph is about the particular situation of an investment manager etc. recouping costs through sharing dividend income, it contains the statement that product issuers must continue to account for the entire income in the fund’s investment return, in that paragraph 97.44 states “*The shared portion of the income is*

to be considered and disclosed as a management cost ...". Although not entirely clear (and we suspect not intended), the words in paragraph RG 97.44 might be seen as a statement of general application to the co-investment situation referred to in paragraph 33 (of this submission) above.

38. We request ASIC clarify the potential confusion in the potential literal interpretation of the Class Order in relation to applying the Class Order to co-ownership or partial ownership situations. As mentioned above, it should be made clear in RG 97 that only that proportion of amounts that reduce the relevant direct or indirect share of the income or property of the interposed vehicle attributable to the up-stream entity should be taken into account (this seems to us to be the common sense approach which we seek ASIC confirm in its final RG 97).
39. A more sensible interpretation would be that the proportionate amount of the costs should be used (namely \$25 indirect costs being commensurate with the MIS's 25% holding in the interposed vehicle). We consider that it is possible also to interpret clause 101A Indirect costs in a manner consistent with the more sensible interpretation (that is, applying costs in the interposed vehicle, on a proportionate basis commensurate with the holding (direct or indirect) of the MIS (using our example) in the interposed vehicle). Given the uncertainty as to the interpretation (on some literal readings of the Class Order), we urge ASIC to avoid these concerns by confirming in RG 97 that the costs to be used is the indirect costs referable to, proportionate with or commensurate with (using our example) the MIS's interest in the interposed vehicle.
40. This issue could be simply addressed by amending limb (a)(ii) of the Class Order definition of indirect costs or, alternatively, by providing guidance in Regulatory Guide 97 to the effect that limb (a)(ii) of the definition is only intended to capture reductions in the income or property attributable to an interposed vehicle that relate to the trustee's specific holding, and are not intended to capture distributions to other investors in the interposed vehicle.

ASIC Question: B1Q3 The application of interposed vehicles and indirect cost varies between superannuation and managed investment products. Do you consider the proposed RG sufficiently explains these differences?

41. The different definition of indirect costs between superannuation and managed investments will not aid comparability and adds to complexity of the fee and costs disclosure regime. Given the importance of the distinction, ASIC should provide a rationale for it in RG 97. Because of the different treatment of superannuation and managed investments, superannuation trustees can no longer rely solely on the ICR information provided by a managed investment product provider which is often sourced via a data aggregator. We seek guidance on the additional reasonable steps that ASIC believes should be taken by a superannuation trustee to obtain information on transactional and operational costs not included in the managed investment product ICR. We also refer to our comments below in relation to *buy-sell spreads/margins* and our comments in paragraphs 66 to 70 in relation to *performance fees*. The inconsistency between the managed investment and superannuation

- fee and cost disclosure regimes are particularly impracticable and difficult for superannuation platform style products – the regimes appears to disregard these large scale superannuation vehicles.
42. Also, the quantification of net transactional costs of a managed investment product, being the buy/sell margins less actual brokerage incurred, is a complex and costly exercise that is not currently performed.
43. We seek guidance on how superannuation trustees should reasonably estimate such costs if the responsible entity of the managed product provider does not provide these costs.
44. We consider that Draft RG 97 does not sufficiently explore the differences between the indirect cost rules for managed funds and the indirect cost rules for superannuation funds. For example, a managed fund would not need to include its own transaction costs as part of its indirect costs, but a superannuation fund that invested in that managed fund would need to disclose those transaction costs as part of the superannuation fund's indirect costs.
45. Further, a managed fund would not need to include in the calculation of its indirect costs the transaction costs of any interposed vehicle in which it invests. However, the superannuation fund investing in a managed fund would need to include the transaction costs of those interposed vehicles in the calculation of the superannuation fund's indirect costs.
46. We request that the different application of the fee and cost regime between superannuation and managed investments be explored and explained further in RG 97, including by way of examples if necessary, including (but not limited to) the situation of superannuation platforms. This request is not a criticism of the steps ASIC has taken in the Draft RG 97 but rather a reflection of the complexity and difficulty of the application of the regime (and the fact that the regime differs for superannuation and managed funds).
47. It would be preferable for certainty, simplicity, clarity and consistency that the managed investments regime for indirect costs should be adopted for superannuation. *We foreshadow that so long as the fee and cost disclosure regimes are different across superannuation and managed investments, there will be complexity and difficulty in implementation and application of the regimes across collective investment vehicles (i.e. superannuation and managed investments) and this does not aid consumer understanding.*

Requirement to reasonably estimate costs that are known

ASIC Question: B1Q4 Do you consider the guidance provided on the requirement to reasonably estimate indirect costs would assist you in complying with this requirement?

48. The Class Order has extended the law beyond the provisions of the Corporations Act by requiring a reasonable estimate of costs which are not actually known to issuers. The Corporations Act requires disclosure to the extent *actually known* to the issuer (and certain

other persons). We consider it is not entirely free from doubt as to whether ASIC's Class Order powers extend so far as to permit ASIC to modify the law to require disclosure of an estimate of a cost which is not "actually known" to the issuer (given the Corporations Act states that PDS disclosure is required to the extent *actually known* to (relevantly) the issuer and other persons referred to in section 1013C(2)). We assume ASIC has formed the view that the Class Order may be made. (FSC does not provide a definitive conclusion on the matter.)

49. To the extent that the Class Order is designed to provide comfort to trustees that a reasonable estimate may be used (even where costs are not known) and that trustees are not required to expend disproportionate time and resources ascertaining unknown costs, this is welcome and appropriate.
50. While it is difficult to be prescriptive on materiality guidance, we consider that it is essential that ASIC state in its updated RG 97 that the key is "reasonable" estimate and that trustees are not expected to expend significant resources and system changes to "chase down" non-material levels of expense. This is important because in some cases, where a trustee enquires of an intermediary, the extent to which information will be provided (or detailed information provided) will depend on the circumstances. Clearly trustees will exercise their duties in requesting the information where reasonable
51. The feedback from FSC members is that the Draft RG 97 is unclear as to what is a "reasonable estimate". We seek ASIC guidance in RG 97 as to when the trustee is not required to provide an estimate of a cost it does not actually know, on the basis that it is not "reasonable" to expect the trustee to do so, for example due to the systems and other cost implications of "chasing down" non-material costs and expenses through a chain of external interposed vehicles.

ASIC Question: B1Q5 Do you agree that it would be a matter of good practice for trustees and responsible entities to document their procedures for making reasonable estimates as a means of enhancing consistency?

52. We do not consider ASIC needs to provide guidance in RG 97 as to documentary procedures. AFSL duties apply and issuers should be able to substantiate estimates if required. Accordingly, the FSC recommends that comments on these matters be removed from RG 97.

Over the counter derivatives costs

ASIC Question: B1Q6 Do you consider the guidance and examples sufficient to understand the appropriate treatment of buy/sell spreads of OTC derivatives for superannuation and managed investment products?

53. We acknowledge the Class Order has been finalised. We however refer ASIC to our enclosed 22 October 2014 submission in relation to derivatives (see paragraphs 10 to 18 of that submission). We do not agree that a buy-sell spread of an OTC derivative would generally be an indirect cost (in the sense a cost the investor would not bear if investing in the OTC

- derivative directly). Further, there are significant practical difficulties in estimating the embedded cost of an OTC derivative. Further, we do not agree with ASIC limiting its carve out to hedges – managing asset exposure of a fund is an equally legitimate use of derivatives which does not raise the concern we assume ASIC is concerned about (namely, the use of OTC derivatives to “hide” otherwise disclosable fees and costs, to the extent ASIC is aware of such a practice). The ASIC approach to derivatives costs in the Class Order adds complexity and does not appropriately target the mischief (to the extent ASIC is aware it exists) of the use of derivatives to “hide” fees and costs. Further, ASIC’s approach may not support consistency (as exchange traded derivatives are treated differently from OTC derivatives which are not hedges).
54. We request that ASIC consider that (consistent with our 22 October 2014 submission) the buy-sell spread of derivatives can be treated as transaction costs of the fund, where derivatives are used for managing market exposure. Examples where this could apply include:
- (a) seeking to stay invested while having sufficient cash to meet fund liabilities;
 - (b) reducing transaction costs;
 - (c) situations where derivatives are favourably priced relative to equity or fixed income securities;
 - (d) where derivatives are a more efficient way of gaining exposure than holding the physical securities.
55. The above are common and efficient uses of OTC derivatives in the wealth management sector. The approach to hedges (in ASIC’s Class Order) should be extended to these well-known and perfectly legitimate uses of derivatives (i.e. which do not involve the nefarious purpose of “hiding” fees and costs which would otherwise be disclosable). Without this extension to such common use of derivatives in the wealth management sector, ASIC’s changes could have the unintended consequence of making possibly lower cost funds look more expensive to the investor, not supporting consistency and not aiding comparability (funds using OTC versus exchange traded) derivatives.
56. It is not clear from the Draft RG 97 how an issuer may ascertain the buy-sell spread. Not all OTC derivatives have a simple premium. Often the OTC derivative is an exchange of payments. To ascertain the spread requires the counterparty to inform the issuer the implicit amount it incorporates into the pricing of the derivative (which may be confidential information, and which the – for example – bank counterparty is not compelled to disclose).
57. We support consistency in disclosure. It is possible that the treatment of OTC derivatives may result in inconsistent disclosure in that – *non-hedge*-OTC derivatives are captured by ASIC’s Class Order, whereas hedge OTC derivatives (and exchange traded derivatives) are not captured. It is possible therefore that funds using OTC derivatives for investment

management purposes to achieve an investment objective (but not hedges) may appear more expensive than a fund using an exchange traded derivative or a hedge-OTC derivative. This does not aid consistency or comparisons (apart from competitive neutrality concerns). To the extent ASIC is seeking to ensure that the use of derivatives to avoid disclosure of indirect costs is prevented, we refer ASIC to our 22 October 2014 submission (in particular paragraph 18). ASIC's methodology in the Class Order is in our view not conducive to consistent disclosure, nor in our view is requiring a calculation of legitimate uses of OTC derivatives to efficiently manage a fund, appropriate given the difficulty with obtaining such costs. In any event, costs of OTC derivatives are generally a cost an investor buying the OTC derivative directly would bear (hence should not be treated as an indirect cost).

58. Where derivatives are used for the purpose of "hiding" indirect costs, then we agree that such costs should be disclosed. We are not aware of any systemic use of OTC derivatives for such purpose (and if it existed may raise a question as to trustee duties). We refer ASIC to FSC's detailed submissions in our 22 October 2014 submission in relation to ASIC's approach to OTC derivatives.
59. Capturing costs (i.e. "buy-sell" spread) of non-hedge OTC derivatives will require onerous system and process changes to gather this information in a meaningful way. In our view this is inconsistent with the statement in the Explanatory Statement to ASIC's Class Order that "The Office of Best Practice Regulation has agreed with ASIC's assessment that the class order will have a minor and machinery impact and therefore no Regulation Impact Statement is required."
60. While we refer ASIC to our October 2014 submission for our detailed comments, in part we stated and wish to reiterate:

"10. It is not clear why the buy-sell spread for over-the-counter (OTC) derivatives should be treated as indirect costs rather than transactional and operational costs, in direct contradiction to the definition of "transactional and operational costs" in item 103 of Schedule 10 of the Corporations Regulations 2001 (Cth). Nor is it clear what constitutes 'hedging' or why the treatment of the *transaction cost* (i.e. the in-built buy-sell spread) of a derivative changes depending on whether the derivative is used for investment or hedging purposes – the implication being that buy-sell spreads on *hedge derivatives* are *transaction costs* (which we agree with), but buy-sell spreads for *all other types of OTC derivatives are not to be treated as transaction costs* but instead to be deemed to be an indirect cost (which we disagree with).

11. A buy-sell spread for an OTC derivative reflects the cost of entering into the transaction and is built into the price of the derivative (regardless of whether or not the derivative is used for investment or hedging purposes); it is not a fee charged in addition to the cost of the transaction. In any event it would be extremely difficult, if not impossible, for a trustee or responsible entity to

extract and ascertain the buy-sell spread of an OTC derivative in order to disclose it.

12. Derivatives are used for investment exposure purposes, for hedging and for other investment purposes. For example, equitising cash is a common use of derivatives for share funds. We do not agree that a buy-sell spread of a derivative is an indirect cost. ASIC's proposal to include the spreads on derivatives as an indirect cost is not appropriate.

...

17. If ASIC is genuinely concerned that issuers are entering derivatives for the purpose of avoiding fee disclosure (rather than for an investment management related purpose), instead of ASIC's test in clause 101A in relation to the buy-sell spread of derivatives, ASIC should adopt an anti-avoidance test. An anti-avoidance test is a more targeted test directed at the mischief ASIC is concerned about (hiding fees via derivatives). ASIC's Class Order test is a blunt instrument which treats all *transaction costs* (i.e. buy-sell spreads) of OTC derivatives which cannot be described as hedges *as instead to be treated as an indirect cost* – this approach directly contradicts the current definition of transactional and operational costs in Schedule 10. “

ASIC Question: B1Q7 Is the guidance provided sufficient to apply the definition of buy/sell spread of OTC derivatives when used for hedging purposes by a responsible entity of a managed investment product?

61. We are concerned that the ASIC approach to OTC derivatives is a solution which is not appropriately targeted to (if it exists, and we assume ASIC may have concerns) issuers using derivatives to hide otherwise disclosable fees and costs. We agree with closing down such practice (if it exists, and we defer to ASIC's supervisory experience on any use of derivatives for the illegitimate purpose of hiding costs rather than for an investment objective purpose). We do not agree with ASIC's interpretation though that the cost of OTC derivatives, broadly speaking, is not a transaction cost or a cost of the asset (namely the asset being the derivatives). However, we concede ASIC has proceeded with that treatment in the Class Order following consultation.
62. ASIC Example 9 begs the question, what is the “buy-sell spread”. Obtaining that information requires the will and assistance of the sell-side counterparty. This gives rise to significant reliability implications, and systems issues in implementing a system to seek to obtain reliable information from a counterparty who may not need to or wish to verify the spread (the spread which may include a profit or shareholder return or cost of capital charge component of the sell-side counterparty).

63. We acknowledge the Class Order is finalised. We simply observe that there is likely to be practical difficulties in many cases in seeking to comply with ASIC's requirement to ascertain the buy-sell spread of an OTC derivative. We wish to inform ASIC in advance of the implementation of the Class Order. Further guidance or refinement may be needed in future.

Inclusion of additional voluntary information

ASIC Question: B1Q8 Do you consider this guidance to be appropriate?

64. We consider that the Draft RG 97 should set out ASIC's views on the law (or modified law in terms of the Class Order) as opposed to additional information ASIC may consider it a matter of good practice to disclose.
65. To the extent paragraph 97.66 of Draft RG 97 may be seen to impose ASIC expectations (beyond the law), we do not support the paragraph. However, to the extent draft paragraph 97.66 is rather intended to be facilitative and provide flexibility in a prescriptive regime (for example, like draft paragraph 97.62 which contemplates some tailoring of the fees and costs template and the example of annual fees and costs may be appropriate in limited circumstances), then we support that objective. FSC members are unsure whether the intention of ASIC in including draft paragraph 97.66 in its current form is the former or the later - we seek ASIC's clarification. If it is the former objective, we do not support draft paragraph 97.66 as it imposes prescription beyond the law and the matter should be left to issuers to expand beyond the law as they see fit. If the later objective (ASIC acknowledging some flexibility is permitted), we support paragraph RG 97.66 with amendments to make it clear that ASIC is simply acknowledging some flexibility might be appropriate (and is permitted) in particular circumstances (along the lines of draft paragraph RG 97.62). It is up to issuers as to whether they disclose more detail. Some information may be commercially sensitive.

Performance Fees

ASIC Question: B1Q9 Do you consider this guidance to be appropriate?

66. At Draft RG 97.55, ASIC refers to "incorrect practices of non-disclosure". It is not clear to us what this phrase means. Does it mean non-disclosure, or disclosure of amounts ASIC considered to be incorrect disclosure?
67. Estimating a performance fee is difficult. To aid industry consistency we ask ASIC to include in its updated RG 97 that one reasonable way to estimate performance fees is based on the average yearly performance for the last three years (where available). If ASIC provided this as non-prescriptive guidance in RG 97, it is likely industry may converge to a common practice of using that basis as one basis of estimating performance fees. However it is imperative that ASIC *not* mandate that that would be the only basis to reasonably estimate performance fees particularly in light of new funds where no performance history exists or where past performance has no relevance to possible future outcomes.

68. One view held among issuers is, absent particular circumstances, last year's performance fee is not an unreasonable starting point for estimating next year's performance fee. Issuers also express significant concerns with going beyond this proxy to re-assess an estimate of performance fees based on future performance which involves risks given the Corporations Act and ASIC Act provisions on statements relating to future matters (and the guidance in ASIC RG 170). Another possible scenario consistent with this, and which would aid in investor comparability, is to give issuers the option (but not mandated) to estimate performance fees by disclosing the performance fee amount that would be payable on outperformance of a particular percentage (without of course providing any guarantee that the outperformance would occur). Again, it is imperative that ASIC not mandate a particular form or method of estimating performance fees but rather provide ASIC's views on some permissible (but non-exhaustive) methodologies, which may well assist in comparability to the extent industry chooses to adopt the ASIC alternative permissible (but not exhaustive) means of estimating performance fees.
69. Our members seek guidance in RG 97 on the application of the Class Order to performance fees charged down the investment chain (particularly in vehicles not owned or controlled by the superannuation trustee or responsible entity).

ASIC Question: B1Q10 Are there scenarios that you consider it would be appropriate to give further guidance on?

70. Our members seek guidance in RG 97 on the application of the Class Order to performance fees charged down the investment chain (particularly in vehicles not owned or controlled by the superannuation trustee or responsible entity).

Insurance Disclosure

ASIC Question: B1Q11 Do you consider this guidance to be appropriate?

71. Insurance premiums are dependent on a number of risk factors such as age, smoker status, occupation etc. Whilst examples may be given in a PDS it is not practical to detail all possible combinations that may apply to a prospective member. In addition, the cost of insurance cover available through corporate superannuation products for all types of cover may differ between employer groups depending on the arrangements in place and it is not possible to detail all of these arrangements in the PDS.
72. We believe it would be helpful if RG 97 takes into account these practical concerns when issuing any guidance relating to insurance disclosure and where appropriate gives specific guidance with examples. In particular we believe that a PDS that provides contact information for a quote to be obtained based on your individual circumstances should be sufficient disclosure.

73. The industry is currently adopting a number of different approaches to the disclosure of insurance costs in the fees and costs table. Some will disclose nothing in the table but rely on a footnote, others will disclose a statement in the 'Other fees and costs' row as well as the footnote while others will include a statement in this row about insurance costs together with a statement about how and when they are paid.
74. The FSC would welcome ASIC's guidance on disclosure of insurance costs in the fees and costs table itself, and we request that any ASIC guidance have regard to our comments in the above three paragraphs. It would be appropriate for ASIC to consult on any draft guidance in relation to insurance cost disclosure prior to finalising any guidance, and FSC would welcome the opportunity, along with our members, to comment on any drafts.

ASIC Question: B1Q12 Do you recommend any other guidance that should be included to further assist industry in this area?

75. FSC has no further comment.

Disclosing fees and costs for a stapled security

ASIC Question: B1Q13 Do you consider this guidance to be appropriate?

76. FSC has no comment.

ASIC Question: B1Q14 Do you consider that it would be more appropriate for PDS prepared for stapled securities to be prepared on the basis of combining the fees and costs for the managed investment scheme and body corporate security components, in a similar manner as required for periodic statements for listed and quoted stapled securities under Class Order 13/1200? If so, do you consider it appropriate for ASIC to give effect to this requirement by way of a class order?

77. FSC has no comment.

ASIC Question: B1Q15 If PDS need to be prepared on the basis of combining the fees and costs for the management investment scheme interest and body corporate security components, do you consider it would still be useful and necessary to disclose the fees and costs on a separate basis as well?

78. FSC has no comment.

Disclosing start-up and initial one-off fees or costs

ASIC Question: B1Q16 Do you consider this guidance to be appropriate?

79. In general terms we support ASIC's guidance in Draft RG 97 at paragraphs 97.140 to 97.142 in relation to *initial one-off fees or costs*.

80. In relation to *start-up costs* we seek further guidance on the period to which start-up costs should be included in any fee disclosure.

ASIC Question: B1Q17 What examples do you consider useful for responsible entities to include in the PDS for investors to understand start-up and other initial one-off fees?

81. FSC has no further comment.

General miscellaneous comments in relation to Draft RG 97 and the Class Order and fee and cost disclosure regime

Investments via a life policy

82. Draft RG97 contains wording and examples which indicate that where a superannuation product invests via a life company, the fees charged at the life company level are all considered to be 'indirect costs'. We understand there are circumstances where the vast majority of superannuation assets are invested via a life company and the majority of fees are charged by the life company rather than the superannuation trustee.
83. In this situation, one of the industry practices is to 'look through' this arrangement for the purposes of fee disclosures and show at the superannuation fund level the respective fees at the life company/life policy level against the appropriate categorisation (e.g. administration fee / investment fee etc.). The wording at Draft RG 97, paragraph RG97.23, and *Example 4: Cash investment option* on page 12 of Draft RG 97 seem to indicate that under the revised RG 97 these life company/life policy fees should all be shown as 'indirect costs' at the superannuation fund level rather than on a 'look through' basis.
84. Showing the fees as 'indirect costs' at the superannuation fund level may be less informative to investors than the current look through approach that we understand some issuers adopt. We therefore request that the final version of RG 97 provide the flexibility for superannuation investments through a life company to adopt a 'look through' approach and show the respective fees of the life company/life policy against the appropriate fee type at the superannuation fund level. From the superannuation member's perspective, the fact that the monies are invested via a life company is not a key consideration or differentiator, and should not 'cloud' the disclosure of the fees at the superannuation fund level. It would be more informative for superannuation members (which achieve exposure via a life policy) to see the fees reported against the different fee types on a look-through basis, than for all fees to be reported as indirect costs of the superannuation fund.

Quantification of transactional costs for inclusion in ICR – superannuation funds

85. The introduction of the concept of *indirect costs* for superannuation products now means that transactional and operational costs of any interposed entities must be included in the Product Disclosure Statement (PDS) fee table under the Indirect Cost Ratio (ICR) to the extent that

- they reduce the return on investment of a member. It is common practice in the industry to charge buy and sell margins on investment option transactions (sometimes referred to as ‘transaction cost factors’) by their inclusion in higher buy and lower sell unit prices as a means of ensuring members who transact infrequently do not unfairly bear the costs generated by members who transact more frequently. Offsetting these buy and sell margins retained by the portfolio are the actual transaction costs incurred in any interposed entities.
86. Actual costs incurred will relate to both member initiated transactions as well as portfolio trades initiated by the investment manager seeking to rebalance portfolios and maximise returns. The quantification of the **net transaction costs** for inclusion in any ICR disclosure therefore becomes a very complex exercise and requires the quantification of all transaction costs actually incurred by the portfolio less any buy and sell margins retained by the portfolio based on actual inflows and outflows and the respective buy and sell margins that existed at the time of the transaction.
87. The calculation can be further complicated by fund of fund structures where each fund in the investment hierarchy may charge a buy and sell margin in order to recover the buy and sell margins levied by the underlying funds; however, as transactions in the underlying funds are normally netted, this can result in any excess of actual transaction costs being to the benefit of fund unit holders as a whole. In addition, as managed investment products are not required to include transactional and operational costs in their ICRs (except those related to OTC derivatives for non-hedging purposes), a superannuation trustee will not be able to rely on ICR’s provided by managed investment product issuers and must seek additional information from managed investment product providers who are not obligated to provide such information. This is particularly problematic in wrap investment platform structures.
88. Further guidance would be appreciated on how these costs should be calculated for inclusion in any ICR disclosed in the PDS.

Disclosure of “indirect fees” in periodic statements

89. Paragraphs 90 to 93 below assume that it is acceptable for issuers of superannuation investments through a life company to adopt a ‘look through’ approach and show the respective fees against the appropriate fee type for e.g. the life policy fee as an explicit fee rather than an indirect cost. See the section headed “*Investments via a life policy*” (paragraphs 82 to 84 above) in which we seek ASIC confirmation in RG 97 that “look through” a life policy is acceptable.
90. Periodic statements are required to disclose *Indirect Costs of Your Investment* being the approximate amount that has been deducted from a member’s investment and includes amounts that have reduced the return on a member’s investment that have not been charged directly to a member as a fee.

91. In paragraph RG 97.147 of Draft RG 97, ASIC sets out guidance that the amount to be disclosed as *Indirect costs of your investment* in periodic statements should align to the Indirect Cost Ratio disclosure in any PDS and should not include administration and investment fees which should be considered to be fees directly charged to the member in performance of these functions. However, these fees will not be shown in the transaction list in any periodic statement as they are included in the unit price and are not directly debited in the member's account. In addition, any buy-sell spread charged by a reduction in the unit price will be similarly excluded from *Indirect costs of your investment* and not shown in any transaction details in a periodic statement.
92. Accordingly, ASIC guidance is sought on how investment fees, administration fees and any buy-sell spread charged by the trustee by way of a reduction in the unit price should be disclosed in periodic statements if these "indirect fees" are not to be included in *Indirect costs of your investment*. The treatment indicated in paragraph Draft RG 97.147 appears at variance with industry practice. We are otherwise not aware of ASIC guidance as to how to show "*Indirect costs of your investment*" in a periodic statement (per clause 301 of Schedule 10) (such as buy/sell spread, investment fees or administration fees charged by way of a reduction in a unit price), given clause 301(2) of Schedule 10 notes that the amount inserted in "*Indirect costs of your investment*" "must include" certain amounts (that it, is not necessarily exhaustive). Various views are held among industry including that indirect costs (including any buy/sell spread – even if disclosed as a "fee" in the PDS) would still need to be calculated and included somewhere as part of the "*Indirect costs of your investment*" disclosure in a periodic statement. The application of these matters to periodic statements is an area of confusion among industry and ASIC guidance is requested.
93. Further, we seek an extension of ASIC's facilitative compliance period for periodic statements to 1 July 2016 in order for members to make the necessary system changes to comply with ASIC's guidance in RG 97 (once finalised following this consultation) with a commensurate extension to ASIC's facilitative compliance period should final guidance (in RG 97) not be finalised by 30 June 2015.

Cost v fee – further guidance sought

94. For periodic statements in particular and generally, what ASIC understands as a 'fee' should be addressed. The Draft RG 97 notes that a cost charged as a fee takes the matter out of the indirect cost definition, without guidance as to what ASIC considers a fee to be. Given the distinction is important for the indirect cost definition, ASIC might consider whether or not to align its view of a 'fee' to that of APRA as set out in APRA FAQ 122 (accessed from APRA's website on 23 February 2015):

“FAQ 122: What is the difference between fees, costs and expenses within the APRA reporting forms? (amended 23 October 2014)”

A: The terms ‘fees’, ‘costs’ and ‘expenses’ are used in a range of ways by different industry participants. For clarification, APRA has defined these terms as they apply in the reporting collection.

- **Fee:** means an amount that is directly charged to a member (regardless of who pays the fee) and will form part of the fee disclosure required in PDSs. *Reporting Standard SRS 540.0 Fees* (SRF 540.0) collects information on fees as do *Reporting Forms SRF 700.0 Product Dashboard* (SRF 700.0), *SRF 702.0 Investment Performance* (SRF 702.0) and *SRF 703.0 Fees Disclosed* (SRF 703.0).
- **Cost:** means an indirect or embedded amount that the RSE licensee draws from members; these may or may not be disclosed and can take the form of a deduction from a member’s return, contributions or balance. SRF 700.0, SRF 702.0 and SRF 703.0 collect information on both fees and costs including costs which form part of the indirect cost ratio.
- **Expense:** means the amount that the RSE licensee incurs in operating the fund. *SRF 331.0 Services*, collects information on expenses as does *SRF 330.0 Statement of Financial Performance*, *SRF 330.1 Statement of Financial Performance* and *SRF 330.2 Statement of Financial Performance.*”

Platforms and disclosure of fees and costs under section 1012IA

95. The PDS law has changed significantly since ASIC finalised its policy on section 1012IA and issued Regulatory Guide 184. Since that time, the short-form PDS regime (i.e. the regime in Schedules 10D (superannuation) and 10E (simple managed investment schemes) of the Corporations Regulations) has been released resulting in questions on fee disclosure where an integrated PDS is adopted.
96. It is currently unclear how the accessible financial product’s fees should be disclosed in a superannuation fund’s integrated PDS particularly given the divergence in terminology between a superannuation fee table and a managed fund fee table. The FSC recommends that ASIC expand RG 97 to address these types of issues.

Consistency of the Class Order (i.e. CO 14/1252) with ASIC policy on platform costs disclosure

97. RG 97 could be interpreted in a way that is inconsistent with *RG 184 (Superannuation: Delivery of product disclosure for investment strategies)* and related CO 06/636, and *RG 148 (Platforms that are managed investment schemes)* and related COs 13/762 and 13/ 763.
98. We assume that no inconsistency was intended and therefore suggest that the wording in RG 97 be clarified to remove any suggestion of inconsistency.
99. In particular in Draft RG 97.29 and 97.30 it is not always clear which entity is being referred to and which product’s PDS is being referred to. Nor are all the intended practical ramifications of paragraph RG 97.29 clear.

100. Below is the text of Draft paragraphs 97.29 and 97.30 with five FSC Comments noting areas of some confusion among FSC members and which we request ASIC clarify by amending or expanding RG 97 to remove any ambiguity raised in the FSC Comments:

Draft RG 97.29 *If there is an arrangement (e.g. IDPS) where a product issuer* ^{See FSC Comment 1}
provides a retail client with a PDS under s1012IA for a trust, body or other structure that is invested in through the offered product or investment option—in order for the retail client to give an instruction about an investment in that product or option—then that trust, body or other structure is not an interposed vehicle. For example, if a superannuation wrap platform allows retail clients to provide instructions on whether to invest in a registered managed investment scheme that has a PDS (which is to be given to retail clients before they make an investment in that investment option), then the registered managed investment scheme is not considered to be an interposed vehicle for the purposes of disclosure by the superannuation platform ^{See FSC Comment 2}

Note: Class Order [CO 13/763] requires an IDPS guide to provide disclosure of the interests in the IDPS in accordance with Sch 10, as if the interests were managed investment products.

^{See FSC Comment 3} **Draft RG 97.30** *On the other hand, if the PDS* ^{See FSC Comment 4} *describes the asset allocation for the investment option (e.g. a balanced option or a product) as including an investment in a trust, body or partnership of a particular type that is predominantly in the business of investing in securities or financial products, (e.g. hedge funds or private equity funds) then these funds would be interposed vehicles and their costs would need to be considered in the calculation* ^{See FSC Comment 5} *of the indirect costs for the investment option or product.*

FSC Comment 1: Is the “product issuer” being referred to here the IDPS operator or other platform operator; or is it the issuer of the underlying product in which the platform invests? Presumably the former, however we request that ASIC refine draft RG 97.29 to clarify this.

FSC Comment 2: The position that the scheme in this example is not an interposed vehicle for the purposes of paragraph (1)(a)(ii) of the definition of “101A Indirect costs” in the Class Order seems appropriate. However, this paragraph (i.e. Draft RG 97.29) might be interpreted as implying that the scheme is nevertheless “property attributable” to the investment option of the platform pursuant to paragraph (1)(a)(i) of the definition of *Indirect costs* and hence that the costs of the scheme should be included in the indirect cost ratio for the platform (i.e. included in the

indirect cost ratio for an IDPS in its IDPS Guide or for a superannuation platform in the superannuation product PDS).

Such a conclusion would conflict with Example 7 in Draft RG 97.33 and more fundamentally would conflict with existing ASIC policy positions. For example, see RG 148.162 – 148.166 and notional paragraph 912AD(4)(e) as inserted by IDPS CO 13/763 ; and superannuation platform disclosure option 3 under CO 06/636).

FSC Comment 3: Is this paragraph 97.30 intended to be a continuation of the subject of platforms? It appears so but this is not clear.

FSC Comment 4: Is this referring to the platform’s PDS or the PDS for the underlying investment option? If referring to the platform’s PDS, then is this paragraph saying that the costs of the hedge fund or PE fund should be included in the ICR for the *platform* product (i.e. included in the ICR in the IDPS Guide or super platform PDS)? If so, that would be an inappropriate outcome and inconsistent with the other IDPS/super platform RGs and COs already referred to.

FSC Comment 5: “Calculation” for the purposes of which PDS? The PDS (or IDPS Guide) for the head platform, or the PDS for the hedge fund or PE fund? If the former, this would be an inappropriate outcome as mentioned above. Such a conclusion would conflict with Example 7 in Draft RG 97.33 and more fundamentally would conflict with existing ASIC policy positions for IDPS and superannuation platforms. For example, such an outcome would conflict with RG 148.162 – 148.166 and notional paragraph 912AD(4)(e) as inserted by IDPS CO 13/763; and with superannuation platform disclosure option 3 under CO 06/636.

Minor drafting point on CO 14/1252

101. Paragraph 6(a)(iv) of the Class Order purports to insert a revised definition of Indirect Costs into Schedule 10 of the Corporations Regulations 2001 (Cth) by way of inserting a new clause 101A. As a drafting point, it appears to us that this sub-paragraph (iv) should more appropriately be numbered as paragraph (b), as the subclauses to paragraph (a) all relate to changes within clause 101 (not clause 101A). Further, the operative wording which inserts the definition of *Indirect costs* does not appear correct, and should be amended as marked up below:

~~(iv) by inserting after the definition of **withdrawal fee**:~~ (b) after clause 101, insert:

102. The existing paragraphs (b) to (h) of the Class Order should then be re-numbered accordingly as paragraphs (c) to (i).

Thank you for the opportunity to make this submission and for ASIC's continued and ongoing consultation and engagement with industry on fee and cost disclosure matters.

Please contact Stephen Judge on (02) 9299 3022 if you have any questions on our submission.

Yours sincerely



Stephen Judge
General Counsel