FSC FINANCIAL SERVICES COUNCIL

7 May 2015

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

By email only (to Maan Beydoun)

Dear Maan

FSC comments on the 28 April 2015 draft of ASIC Fee and Cost Class Order Amendment (which relates to 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 28 April 2015 draft amendment (the **Class Order Amendment**) to the Class Order 14/1252 on fees and costs. ASIC provided an extension for FSC to lodge our submission to 7 May 2015. Given the law is the Class Order we consider that a period in the nature of Exposure Draft legislation (perhaps at least 2 weeks) should be provided to review (what will be the law), other than Class Orders which are simple in drafting or subject matter or which are unquestionably machinery and minor (such as changing transition dates). We observe that consultation on the fee and cost Class Order has occurred since around August 2014, so a longer period to review the Class Order is we think reasonable. That said, we do thank ASIC for allowing FSC to comment on a draft of the Class Order.

2. FSC supports comparable and consistent cost and fee disclosure. This assists consumers to compare products and assess fees and costs.

3. Given the complexity of the subject matter and the complex drafting, *our members would like an opportunity to meet (or have a conference call) with ASIC on this submission after ASIC has had an opportunity to consider the submission*. We observe that Class Orders are "law" and the Class Order Amendment clarifies and re-writes the law (by supplementing/refining the fee and cost disclosure regime) and therefore we request that ASIC provide an opportunity to meet (or call) ASIC to discuss our submission with our members. We acknowledge there have been multiple consultations but note that this is the first time our members have seen the proposed Class Order Amendment.

4. As previously communicated by FSC to ASIC, the transition period is one of the key issues. ASIC would be aware that any change to PDS law, and any change to periodic statement content requirement in particular, requires a transition period which allows industry a fair and reasonable time to implement the changes, particularly periodic statement content requirements which involve system/IT changes. The Class Order Amendment does not

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commensurately move the transition period even though the Class Order (as proposed to be amended) and the associated RG 97 is not finalised. We urge ASIC to commensurately move the transition period. We comment on this further in this submission.

5. We also refer in this submission to ASIC Regulatory Guide 97 *Disclosing fees and costs in PDSs and periodic statements* (**Draft RG 97** or **RG 97**) which is currently being reviewed by ASIC. We refer to our 22 October 2014 submission on the fee and cost Class Order, which has now been finalised as ASIC Class Order 14/1252. We also refer to our 2 March 2015 submission relating to the Draft RG 97. Many of our comments which we made in those submissions apply. Therefore this submission should be read in light of our 22 October 2014 and 2 March 2015 submissions.

6. Our comments (in addition to those contained in the prior submissions referred above) are below and provided in a tight timeframe. They reflect the comments of our members to date. (Given the complexity of the Class Order Amendment and that our members will need to digest the final RG 97, members and FSC may approach ASIC with further questions, comments or requests for clarification.) The Class Order is important (as it is the law) but to the extent that any clarification or guidance may be included in RG 97, which we understand will be updated prior to 1 July 2015, the key will be both the Class Order (as amended) and any ASIC guidance, expectation or clarification contained in RG 97. Due to the complex drafting of the Class Order and draft Class Order Amendment, this may lead to different understandings or interpretations (except where the policy is clear perhaps). Hence RG 97 commentary is important to assist consistency of interpretation. There has not been complete alignment of FSC member interpretations on the Class Order Amendment - FSC considers this may possibly reflect the complex drafting of the Class Order Amendment as well the limited timeframe to collectively discuss the Class Order Amendment and reach consensus on interpretations (where possible).

7. We have not reviewed the proposed updated RG 97 (although our 2 March 2015 submission did comment on ASIC's proposals for RG 97 set out in the ASIC *Review of Regulatory Guide 97,* 12 December 2014).

8. FSC acknowledges the difficulty and complexity of the fee and cost disclosure regime, and that ASIC is seeking to facilitate clarity in light of the regulations. We also acknowledge that it is no easy task to clearly draft the necessary refinements by Class Order. Our comments are – as always – intended to be constructive. We thank ASIC for continuing to consult with our members.

9. A consistent theme of comments received from FSC members is that interpreting the Class Order and the Class Order Amendment has its difficulties given the complex drafting style and the need to navigate between the Corporations Regulations and the Class Order. Therefore any explanation provided by ASIC in RG 97 to clarify ASIC's intention is critical. FSC expects that over time industry is likely to seek further ASIC guidance depending on what is covered in the final form of RG 97.

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10. Our members are concerned with a variety of issues with the draft Class Order Amendment. Broadly, there is a concern that the amendments create even greater complexity (and therefore uncertainty) in an already complex regime. We are concerned that some of ASIC's intended outcomes are not satisfied by the draft Class Order Amendment. Our members also have a variety of policy and technical concerns with the drafting.

Transition

11. As a general principle, transition periods should not commence prior to finalisation of all the material which regulated entities need to comply with or have regard to (such as ASIC regulatory guides). In this case, that material is any Class Order (as proposed to be amended) and RG 97. RG 97 will contain guidance which industry will need to have regard to. Accordingly, the transition period needs to accommodate the fact that the relevant material is not yet final. To be clear, FSC is not asking for an extension to the *length* of the transition period but rather we reiterate that the transition period should commence from a suitable time after finalisation of this material. Hence, ASIC should commensurately move the transition date currently set out in Class Order 14/1252 as that Class Order is not final (as it is to be amended) and further ASIC guidance (in RG 97) is not final. The transition period should also have regard to the fact that some of our members have already, or will by 30 June 2015, opt in early into the Class Order based on its current form (that is, pre the draft Class Order Amendment). Hence we request the following transition arrangements (we reiterate our previous submissions in this regard) apply *provided ASIC finalise the Class Order amendment and RG 97 no later than June 2015*:

   (a) **New PDSs**: New superannuation and managed investment PDSs first *issued* (that is dated) on or after **1 January 2016** must comply with the Class Order (as amended);

   (b) **Existing PDSs**: Existing superannuation and managed investment PDSs first *issued* (that is dated) prior to 1 January 2016 must be updated to comply with the Class Order by **1 January 2017**.

Early opt in

12. Regardless of the transition period, issuers should be able to opt in early. In that regard the Class Order drafting should accommodate that during the transition period, the law should allow *either* the current arrangements (pre the Class Order Amendment) *or* the post Class Order Amendment arrangement, so that:

   (a) existing PDSs can be updated progressively throughout the transition period (up until 1 January 2017 for PDSs dated prior to 1 January 2016, as previously submitted);

   (b) any new (including replacement) PDSs dated prior to 1 January 2016 should not have to be reissued again within a short period (i.e. firstly to comply with existing disclosure

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requirements and then again shortly thereafter to comply with these new requirements).

13. This is particularly relevant where the proposed amendments rectify previous drafting errors in the Regulations and/or the Class Order, such as with the Consumer Advisory Warning (**CAR**), where correct disclosures should be sanctioned by the law *as soon as it is practicable* for the issuer to update their PDS. However, it should not be necessary for an issuer to update/replace a PDS just to correct the CAR since this disclosure is being updated to correct anomalies in the original regulations.

14. By the same token, a number of issuers will have already opted into compliance with ASIC Class Order 14/1252 (in its current form). It may be too late for these issuers to comply with the amendments in the draft Class Order Amendment (for existing PDSs). Accordingly, the FSC recommends that ASIC provide transitional relief for the amendments (this is our preference), or if ASIC disagrees with providing transitional relief then ASIC should issue a no action position for those who comply with the current version of the Class Order.

15. Finally, it should not be necessary for a new or replacement PDS that includes the new fee disclosure requirements ahead of the required date to contain a statement that it has adopted the Class Order early. Such a statement would mean nothing to the consumer and would become obsolete anyway as the compliance date passes during the life of the PDS. It should also not be necessary for issuers to notify ASIC of early opt-in.

Costs for OTC derivatives

16. We understand ASIC has made its policy decision. ASIC will be aware that we do not agree that a buy-sell spread of an OTC derivative would generally be an indirect cost. We refer ASIC to our prior submissions on OTC derivatives set out in our 22 October 2014 and 2 March 2015 submissions. Those submissions set out suggestions for ASIC to achieve the policy objective (such as an anti-avoidance text for entities who use derivatives for the pre-dominant or sole purpose of not disclosing indirect costs – we observe that trustee/responsible entity duties would also be relevant here). We refer to paragraph 18 of FSC's 22 October 2014 submission in relation to an anti-avoidance test. In addition to our detailed comments on derivatives in our prior submissions we particularly wish to reiterate that FSC members inform FSC that capturing "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 for the Class Order (i.e. CO 14/1252) that *"…the class order will have a minor and machinery impact and therefore no Regulation Impact Statement is required."*.

17. Without resiling from our views above on ASIC's approach to derivatives, while the proposed changes in the Draft Class Order Amendment make the provisions clearer than the Class Order, the changes do not address the fundamental issue of why the buy/sell spread (to the extent that can be reasonably determined – see our prior submissions on ASIC's approach to

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OTC derivatives) for non-hedge OTC derivatives are now to be treated as indirect costs rather than transaction costs. Nor does it explain why there is a hedging exception for managed funds but not for superannuation funds.

Investment option definition

18. We wish to raise a potential matter in relation to the new definition of "investment option" which may have unintended consequences for switching and "switching fee". We have not had time to consider this in detail but we request ASIC to consider if the new definition of "investment option" has any unintended consequences for "switching fee". Provided there is a reasonable time to do so, we can engage with our members on this aspect further if ASIC requests. In order to provide our submission promptly however, we simply ask ASIC to provide assurance that it has considered the matter and it does not consider there are unintended consequences of the new definition of "investment option" for the "switching fee" definition.

19. Our members have noted that the proposed Class Order Amendment has not addressed the problems with the "switching fee" definition in the Class Order, which currently incorrectly limits switching fees for superannuation products other than MySuper products to **cost recovery only**.

20.

Recommendations:
ASIC consider the proposed new definition of "investment option" as it applies to the definition of "switching fee".
ASIC also consider amending the relevant part of the definition of "switching fee" to read: "(b) for a superannuation product other than a MySuper product–means a fee paid or payable when a member switches all or part of the member's interest in the superannuation entity from one investment option or product in the entity to another".

Consumer Advisory Warning

Paragraph 4(f) Class Order Amendment - Superannuation product consumer advisory warning ("CAR")

21. We welcome ASIC rectifying the consumer advisory warning in superannuation Product Disclosure Statements. We do however have some concerns with the proposed amendments which are outlined below.

22. The reference to "your employer" in the revised CAR for superannuation products is not universal. It is really only relevant to employer sponsored superannuation products. The

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reference is certainly not relevant in superannuation products where the fund does not accept employer contributions, for example a superannuation pension offer. Therefore, we suggest inserting the words ", as applicable," between "employer" and "may". This is consistent with the CAR for managed investment products where the corresponding sentence includes "where applicable" at the end. Alternatively (and preferably), a trustee should be able to omit the words "or your employer" if they are not applicable.

23. In addition, to avoid giving the impression that all fees and costs are negotiable, a trustee should be able to indicate which fees are negotiable as provided for in the following sentence:

> *You [or your employer] may be able to negotiate to pay lower [investment/administration/switching/exit] fees.*

24. **Recommendation:** The sentence in the CAR be amended to read as follows (with optional text as applicable appearing in square brackets "[ ]" below):

> *You [or your employer] may be able to negotiate to pay lower [investment/administration/switching/exit] fees.*

Periodic statement amendments

25. We welcome ASIC addressing the issues of indirect fee disclosure in periodic statements. We do however have some concerns with the proposed amendments which are outlined below.

26. While we support the clarification in relation to periodic statements, our members are particularly concerned about ensuring there is an appropriate transition period in particular relating to the proposed amendment to clause 301 in Schedule 10 of the Corporations Regulations. **Any further changes to periodic statement templates necessarily entail lead time for systems adjustments, as well as increased costs**. In addition, the note immediately after the proposed revision to clause 301 potentially creates a further degree of confusion. If the note is purporting to introduce a revised treatment for unitised fees charged by the super trustee, this needs to be properly enunciated by an appropriate Class Order modification.

Paragraph 4 (h) - Disclosure of 'indirect fees' in periodic statements

27. Our members have particular concerns with the proposed drafting for the changes for *periodic statements*. Paragraph (h) of the draft Class Order Amendment amends the indirect costs disclosure in *periodic statements* and inserts what our members consider to be an ambiguous note at the end of clause 301. This has caused confusion, and varied and uncertain interpretations of ASIC's drafting, among our members.

28. Under clause 301 of Schedule 10 to the Regulations, periodic statements are required to disclose Indirect costs of the investment being the approximate amount that has been

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deducted from a member's or account holder's investment, including amounts that have reduced the return on the member's or account holder's investment but are not charged directly as a fee.

29. Under clause 301(2)(a) the amount inserted for a MySuper product or an investment option offered by a superannuation entity must include the indirect costs for the MySuper product or investment option and under clause 301(3), the amount must be shown as a single total amount in dollars.

30. The changes to the Corporations Regulations imposed by the *Superannuation Legislation Amendment (MySuper Measures) Regulation 2013 (Cth)* do not include an obligation to disclose in periodic statements fees which are deducted from unit prices and crediting rates before they are struck, such as investment fees and some percentage-based administration fees.

31. However, clause 301 does not limit this amount to only the indirect costs of the MySuper product or investment option and as such some FSC members have interpreted this clause to mean that it may include any fees that are deducted from fund assets before the unit price is struck for a MySuper Product or investment option ("**indirect fees**") (and that are not a direct deduction from the member's account). This interpretation is also consistent with the previous definition of Other Management Costs that was amended by the *Superannuation Legislation Amendment (MySuper Measures) Regulation 2013*.

32. The draft amendment proposed to clause 301 suggests that superannuation providers must separately disclose indirect fees from indirect costs in a *periodic statement,* along with changes to the prescribed text to clarify that Indirect cost of your investment should not include any fees (i.e. should be restricted to indirect costs only).

33. A consequence of this means that there are no requirements for prescribed wording around indirect fees leaving open the possibility that different industry participants will disclose indirect fees in different ways.

34. The note inserted by the draft Class Order Amendment refers to fees charged that are not reflected in transactions in the periodic statement needing to be disclosed separately in periodic statements. Including this in a note suggests that the law currently requires separate disclosure of these amounts – and various FSC members consider this is incorrect (although there have been different interpretations due to the uncertainty of the regulations). We consider it beyond the scope of technical amendments to include substantive amendments, particularly through the use of a note. We acknowledge ASIC's intent to clarify the previous varied interpretations and we therefore strongly urge ASIC to consult (on a targeted basis) with various affected FSC members and FSC as to the impacts of the proposed changes to the periodic statement content requirements. In saying this, this is not a disagreement as to what is or should be the approach but we make ASIC aware that industry is uncertain as to the impacts of the current proposed Class Order Amendment and some members have significant

concerns in relation to potential IT and system build impacts. Hence, we urge ASIC to quickly consult with industry and FSC on this point (a conference call may suffice but a meeting with ASIC and affected FSC members would be preferred).

35. (**Cost Impacts**): Unlike changes to Product Disclosure Statements generally, changes to *Periodic Statements* can only be implemented by changes to information technology systems. Any changes to information technology systems require a long time to develop and implement and are extremely costly.

36. As the Class Order did not contemplate any changes to clause 301 we believe that the changes now being proposed to periodic statements should be subject to the Regulatory Burden Measurement Framework given that there would be significant additional costs involved to make these changes. Based on past experience in implementing the changes introduced by the MySuper Measures Regulations, one of our members has estimated that applying the new requirements across all products could cost in the region of $1.5 million. Even if the changes were restricted to contemporary products only (i.e. those with a current PDS on issue with the corresponding disclosure of Indirect Cost Ratio), the same member estimates costs could be in the order of $0.8 million. (While FSC has not verified some further anecdotal evidence passed on to FSC in preparing this submission, FSC has also been informed by another member that the IT changes for some members may well be multiples of 7 figures - that is multiples of $million.)

37. **Recommendation**: ASIC consult on refinements to clause 301 for example consult on clause 301 being amended <u>for superannuation products</u> as follows:

    (1) For superannuation products, the following text and the appropriate amount, in dollars, must be inserted after the part of the periodic statement that itemises transactions during the period:

    Indirect fees and costs of your investment

    This approximate amount has been deducted from your investment and includes all amounts that have reduced the return on your investment but are not charged directly to you.

    (2) The amount inserted must include all investment fees, administration fees and indirect costs of any MySuper products or investment options offered by a superannuation entity that are not otherwise included in the list of itemised transactions.

38. Industry needs clear guidance from ASIC as to how indirect fees are to be disclosed in periodic statements. We refer ASIC to paragraph 92 of our 2 March 2015 submission.

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Periodic statements – summary

39. In the limited time available to garner views of the membership, in summary:

(a) There has been uncertainty as to how the periodic statement content requirements apply to indirect fees incorporated in the unit price and which are not separately shown as a transaction in the periodic statement – an uncertainty generated by the regulations which are not clear on this point. (We welcome ASICs efforts in seeking to remove the uncertainty.)

(b) While there may be varied views on the matter, some FSC members have noted that to the extent that changes proposed by the Class Order Amendment would require a "rolling up" of indirect fees (incorporated in a unit price) in *periodic statements* (i.e. to include/"roll up" indirect fees incorporated in a unit price) this may have significant transitional and system implications and therefore we urge ASIC to meet (or call) with FSC and FSC members on this particular aspect prior to finalising the Class Order Amendment. We have included some cost information above. FSC supports the principle of robust fee disclosure and is not taking any policy issue with the principle of disclosing fees – rather we point out to ASIC that prior to finalising its clarification in relation to indirect fee disclosure in *periodic statements* ASIC should reach out to FSC members to understand the cost and systems implications so that appropriate consideration can be made by ASIC in relation to this matter prior to any final position being determined by ASIC.

(c) Given the uncertainty (and therefore varied views) on the inclusion of indirect fees (included in unit prices and not separately charged as a fee) arising under the current regulations, FSC considers that a targeted consultation is required by ASIC prior to finalising the position for *periodic statements*. For example, some members have noted that to change the law (compared to members' current interpretation based on the Corporations Regulations) to now require rolling-up of indirect fees in unit prices, should be subject to a regulatory impact analysis.

(d) In conclusion (on the periodic statement points), FSC members support ASIC acting on industry uncertainty and varied interpretations of the *periodic statement* provisions, but we urge ASIC to undertake further consultation with industry on this aspect in particular prior to finalising the Class Order Amendment.

40. ***Observation***: The note to clause 301 in the Class Order Amendment is causing some confusion as to ASIC's intention (meaning our members are confused as to how they should read clause 301 together with the note). Given some uncertainty and different interpretations of the draft Class Order Amendment in relation to *periodic statements* and given the IT/systems implications whenever *periodic statement* content requirements are amended or clarified, we think that ASIC must undertake a brief and targeted consultation with FSC members to discuss this point prior to finalising the Class Order Amendment. FSC will facilitate any meeting or conference call to facilitate this suggested targeted consultation.

Increased complexity with *Interposed Vehicle* definition

41. In the background information in the email ASIC sent to the FSC which attached the Class Order Amendment, ASIC suggests that the new definition of "Interposed Vehicle" will reduce complexity. However, our members feel differently. The definition of "Interposed Vehicle" in the Class Order imposed a simple one tiered test, being whether or not the vehicle satisfied one of the exemptions to the definition.

42. In relation to the revised definition of *interposed vehicle* in the proposed Class Order Amendment, our preliminary assessment is that the new 50% exposure by asset valuations and *relevant securities* concepts potentially raise various outcomes as to whether or not an underlying investment is an interposed vehicle. These may or may not be consistent with ASIC's intentions in introducing the new tests. *Further consultation should therefore be undertaken, including by way of clarification of ASIC's expectations in a revised draft RG 97*. To assist industry applying the Class Order (post Class Order Amendment) consistently, we request that ASIC explain in detail in RG 97 ASIC's intention and reasons for each of the proposed changes, such as why certain investments are included and others are excluded (e.g. real property in the definition of relevant securities), and setting out the differences between the draft Class Order Amendment and the existing Class Order so that members can resort to this material in applying the amended Class Order and RG 97.

43. The draft Class Order Amendment sets out a significantly more complex definition which requires multiple layers of tests to be assessed in order to determine whether an entity is an interposed vehicle. For example, the new definition of "***interposed vehicle***" would require two threshold tests to be considered in order to determine which *interposed vehicle* test would apply.

44. In particular, our members would firstly need to undertake the following to determine the extent of an entity's investment in "relevant securities":

    (a) an analysis of the assets of the vehicle to determine the extent to which it is invested in securities or other financial products; and

    (b) an analysis of those securities or other financial products to determine whether they are a means to make an investment in real property or confer control over another entity.

45. This analysis would need to be undertaken in order to determine which *interposed vehicle* test is to be applied, and which exemptions are applicable. Accordingly, once the entity's amount of relevant securities is determined, there are additional tests to be applied.

46. In the limited time available, we do not understand the second limb of the definition of "***relevant securities***". Some of our members have indicated they are not sure what the definition means.

47. The above outline demonstrates the significant additional analysis required in order to ascertain whether or not an entity is an *interposed vehicle*.

48. Further, we do not agree that a body, partnership or trust should be classified as an interposed vehicle on the basis that 50% of its assets are invested in relevant securities.

49. Presumably, this has the potential to capture a wider range of investments simply because the relevant entity holds 50% securities or financial products on their balance sheet (we also note that no distinction is made between an entity that invests on its own behalf or in a fiduciary capacity). In addition, it should not be the expectation that responsible entities or trustees review the balance sheet of various investments for the purpose of determining whether they are an interposed vehicle.

50. ***Recommendation***: ASIC revert to the original drafting of the definition of *interposed vehicle*, but change that definition to address our prior submissions, for example, by aligning the listed asset and unlisted asset exclusions.

51. The complexity in the Class Order Amendment definition of *interposed vehicle* makes it extremely difficult to determine what substantive changes ASIC proposes to make by replacing the current definition of *interposed vehicle*. It seems to us that, apart from the changes identified in the background explanation provided by ASIC to FSC along with the Class Order Amendment, there are few substantive changes intended by ASIC despite the significant rewrite of the definition of *interposed vehicles* in the Class Order Amendment and the increased complexity of the definition.

52. If ASIC determines to retain this definition of *interposed vehicle* (that is, as contained in the draft Class Order Amendment), it would assist industry's ability to interpret and apply the definition in a consistent manner, if ASIC provided a more detailed explanation of the substantive differences intended by ASIC between the current definition (contained in the Class Order) and the new definition contained in the Class Order Amendment, as well as provide worked examples in RG 97.

53. A potential alternative is to define *interposed vehicle* as a:

> *body, partnership or trust, for which the value of the interest of the product or option is predominately derived from the value of relevant securities.*

(FSC has not had an opportunity to fully canvass the potential alternative definition among the membership so we provide it as an initial suggestion only, subject to ASIC undertaking soft-consultation on the final wording.)

54. In particular, at a minimum we seek ASIC to clarify the application of the 50% test (if it proceeds with it) in ASIC's guidance (RG 97). We request that ASIC clarify in its guidance (RG

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97), exactly what types of vehicles would be caught and what types of vehicles this would not capture.

For example, it would appear to capture:

- open ended managed investment schemes;
- exchange traded funds;
- unitised investment trusts;

We think it would definitely not capture:

- shares in a company;
- listed property trusts; etc.

Minor Formatting suggestions

55. We make the following format comments for ASIC to consider in finalising the Class Order Amendment:

(a) In paragraph 4 of the Class Order Amendment, please insert a paragraph space between sub-paragraph 4(c) and sub-paragraph 4(d) (this is on page 1 of the Class Order Amendment);

(b) There is a space before the ":" (twice appearing) in sub-paragraph 101A(3)(a)(ii)(D) (on page 2 of the Class Order Amendment). Please remove the space in each case.

(c) Please insert a missing close bracket (i.e. ")") after "(7" on page 2 of the Class Order Amendment; and

(d) There is font variation within the Class Order Amendment (for example sub-paragraph 101A(3)(a)(ii)(D)(8) on page 2 of the Class Order Amendment).

Policy concerns

56. Our members still have significant concerns with the inconsistencies inherent within the indirect cost regime with no apparent justification for these differences. Some of these concerns and inconsistencies are set out below.

57. In particular:

(a) managed funds need not disclose their transactional and operational costs or the transactional and operational costs of interposed vehicles, but superannuation funds need to disclose their own transactional and operational costs and those of interposed

vehicles (which will include those of managed funds, even though the managed funds do not need to disclose those costs themselves):

(1) An out-play of this is inconsistency between managed funds and superannuation in that managed funds are now starting to be requested by superannuation funds to prepare a figure *that managed funds themselves do not or are not required to prepare* (even though transactional and operational costs are not treated as part of the management cost for a managed fund – in our view this managed funds treatment is the appropriate categorisation/treatment as transaction costs are not a cost of the "vehicle" but a cost direct investors (investing in the underlying assets invested in by the vehicle) would similarly bear).;

(b) managed funds need not disclose asset-based costs (only entity-based costs), but superannuation funds do;

(c) there is a managed fund exclusion from indirect costs of the buy-sell spread for OTC derivatives used in hedging, but no similar exclusion for superannuation funds;

(d) the definition of "relevant securities" excludes real property-related investments but not other similar investments, such as infrastructure investments.

58. ***Recommendations:***

(a) As previously submitted by FSC, apply the exclusions from management costs in the managed funds regime to superannuation funds.

(b) Extend the exclusion for real property investments to other unlisted assets, such as infrastructure investments.

59. Our members wish to reiterate our comments in paragraphs 41 – 47 and 85 – 88 of the FSC submission dated 2 March 2015. Any inconsistencies between the managed investment and superannuation fee and cost disclosure regimes will create potential inaccuracies and obscure fee and cost comparisons across funds for members. In order to resolve these issues, the application of rules in relation to interposed vehicles and indirect costs (including any transaction costs) should be consistent across superannuation and managed investment products. Obligations should not be imposed upon the trustee of a superannuation fund to estimate interposed vehicle indirect cost amounts or transaction cost amounts unless the managed investment product provider is required to disclose these as part of their overall indirect cost ratio. As cited in the FSC submission dated 2 March 2015, the current regime will be costly and cumbersome for superannuation trustees, limiting the clarity and consistency of fee and cost disclosure information for members.

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Technical drafting comments

60. Our members have a number of technical concerns regarding the operation of various parts of the draft Class Order Amendment. The following table lists some of the technical concerns with the draft Class Order Amendment raised by some of our members. We add the caveat/observation that for the reasons previously explained in this submission and given the complex subject matter and drafting there is not absolute unanimity on all interpretation issues among FSC's membership. The table below reflects a sample of comments raised by some of our members (but should not be interpreted by ASIC as a definitive view of FSC or any particular FSC member as to how the Class Order Amendment might be interpreted):

Our Ref	Class Order Reference	Term / Issue	Concerns
A.	Clause 101A(3)(a)(ii)(A) Meaning of "security"	The definition of indirect cost includes a reference to a "security" other than a share.	Section 92(1) of the *Corporations Act 2001* (Cth) defines a "security" to include debentures, stocks and bonds. Section 92(2) defines a security, when used in relation to a body, to include debentures of the body. It is not clear whether the reference to "security" in the draft Class Order Amendment is a reference to the section 92(1) definition or the section 92(2) definition.

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Our Ref	Class Order Reference	Term / Issue	Concerns
B.	Clause 101A(3) "buy-sell spread" for non-hedge OTC derivatives	The buy/sell spread of an OTC derivative is not an indirect cost (or should not be). We refer to FSC's prior submissions (22 October 2014 and 2 March 2015). Further, capturing this information can be very problematic and system intensive and our members are unclear on many aspects of what and how they would meet this requirement.	We think an anti-avoidance test is a better approach to ASIC's policy concerns. We agree that use of derivatives for the purpose of hiding fees or costs which would otherwise be disclosable would be a concern (to the extent the practice exists) and we think ASIC can and should address this by removing clause 101A(3) and instead applying an anti-avoidance test (see paragraph 18 of FSC's submission dated 22 October 2014). FSC members continue to support the approach of an anti-avoidance test instead of ASIC's current approach set out in clause 101A(3) which is an overly extensive approach (with systems and cost implications, and difficulties in compliance and measurement) compared to a more appropriate and targeted arrangement of using an anti-avoidance test previously submitted by FSC.
C.	Clause 101A(3) Apportionment of costs	Where a managed fund or superannuation fund is not the sole investor in an interposed vehicle, only a portion of the vehicle's costs should be reported in its indirect costs.	We recommend that clause 101A(3) be amended to include an express statement about this.
D.	Clauses 101A and 101B No express reference to needing to have an investment in an interposed vehicle	The definitions of "indirect costs" and "interposed vehicle" do not expressly state that a managed fund or superannuation fund must be invested in a vehicle, directly or through another interposed vehicle, for it to be an interposed vehicle.	We recommend that clause 101A(3) be amended to expressly acknowledge this.

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E.	Clause 101A(3)(a)(ii)(D)(1), (2) and (5)	Subclause (1) refers to a financial product other than the financial product to be delivered. Subclause (2) refers to an asset and subclause (5) refers to a commodity.	We recommend that subclause (2) be amended to exclude the financial product to be delivered.
F.	Clause 101B(1) Value of relevant securities	An interposed vehicle is a body, trust or partnership that has more than 50% of its assets by value in relevant securities.	This is problematic in the sense trustees should not be required to review balance sheets of various investments for the purposes of determining whether they are an interposed vehicle.
G.	Clause 101B(2) *Interposed vehicle* definition for listed entities holding less than 50% in relevant securities	Subclause (2) provides that a listed entity holding less than 50% in relevant securities is **not** an interposed vehicle unless, having regard to the PDS, it is the means of achieving the investment, rather than the investment itself.	The best way to explain our understanding of the drafting (although we are uncertain if our understanding is correct) is to give an example. A listed Sydney airport fund would be considered to be the means of achieving the investment in Sydney airport and so should be an interposed vehicle under this definition. However, an alternative understanding is a listed airports fund is the actual investment as it would invest in a portfolio of airports. The determination of whether or not the entity is the means of investment is based on an analysis of its purpose and asset portfolio. It is not determined by reference to what a managed fund or superannuation fund says about the entity in its PDS. Accordingly, we are concerned that this definition does not achieve its purpose (as we understand its operation). As noted above, our recommendation is not to proceed with this definition. However, if ASIC does determine to do so, we recommend that it provide a significant number of worked examples in RG 97 (if not the Class Order itself).

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H.	Clause 101B(2) and (3) Different tests for listed entities and unlisted entities	The test in subclause (3) differs substantially to subclause (2). It provides that an unlisted entity holding less than 50% in relevant securities is an interposed vehicle unless having regard to the PDS it is considered to be the true investment rather than the means by which the investment is made.	We see no policy basis for the establishment of different tests for interposed vehicles depending on whether the entity is listed or unlisted. As noted above, our recommendation is not to proceed with this definition of *interposed vehicle*. However, if ASIC does determine to do so, we recommend that the tests in subclause (2) and (3) be aligned.
I.	Definition of "relevant securities"	The definition refers to securities and other financial products that give control over a body, partnership or trust. Section 50AA of the Corporations Act defines "control" in relation to body corporates, but not partnerships or trusts.	We recommend that ASIC explain what test of control should be applied in relation to body corporates, partnerships and trusts.

Other

61. Upon finalisation of the Class Order amendment and RG 97, it would assist users if a consolidated Class Order was provided or the link to the consolidated (post Class Order Amendment) Class Order 14/1252.

62. 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. We think consultation on substantive Class Orders is appropriate and welcome and applaud ASIC for its sensible approach in undertaking multiple consultations prior to finalising the "law" (as set by the Class Order).

Please contact Stephen Judge on (02) 9299 3022 if you have any questions on our submission and (if ASIC takes up the request of FSC and FSC members) to arrange a call/meeting with FSC members on

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this submission (and in particular on the periodic statement content aspects) prior to finalising the Class Order Amendment.

Yours sincerely

Stephen Judge
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