CORPORATE SUPER ASSOCIATION

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Ms Maan Beydoun
Senior Specialist
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Australian Securities and Investments Commission
Level 5
100 Market St
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Dear Ms Beydoun

REGULATORY GUIDE RG 97: AMENDED DRAFT, JULY 2015
COMMENTS FROM THE CORPORATE SUPER ASSOCIATION

Background

Established in 1997, the Association is the representative body for large corporate not-for-profit superannuation funds and their employer-sponsors. The Association represents a total of 25 funds controlling $65 billion in member funds, held in a total of 695,396 individual accounts. In general, these funds are sponsored by corporate employers, with membership restricted to employees from the same holding company group, but we also include in our membership several multi-employer funds with similar employer involvement and focus.

General Comments

We appreciate ASIC's efforts to provide updated guidance on fee and cost disclosure.

We acknowledge the efforts that ASIC has made to clarify "reasonable estimates", which may assist us where funds of funds are involved, and where performance fees, by their nature, cannot be predicted.

We have received feedback from our members regarding the new documents, and the following general points are raised, representing serious issues for our funds.

- The provisions, as amended by CO 14/1252, are very complex. We would support the issuing of a revised CO 14/1252 instead of piecemeal modification.
- The efforts to reduce amounts included in "indirect costs" by re-allocation to "investment fees", have unfortunately resulted in further complexity, and will result in the inclusion of many estimates in investment fees.

- The new definition, "indirect fees", applying only to periodic statement disclosure, does not correspond to anything disclosed in the PDS.
- Difficulties arise because managed funds are treated differently from superannuation funds.

  The use of "indirect cost", where managed funds have "management costs", which correspond to some extent but do not completely overlap, creates difficulties for superannuation funds investing via managed funds. The result of the incomplete overlap is that superannuation funds cannot rely on the immediately disclosed information regarding indirect costs in the managed funds. They must delve deeper to find the larger group of costs to be disclosed in the superannuation context, notably transaction fees (excluded from "management fees" by clause 102, but not from "indirect costs") and operational costs (see RG 97 paragraph 66).

  It seems strange that superannuation funds should be required to disclose a wider group of costs in their indirect costs than do managed funds, thus inhibiting direct comparisons of similar products.

- For defined benefit funds, greater certainty is needed regarding the obligation of hybrid funds to disclose or not to disclose indirect costs in the PDS, in relation to the defined benefit members.
- For defined benefit funds, it appears from the discussion that indirect costs may be disclosed in periodic statements as "nil" where no charge is made to the member, but the PDS position remains unclear.

Further Detailed Comment

1. Examples of fees and costs

Paragraph 4(k) of the draft class order now requires trustees to include a note below the worked example of fees and costs in the PDS that includes the following text:

> *Additional fees may apply. And, if you leave the superannuation entity, you may be charged an exit fee of $x and a buy/sell spread which also applies whenever you make a contribution, exit, rollover or investment switch. The buy/sell spread for exiting is y% (this will equal to $z for every $50,000 you withdraw).*

The yellow highlighted text needs re-working to remove repetition.

We believe that there needs to be an exclusion, so that if a fund does not charge a buy/sell spread the relevant text can be omitted, rather than disclosing a fee of: "0% which will equal $0 for each $50,000 withdrawn." Paragraph 000.154 seems explicitly to require disclosure of an exit fee of nil in this note. We agree that "nil" needs to be shown in the table, but it is not needed in the text.

2. *Investment fees*

New paragraph 000.33 of the draft Regulatory Guide states:

> *For superannuation products, amounts payable by the trustee out of the superannuation fund for investment and administration are treated as fees and not indirect costs. This includes payments to an investment manager[s] acting for the trustee under a mandate including fees based on their performance or otherwise.*

This statement does not seem to be consistent with either the previous draft RG or other content of this version, which led us to conclude that in fact corporate funds' investment fees should be disclosed as indirect costs. Further, the statement is included under the heading "Fees are disclosed prospectively" and does not seem to be relevant to that heading. The inclusion of this paragraph needs to be reviewed, and if it is intended to be included then further explanation and clarification is required.

3. Updating a PDS

There is a new sub-section at RG 97 paragraph 000.24 to 000.28 inclusive entitled "Updating a PDS" which seems to suggest that PDSs may need to be updated more frequently than annually for changes in indirect costs. Indirect costs must be based on the costs incurred in the previous financial year (with an exception for new products which is not relevant here), but then RG 000.27 includes the following:

> *Updating the PDS for changes in indirect costs each year promotes comparability and the PDS may also need to be updated following the completion of a financial year. This would apply if what is known or ought to be known or reasonably estimated for the financial year that has ended after the PDS was prepared is no longer the same as indirect costs for the previous financial year. An amount for indirect cost disclosed in the PDS, which is incorrect to the knowledge of the trustee or responsible entity or no longer is a reasonable estimate, may be defective in its representations about indirect costs when considered against the indirect costs incurred the financial year that ends after the PDS was prepared.*

Consider the example of a fund with a 30 June year end. Such a fund would typically be able to calculate indirect costs for the previous year (say 2015) by the end of July (or the end of August if audit clearance on the financial statements is required) and then issue the PDS with a commencement date of, say, 1 October 2015 to allow for the requirement to give 30 days' notice of fee increases where the PDS is used for that purpose. That PDS should then apply (ignoring other fund specific changes) until 1 October 2016. But by 1 July 2016 the indirect costs shown will not be for "the previous financial year" and so the PDS will not comply.

This section should be reconsidered, so that funds can name the financial year in question (e.g. 12 months ending 30 June 2015) so that they only have to issue one PDS a year for this purpose.

4. Indirect fees

The RG discusses the meaning of indirect costs in great detail, then a new concept of "indirect fees" is introduced solely for the purpose of periodic statement disclosure. This term first appears in RG 000.169, which reads as follows:

> *In order for consistency between disclosures in the PDS and periodic statement, we consider that, for the purposes of the disclosure in the periodic statement for superannuation products, only an amount indirectly charged to members through interposed entities will be classified as an indirect cost, while any costs deducted from the superannuation fund that are fees and costs should be identified as indirect fees. For example, where an issuer charges a percentage-based investment fee which is reflected as a reduction in the unit price or crediting rate, that fee would be disclosed as an indirect fee and not included in the indirect costs...*

It is unclear how introducing an entirely new term solely for periodic statement disclosure, which is not referred to anywhere in the PDS, could enhance "consistency between disclosures in the PDS and periodic statement".

In addition, the explanation of this term in this paragraph remains somewhat unclear. We understood that funds which invest solely in PSTs and wholesale trusts were investing in interposed vehicles: hence, what we had previously disclosed as "investment fees" in the PDS would now be disclosed as indirect costs.

This understanding is consistent with the examples in the new draft RG. From RG 97 paragraph 000.169, therefore, it appears that trustees of such funds, as "issuers" of the periodic statement, are not actually charging percentage based fees that are reflected in the crediting rate: they are instead passing on such fees charged by the investment managers, so the periodic statement will show such amounts as indirect costs. This will be consistent with the PDS disclosure ***if this interpretation is correct***. It would be helpful if ASIC could confirm this in the RG.

5. *Exemptions for defined benefit sub-funds*

The RG continues to refer to "pure defined benefit funds", for the purpose of various carve-outs of disclosure irrelevant for such funds, such as employer defined benefit contributions, without acknowledgement that there are also defined benefit sections in hybrid funds.

For our membership, most defined benefit interests are now found in hybrid funds, which are not pure defined benefit funds, but which continue to include categories of membership (which may or may not be formal sub-funds), usually closed to new members, which would be pure defined benefit funds if those categories were stand-alone funds. Explicit recognition of these categories in RG 97 would assist trustees.

6. *Compliance with Corporations Regulations*

RG 97, paragraph 000.171, states that any movements of reserves must be reported in periodic statements to the holders of the superannuation product in accordance with reg 7.9.37(1)(k).

Corporations Regulation 7.9.37 (1)(k) is a fund information (i.e. annual report) requirement, and not a periodic statement requirement.

7. *Movements to ORFR*

ASIC continues to consider, in RG 97 paragraph 000.172, that ORFR deductions from crediting rates or fund assets or investment returns are costs that should be recognised as one or more of the prescribed fees.

We strongly disagree with this approach.

APRA Prudential Standard SPS 114: *Operational Risk Financial Requirement* requires that each trustee must maintain adequate financial resources to address losses arising from operational risks that may affect the fund. APRA has stated, in section 9.1 of its discussion paper on prudential standards for superannuation dated 28 September 2011, that Stronger Super seeks to improve the safety of the superannuation system by introducing a risk-based financial requirement for operational risk. We consider that setting aside resources to benefit members in the event of operational risk losses is fundamentally different from the deduction of fees or costs. While we agree that such provisions should be disclosed to members, in our view they should be separately disclosed and not included in either fees or indirect costs.

Yours sincerely

Mark N Cerché
Chairman
Corporate Superannuation Association