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SUBMISSION ON REPORT 391 — ASIC'S DEREGULATORY INITIATIVES May 2014
BY AUSTRALIAN SHAREHOLDERS' ASSOCIATION

We submit the following comments on ASIC's Deregulatory Initiatives. The Australian Shareholders' Association (ASA) has some 5,500 members, being retail investors in publicly listed entities. ASA is the only body representing this sector of the Australian financial community that has an active position in seeking to achieve improvement in the management of listed entities. ASA supports efforts to eliminate red tape that serves little purpose, but we are concerned that such a description can be used by companies and individuals to condemn or avoid necessary investor protections. We are critical of the recommendations of the Office of Best Practice Regulation which have resulted in substantial cuts to budgets and capabilities of ASIC and the Australian Bureau of Statistics; we believe that these will lead to a major detriment to consumers, smaller investors and the economy.

Corporations law and regulatory practice must achieve transparency, fairness and protection — not only for retail investors but for all investors. We welcome the statement of ASIC's strategic priorities in Paragraphs 2 and 14 and state that they should take precedence over the deregulatory aspirations set out in Paragraphs 3 and 9.

The risk-based approach referred to in Paragraph 7 is pragmatic but we urge caution in assuming unqualified benefits from the self-regulation mentioned in Paragraph 5. There is considerable evidence of the failings of self-regulation across a range of professions and industries.

Waivers from the law ("relief"). Paragraphs 20 and 21 deal with class orders and relief applications. ASA supports the publication of the reasons for approving or declining applications. This could be done anonymously and would provide guidance to the regulated population and to future applications.

Cooperation between regulators: APRA and ASIC reporting standards. Paragraphs 36-38: ASA welcomes this statement and in our submission to the Senate Inquiry into ASIC, we argued strongly for such cooperation. The boundaries between ASIC, APRA, ACCC and at times Treasury are not always clear, and ASA believes that where there is overlap there should be a "lead" regulator. Conversely, there are areas that seem to fall between the scope of regulators — at least in consumer law and finance — and unscrupulous operators design their business models to exploit those gaps.

Regulatory guidance. Paragraphs 39–40: The regulatory guides are helpful, as is the MoneySmart website. Regulatory Guide 107 and CO 14/26: ASA agrees with the requirement for a "prominent statement" but would strengthen the warning to say "ASIC strongly recommends that investors read the disclosure document". Investor protection would be enhanced by requiring issuers to provide links to the relevant notes and guides at MoneySmart. Clear and emphatic warnings are specifically needed for complex products as described in REP 384. We provide more comment under Paragraphs 65–69.

Market Stabilisation. Paragraphs 51–54: ASA would be concerned if there is any diminution of investor protection through "market stabilisation". There is a risk that the arguments set out in Paragraph 52 could be subverted by market manipulation. ASA would want to see comprehensive justification to support assertions that the lack of such legislation has caused inefficient or undesirable trading. We are doubtful that a change to legislation is warranted: in the rare cases where stabilisation might be justified, ASA believes that the present system of requiring issuers to apply to ASIC for relief is safer—as it enables ASIC to apply (and monitor) conditions that suit each particular case. As Paragraph 54 says, any relief must be subject to full disclosure of the extent and nature of the stabilisation, daily, by whom and the period for which the stabilisation is permitted. Any use of derivatives to effect, hedge or amplify these positions must also be disclosed.

Enabling automatic registration for managed investment schemes. Paragraphs 55–57: If automatic registration is to be introduced then stop orders and directions powers MUST also be incorporated into the law to ensure that non-compliant operations are prevented. While a risk-based approach is acceptable, events over the last few years indicate that this is an area where careful scrutiny of managed investment schemes is needed.

Replacing the requirement for an unlisted disclosing entity to lodge continuous disclosures with ASIC. Paragraphs 58–59: ASA accepts the proposal in principle but would need to be satisfied with how ASIC will apply surveillance, to ensure that disclosing entities comply.

Investor self-assessment and key facts sheets. Paragraphs 65–69: Further to our comments under Regulatory Guidance, ASA understands that the proposal in Paragraph 65 will be strictly limited to simple managed investment schemes. We support the idea of a pilot test in this limited sector, but would not be supportive of any proposal to expand the practice into a wider list of products or securities until there had been extensive risk analysis and evidence provided of the need (and benefits) to do so. Prior consultation with retail investor groups would be essential; the complex products discussed in REP 384 should never be considered suitable for this approach.

Under Paragraph 66, would the issuer have to produce an electronic copy of a PDS for ASIC or for its own website? If not, how would intending investors obtain further information, and how would such additional disclosure be monitored for content and consistency with the key facts sheets? Paragraph 67 states, "we expect the benefits of the proposals for product issuers to be: to give them early warning about whether investors understand ...." How and when would this happen? Are the fact sheets to be available for a period of a few weeks *before* investors can buy the product and give feedback within that non-investment period? If that is not the case, it would surely mean that the public could buy the product without any other investors having had the

opportunity to draw attention to possible misunderstandings or problems in the disclosure material.

The above connects with Paragraph 68. Self-assessment tools are worthwhile in principle, but even if rigorous and comprehensive there is still a risk that investors could delude themselves about the extent of their knowledge or ignore the tests entirely, especially if the marketing material is enticing. For the benefit of all parties, we suggest that if this approach is adopted, it be tied to a requirement that the investor must confirm in writing (or by a secure link to the issuer's website) that he/she has successfully performed the self-assessment tests and understands the relevant key fact sheet(s), including its risk summary.

There is ample evidence of investor ignorance, and that investors have lost billions of dollars from investing in products unsuited to their risk profiles. ASA is aware of ASIC's interest in behavioural economics and we are of the view that there is a significant risk that many investors overestimate their own financial knowledge, irrespective of the complexity of the financial product. Many of the promoters/advisers recommending some financial products do not adequately understand them either.

Improvements to auditor resignation requirements. Paragraph 74: ASA supports this proposal.

Yours sincerely

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Chairman