ASIC
Australian Securities & Investments Commission

Level 5, 100 Market Street,
Sydney NSW 2000
GPO Box 9827, Sydney NSW 2001
DX 653 Sydney

Telephone: +61 2 9911 2000
Facsimile: +61 2 9911 2414
www.asic.gov.au

Mr Paul Callaghan
General Counsel
Financial Services Council
Level 24, 44 Market Street
Sydney NSW 2000

7 December 2016

Dear Paul

Consultation Paper 264: Remaking ASIC class order on nominee and custody services (CP 264) and Proposed Draft Instruments

We refer to your letter of 5 October, your emails of 12 October and 7 November and to our earlier meeting of 14 September 2016 where some of your members provided feedback on the CP 264 proposal to require that retail client platform investors have access to underlying product issuer's internal and external dispute resolution system.

In this letter we briefly set out, for background, ASIC's existing policy in relation to this topic and also set out our observations on the themes we elicited from your members' feedback.

Background

Our longstanding view is that we do not consider that there should be an opportunity for regulatory arbitrage in circumstances where retail clients invest directly in a financial product versus where they indirectly invest in the same product through a platform.

As discussed in CP 264, in Consultation Paper 176: *Review of ASIC policy on platforms: Update to RG 148* dated March 2012, we state that we consider that platform clients should have access to a product issuer's internal and external dispute resolution system when they have concerns about investments made through platform.

In implementing the 2013 changes to the platforms policy in:

- ASIC Class Order [CO 13/762] *Investor directed portfolio services provided through a registered managed investment scheme* (**[CO 13/762]**) and
- ASIC Class Order [CO 13/763] *Investor directed portfolio services* (**[CO 13/763]**),

we did not proceed in applying a restriction on an acquisition of a financial product through a platform for a retail client where the underlying product issuer does not have a retail dispute resolution system. Instead, we specifically flagged in Regulation Impact Statement *ASIC policy on platforms: Update to RG 148* (June 2013) that we would implement this change once we had considered the matter further. We have since confirmed that the terms of reference for the existing

ASIC-approved dispute resolution schemes do extend to complaints by platform investors against an underlying issuer.

Furthermore, we specifically flagged our policy in paragraph 81 of ASIC Regulatory Guide 148 *Platforms that are managed investment schemes* (**RG 148**) dated June 2013, where we state that we consider that platform investors should have the protections applying to registered schemes as if they were investing in a managed investment scheme directly and investors should not lose those protections because they acquire interests in the managed investment scheme through a platform.

As stated in paragraph 82 of RG 148, the requirements in [CO 13/762] and [CO 13/763] restrict investments in unregistered managed investment schemes because the Corporations Act (the **Act**) restricts direct investment by retail investors in unregistered schemes. Where an investor must be given a product disclosure statement for an acquisition of interests in a managed investment scheme under section 1012IA of the Act or [CO 13/762] and [CO 13/763], the exclusion from registration in section 601ED(2) of the Act will not apply. This means that, when appropriate, the managed investment scheme will have to be a registered scheme.

The constitution of a registered managed investment scheme must, under section 601GA(1)(c) of the Act, set out the method by which complaints made by members in relation to the scheme are to be dealt with. An Australian financial services licence holder that deals with retail clients must have a dispute resolution arrangement in place that meets the requirements in section 912A(2) of the Act.

Investments by wholesale clients or sophisticated investors not impacted by proposal

A number of your submissions refer to circumstances where a product issuer issues units through a platform and the issuer does not have a retail dispute resolution system in place. For example, one submission states:

> *Revised clause 8 of the proposed Class Order would prohibit acquisition of investments in a managed fund if they do not have a compliant dispute resolution mechanism. Thus investors who wish to invest further monies in wholesale managed funds (i.e. 73% of the investments on that platform) may need to modify their investment strategies such that future investments are only made into retail investment products.*

As discussed in paragraph 24 of CP 264, the dispute resolution requirements apply to the underlying investment as if clients directly accessed the investment. It follows that if the platform client is a retail client, the dispute resolution requirements apply to the underlying investment as if the client had itself directly invested in the financial product. We consider that if a product cannot be accessed directly by a retail client because the issuer does not meet the requirements in paragraph 912A(1)(g) and subsection 912A(2) of the Act, then that same product should not be available to the retail client indirectly through a platform.

The platform operator will only need to ensure that an issuer or seller has a dispute resolution system that covers retail clients where the relevant platform investor is a retail client. The intention is that the dispute resolution requirement will be only relevant in circumstances where:

- if the platform investor had acquired the financial product itself directly, it would have done so as a retail client; and
- the platform acquires the financial product on the instructions of the platform investor.

We note that some amendments to the drafting in draft instruments attached to CP 264 may be required to more clearly reflect this requirement.

Longer transition period

A number of your submissions indicated that more time may be required to review investment lists, to liaise with underlying product issuers (including to implement updates to service level agreements), to conduct due diligence reviews of managed funds on the platform and to analyse and implement any necessary system changes.

We accept that it may take longer for some platform operators to comply with the proposed change. As such, we will provide for a longer transition period by imposing the proposed change in relation to access to dispute resolution system of underlying issuers. We will extend the start date for this requirement by six months so that the requirement will commence from 1 January 2018, rather than from 1 July 2017.

You have noted that there would be an ongoing requirement for operators to determine if changes to each product issuer's arrangements are remain compliant. The requirement relates to whether the platform operator has a "reasonable belief" in relation to certain matters. We think that a reasonable belief can generally be held based on representations by a product issuer, in a PDS or directly to the operator. Contractual warranties might assist a platform operator. We do not expect each platform operator to ask for details of the product issuer's dispute resolution arrangements. Further enquiries may be needed if there is a particular reason to doubt a product issuer's representations.

Balancing regulatory benefit and compliance cost

Given that currently product issuers only provide access to dispute resolution for platform investors where it has previously provided consent to the platform operator (and your members have advised that not many issuers, if any, have provided this consent), there is no data available on what the likely volume of complaints to underlying issuers might be. We note that some of your members have suggested that the volume of complaints is likely to be low.

While we appreciate the suggestion that the volume of complaints might ultimately be low, we also understand that in practice many cases complaints relating to the underlying issuer are ultimately resolved by the platform operator. We do not accept that any platform operator can, or would, be in a position to resolve all types of complaint relating to an underlying issuer. For example, we do not consider that a platform operator would be in a position to resolve systemic compliance concerns or address the root cause of disputes relating to underlying issuers.

We consider that there are several regulatory benefits in implementing the proposed changes, for example:

- to reduce the potential for regulatory arbitrage (such as a product issuer issuing to retail clients through a platform to avoid the dispute resolution requirements that would apply if the product was issued to the client directly); and
- to deter misconduct (where retail investors can complain directly to an underlying issuer, or to an external dispute resolution scheme, we consider that this may promote better outcomes for invests and deter sub-optimal business practices).

We also consider that if the volume of complaints to underlying issuers is ultimately low, then once implemented, the ongoing cost of maintaining the dispute resolution system will be lower.

No divestment required and no impact to exchange traded products or accessible securities

We confirm that we do not propose to require divestment of pre-1 January 2018 platform investments following the implementation of the proposed set of changes. This will be clarified in the final instrument.

We confirm that dispute resolution requirements apply to a registered managed investment scheme that is exchange traded. This requirement is not impacted by the changes proposed in CP 264.

We also confirm that the proposed changes only apply to financial products other than accessible securities, this will also be clarified in the final instrument.

Operator continues to facilitate resolution of disputes with retail clients

Underlying product issuers can receive information in relation to a retail client's investment from the operator who is obliged to facilitate the resolution of the complaint.[1]

In the circumstances, this may continue to involve providing details of an investor's investment to a retail client or directly to an underlying issuer (see paragraph 58 of RG 148). The changes proposed in CP 264 do not impact upon existing privacy requirements or other related obligations. Platform operators and underlying product issuers will still need to satisfy themselves that their individual obligations continue to be met in this regard.

Alternative delivery means

We have not included a review of the provisions for electronic communication in the scope of this set of proposed changes as we have not identified a sufficient basis to broaden the scope of our work.

Before proceeding with an amendment to the legislative instrument, we would need further information to demonstrate that there was an issue of wide concern among platform operators.

We consider that there should be reduced difficulties in obtaining a client's consent to provide information electronically given that platforms are designed to enable client instructions about investment holdings to be effected. This is consistent with an expectation of active involvement and communication with the platform by the client (or their agent).

---

[1] See section 912AD(41) in draft [CO 13/763], section 1013DAB(18) in draft [CO 13/762] and section 912AE(9) in *ASIC Corporations (Nominee and Custody Services) Instrument 2016/XX*).

Other policy issues

Following on from our implementation of the changes proposed in CP 264 (incorporating some updates responding to feedback received during consultation), we intend to monitor this policy area. We may consider implementing further changes at a later date to ensure that there is a level playing field between direct investors and investors investing through a platform or a nominee and custody service (including requirements relating to financial product issuers' compensation arrangements and periodic statement fee and cost disclosure).

We thank you for your submissions on this topic to date and for your general engagement on this matter. We have found the feedback received from consultation was helpful in developing and finalising the amendments to this area of policy.

Yours sincerely

Gerard Fitzpatrick
Senior Executive Leader, Investment Managers and Superannuation